

CLOSING MEMORANDUM

\$47,625,000  
CITY OF MODESTO  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

EXTENSION OF LETTER OF CREDIT

This memorandum will summarize the procedures to be followed in satisfying the conditions precedent to the extension of a letter of credit for the City of Modesto, California (the “City”) of its Water Refunding Revenue Certificates of Participation, 2008 Series A (the “Certificates”).

CLOSING SCHEDULE

Wednesday, June 4, 2014	Via Sidley Austin’s Firmex Virtual Closing Site	Pre-Closing
Thursday, June 5, 2014	Via Sidley Austin’s Firmex Virtual Closing Site	Closing

\$47,625,000  
CITY OF MODESTO  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

MEMORANDUM OF LEGAL PAPERS

to be included in transcripts  
relating to the above-mentioned Certificates

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Closing: Thursday, June 5, 2014

Complete transcripts are to be prepared for distribution to the following parties:

Modesto Public Financing Authority (the “Authority”)

\*City of Modesto (the “City”)

The Bank of New York Mellon Trust Company, N.A. (the “Trustee”)

\*Sidley Austin LLP (“Bond Counsel” or “BC”)

\*JPMorgan Chase Bank, National Association (the “Bank”)

McGuireWoods LLP (“Bank Counsel”)

Public Financial Management, Inc. (“PFM”)

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\* We will be preparing transcripts on CD-ROM for all parties. In addition to CD-ROM copies, parties indicated above with an asterisk (\*) will be receiving one paper copy of the transcript with original signatures of the primary documents.

**Pre-Closing**

The Pre-Closing will be held on Wednesday, June 4, 2014, via Sidley's Virtual Closing Site.

The parties indicated below will deliver five (5) originals of each of the respective documents so indicated below. The documents will be executed in advance of the Closing by the respective parties thereto and delivered no later than the Pre-Closing. Unless otherwise indicated, the documents will be dated as of the date of Closing. All such deliveries will be deemed to have been made in escrow until final delivery at the Closing has been made.

Responsibility for preparing or assembling the documents is indicated in parentheses.

**Closing**

In connection with the extension of the letter of credit for the Bonds, a closing email will be distributed to the financing team by Sidley indicating the transaction is closed.

\$47,625,000  
CITY OF MODESTO  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

DOCUMENTS AND INSTRUMENTS

The following documents and instruments are to be delivered to the appropriate party or parties at the Pre-Closing.

	<u>Index Number</u>
I. <u>BASIC DOCUMENTS</u>	
1. Certified copy of the AMENDED AND RESTATED TRUST AGREEMENT, dated as of May 1, 2008 and amended and restated July 14, 2011, by and between Trustee and the Authority. (BC)	1
2. Certified copy of the REIMBURSEMENT AGREEMENT, dated as of July 1, 2011, between the City and the Bank. (BC)	2
3. Executed copy of the FIRST AMENDMENT TO THE REIMBURSEMENT AGREEMENT, dated as of June 5, 2014, between the City and the Bank. (Bank Counsel)	3
4. Executed copy of the FEE LETTER, dated June 5, 2014, between the City and the Bank. (Bank Counsel)	4
5. SPECIMEN COPY OF NOTICE OF EXTENSION OF LETTER OF CREDIT. (Bank Counsel)	5
6. OFFICIAL STATEMENT SUPPLEMENT NO. 2, dated June 5, 2014, to Official Statement dated May 29, 2008 as supplemented by the Official Statement Supplement No. 1, dated July 5, 2011, and as amended by Amendment to Official Statement Supplement No. 1, dated July 5, 201. (BC)	6

II. AUTHORIZATION OF THE FINANCING

A. By the City

1. Certified copy of Resolution No. 2014-213 of the City Council of the City, adopted June 3, 2014, entitled “A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF MODESTO RELATING TO WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION, 2008 SERIES A; APPROVING THE FORMS OF AND AUTHORIZING THE EXECUTION AND DELIVERY OF A FIRST AMENDMENT TO REIMBURSEMENT AGREEMENT AND FEE LETTER AND APPROVING THE FORM OF AND AUTHORIZING THE DISTRIBUTION OF A SUPPLEMENT TO AN OFFICIAL STATEMENT IN CONNECTION THEREWITH; AND AUTHORIZING CERTAIN OTHER RELATED ACTIONS.” (BC) 7

B. By the Authority

1. Certified copy of Resolution No. \_\_\_-2014 of the Commission of the Authority, adopted June 3, 2014, entitled “A RESOLUTION OF THE MODESTO PUBLIC FINANCING AUTHORITY RELATING TO WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION, 2008 SERIES A; APPROVING THE FORM OF AND AUTHORIZING THE DISTRIBUTION OF A SUPPLEMENT TO AN OFFICIAL STATEMENT IN CONNECTION THEREWITH; AND AUTHORIZING CERTAIN OTHER RELATED ACTIONS.” (BC) 8

III. CLOSING DOCUMENTS

A. Documents Relating to the City

1. CLOSING, SIGNATURE AND INCUMBENCY CERTIFICATE OF THE CITY. (BC) 9

B. Documents Relating to the Authority

1. CLOSING, SIGNATURE AND INCUMBENCY CERTIFICATE OF THE AUTHORITY. (BC) 10

IV. NOTICE

1. NOTICE of Extension of Letter of Credit to Notice Parties, dated June 5, 2014, pursuant to Sections 3.11(f), 11.07(b)(iii) and 11.07(c) of the Amended and Restated Trust Agreement. (Trustee) 11

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Number

V. MISCELLANEOUS

1. DISTRIBUTION LIST. (BC)

12

\$47,625,000  
CITY OF MODESTO  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

CERTIFIED COPY OF AMENDED AND RESTATED TRUST AGREEMENT

The undersigned authorized representative of the Modesto Public Financing Authority (the "Authority"), in connection with the City of Modesto Water Revenue Certificates of Participation, 2008 Series A (the "Certificates") DOES HEREBY CERTIFY that attached hereto is a full, true and correct copy of the AMENDED AND RESTATED TRUST AGREEMENT, dated as of May 1, 2008, as amended and restated as of July 14, 2011, between the Authority and The Bank of New York Mellon Trust Company, N.A., and does hereby further certify that such agreement has not been further amended, modified or rescinded since July 14, 2011, and is now in full force and effect.

[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK.]

IN WITNESS WHEREOF, I have hereunto set my hand this 5<sup>th</sup> day of June, 2014.

MODESTO PUBLIC FINANACING  
AUTHORITY

By:



A handwritten signature in cursive script, appearing to read 'Stephanie Lopez', is written over a horizontal line.

Stephanie Lopez  
Secretary

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AMENDED AND RESTATED TRUST AGREEMENT

between the

MODESTO PUBLIC FINANCING AUTHORITY

and

THE BANK OF NEW YORK MELLON TRUST COMPANY, N.A.,  
as Trustee

Dated as of May 1, 2008

and

Amended and Restated July 14, 2011

Relating to

\$47,625,000

WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

EVIDENCING AND REPRESENTING PROPORTIONATE INTERESTS  
OF THE OWNERS THEREOF IN 2008 PAYMENTS TO BE MADE BY THE  
CITY OF MODESTO  
TO THE  
MODESTO PUBLIC FINANCING AUTHORITY

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## TRUST AGREEMENT

THIS AMENDED AND RESTATED TRUST AGREEMENT, dated July 14, 2011 (the "Trust Agreement"), amending and restating the Trust Agreement dated as of May 1, 2008 (the "Original Trust Agreement"), is by and between the MODESTO PUBLIC FINANCING AUTHORITY, a joint exercise of powers authority duly organized and existing under and by virtue of the laws of the State of California (the "Authority"), and THE BANK OF NEW YORK MELLON TRUST COMPANY, N.A., a national banking association duly organized and existing under and by virtue of the laws of the United States of America (the "Trustee");

### WITNESSETH:

WHEREAS, the Authority is a joint exercise of powers authority duly organized and existing under and pursuant to the Joint Exercise of Powers Act (being Sections 6500 et seq. of the Government Code of the State of California) (the "Act") and a Joint Exercise of Powers Agreement (the "JPA Agreement"), dated as of December 1, 1989, by and between the City of Modesto (the "City") and the Industrial Development Authority of the City of Modesto; and

WHEREAS, the Act and the JPA Agreement authorize and empower the Authority to assist the City in acquiring and financing and refinancing certain additions, betterments, extensions and improvements to the water utility system of the City; and

WHEREAS, the Authority and the City have heretofore entered into a Master Installment Purchase Contract, dated as of November 1, 1997 (the "Master Contract"), as supplemented by the 1997 Supplemental Installment Purchase Contract, dated as of November 1, 1997 (the "1997 Supplemental Contract"), under and pursuant to which the Authority agreed to assist the City by refinancing certain additions, betterments, extensions and improvements to the water utility system of the City (the "1997 Project" as defined therein); and

WHEREAS, the City is obligated to make certain payments to the Authority under the 1997 Supplemental Contract (the "1997 Payments"), and all rights to receive such payments have been assigned by the Authority to State Street Bank and Trust Company of California, N.A., as succeeded by The Bank of New York Mellon Trust Company, N.A. (formerly known as The Bank of New York Trust Company N. A.), as successor trustee for the owners of the Refunding Revenue Certificates of Participation (1997 Water Utility Refinancing Project); and

WHEREAS, the Authority and the City have heretofore entered into the 2006 Supplemental Installment Purchase Contract, dated as of November 1, 2006 (the "2006 Supplemental Contract"), under and pursuant to which the Authority agreed to assist the City by financing certain additions, betterments, extensions and improvements to the water utility system of the City (the "2006 Project" as defined therein); and

WHEREAS, the City is obligated to make certain payments to the Authority under the 2006 Supplemental Contract (the "2006 Payments"), and all rights to receive such payments have been assigned by the Authority to the Trustee, as trustee in relation to the Water Revenue Certificates of Participation 2006 Series A; and

WHEREAS, the Authority and the City have heretofore entered into the 2008 Supplemental Installment Purchase Contract dated as of May 1, 2008 (the "2008 Supplemental Contract" and together with the Master Contract, the 1997 Supplemental Contract, and the 2006 Supplemental Contract, the "Contract"), under and pursuant to which the Authority agreed to assist the City in refinancing the 2006 Project as described in the 2008 Supplemental Contract (the "2008 Project" as defined therein); and

WHEREAS, the City is obligated to make certain payments to the Authority under the 2008 Supplemental Contract (the "2008 Payments"), and all rights to receive such payments are being assigned by the Authority to the Trustee in relation to the Water Refunding Revenue Certificates of Participation, 2008 Series A (the "2008 Certificates"); and

WHEREAS, in consideration of such assignment of the 2008 Payments and the execution and entering into of the Trust Agreement, the Trustee has agreed to execute and deliver the 2008 Certificates in an aggregate principal amount equal to the aggregate principal amount of such 2008 Payments, each representing a proportionate interest in such 2008 Payments; and

WHEREAS, the Authority has determined that all acts, conditions and things required by law to exist, to have happened and to have been performed precedent to and in connection with the execution and delivery of this Trust Agreement do exist, have happened and have been performed in regular and due time, form and manner as required by law, and the execution and delivery of this Trust Agreement have been in all respects duly authorized; and

WHEREAS, in order to support the payment of the principal and Purchase Price of, and interest on, the 2008 Certificates, the Authority, the City and Bank of America, N.A. (the "Initial Liquidity Facility Provider") entered into Standby Certificate Purchase Agreement, dated as of May 1, 2008 (the "Initial Liquidity Facility"); and

WHEREAS, as a result of the expiration of the Initial Liquidity Facility, the Authority and the City have elected to replace the Initial Credit Facility with an Alternate Liquidity Facility in the form of a direct-pay letter of credit (the "Replacement Liquidity Facility") from JPMorgan Chase Bank, N.A. (the "Bank"), effective on the Substitution Date (as defined herein), thereby triggering a mandatory tender of the 2008 Certificates in whole on the Substitution Date for the Initial Liquidity Facility; and

WHEREAS, the Replacement Liquidity Facility constitutes an Alternate Liquidity Facility for purposes of the Contract and this Trust Agreement; and

WHEREAS, the Original Trust Agreement is being amended and restated as of the Substitution Date pursuant to this Trust Agreement, in order to add provisions relating to the Replacement Liquidity Facility; and

WHEREAS, Section 7.01 of the Original Trust Agreement permits any amendments of the Original Trust Agreement, with the prior written consent of the 2008 Certificate Insurer, but without the consent of the Owners, if effective upon the remarketing of the 2008 Certificates following mandatory tender of the 2008 Certificates; and

WHEREAS, this Trust Agreement shall be effective on the Substitution Date;

NOW, THEREFORE, in consideration of the premises and the mutual agreements and covenants herein, and for other valuable consideration, the parties hereto do hereby covenant and agree, as follows:

## ARTICLE I

### DEFINITIONS; EQUAL SECURITY

Section 1.01. Definitions. Unless the context otherwise requires, the terms defined in this Section shall for all purposes hereof and of any Supplemental Trust Agreement and of any certificate, opinion, request or other document herein or therein mentioned have the meanings herein specified unless the context or use clearly indicates another or different meaning or intent:

“Alternate Liquidity Facility” means a letter of credit (including, without limitation, the Replacement Liquidity Facility), line of credit, surety bond, standby purchase agreement or other security or liquidity instrument, as the case may be, approved by the 2008 Certificate Insurer and issued in accordance with the terms hereof with respect to the 2008 Certificates as a replacement or substitute for any Liquidity Facility then in effect.

“Alternate Rate” means, on any Rate Determination Date, for the 2008 Certificates in a Daily Mode, a Weekly Mode, a Flexible Rate Mode or a Term Rate Mode, a rate per annum equal to (a) the SIFMA Municipal Swap Index (the “SIFMA Rate”) most recently available as of the date of determination, or (b) if such index is no longer available, or if the SIFMA Rate is no longer published, the S&P Weekly High Grade Index (formerly the J.J. Kenny Index), or (c) if neither the SIFMA Rate nor the S&P Weekly High Grade Index is published, the index determined to equal the prevailing rate determined by the Remarketing Agent for tax-exempt state and local government bonds meeting criteria determined in good faith by the Remarketing Agent to be comparable under the circumstances to the criteria used by the Securities Industry and Financial Markets Association (“SIFMA”) to determine the SIFMA Rate just prior to when the SIFMA stopped publishing the SIFMA Rate. If there is no Remarketing Agent for the 2008 Certificates, if the Remarketing Agent fails to make any such determination or if the Remarketing Agent has suspended its remarketing efforts in accordance with the Remarketing Agreement, then a financial advisor, investment banker or other qualified party shall make such determination at the expense of the Authority.

“Assigned Rights to Interest” means those rights to receive payment from the Authority pursuant to the Trust Agreement of any interest on 2008 Certificates with respect to which, pursuant to Section 10.05 hereof, the Bank or other Credit enhancement Provider, to the extent it has paid such interest from a drawing under the Replacement Liquidity Facility or other Credit Enhancement, has become subrogated and an assignee and the owner.

“Authority” means the Modesto Public Financing Authority, a joint exercise of powers authority duly organized and existing under and by virtue of the laws of the State.

“Authority Account” means the account by that name established within the 2008 Purchase Fund pursuant to Section 3.09(c) hereof.

“Authorized Denominations” means: (i) with respect to 2008 Certificates in a Daily Mode or Weekly Mode, \$100,000 and any integral multiple of \$5,000 in excess thereof; (ii) with respect to 2008 Certificates in a Flexible Mode, \$100,000 and any integral multiple of \$1,000 in excess thereof; and (iii) with respect to 2008 Certificates in a Term Rate Mode or Fixed Rate Mode, \$5,000 and any integral multiple thereof.

“Automatic Termination Event” means an event of default set forth in a Reimbursement Agreement between the Authority and a Liquidity Facility Provider which would result in the immediate termination of the Liquidity Facility provided pursuant to such Reimbursement Agreement prior to its stated expiration date without prior notice from the Liquidity Facility Provider to the Trustee.

“Available Amount” means the amount available under a Credit Enhancement or Liquidity Facility, as applicable, to pay the principal and interest with respect to the 2008 Certificates or the Purchase Price with respect to the 2008 Certificates, as applicable.

“Bank” means JPMorgan Chase Bank, N.A., and its successors or assigns.

“Basic Certificate Rate” shall mean the rate of interest applicable to 2008 Certificates that are not Liquidity Provider Certificates.

“Beneficial Owner” means, so long as the 2008 Certificates are held in the Book-Entry System, any Person who acquires a beneficial ownership interest in a 2008 Certificate held by the Securities Depository, and during any period the 2008 Certificates are not held in the Book-Entry System, Beneficial Owner shall mean the registered owner for purposes of this Trust Agreement.

“Book-Entry System” means a system under which physical certificates in fully registered form are registered only in the name of a Securities Depository or its nominee.

“Business Day” means any day other than (i) a Saturday or Sunday or (ii) a day on which the Trustee or applicable Remarketing Agent are required or authorized to be closed or (iii) a day on which the office of the applicable Credit Enhancement Provider or applicable Liquidity Facility Provider at which draws or advances will be paid is required or authorized to be closed or (iv) a day on which The New York Stock Exchange is closed.

“Cancellation Date” means the date on which the 2008 Certificate Insurance Policy is cancelled, which date shall be the seventh Business Day following receipt by the Trustee of written notice from (i) the Bank specifying that the 2008 Certificate Insurance Policy is to be cancelled in accordance with the terms of the Reimbursement Agreement between the Bank and the City or (ii) the Authority with the consent of the Bank specifying that the 2008 Certificate Insurance Policy is to be replaced with a substitute Credit Enhancement.

“Certificate of the Authority” means an instrument in writing signed by the Auditor and Treasurer of the Authority or by any other officer of the Authority duly authorized by the Authority for that purpose.

“Certificate Payment Date” means, with respect to any 2008 Certificate, subject to Section 2.03(a) hereof, the Certificate Payment Date designated therein, which is the October 1 on which or, in the case of 2008 Certificates subject to mandatory sinking fund prepayment, by which, the principal component of the final 2008 Payment evidenced and represented thereby shall become due and payable.

“City” means the City of Modesto, a charter city and municipal corporation, duly organized and existing under and by virtue of the Constitution and laws of the State.

“Code” means the Internal Revenue Code of 1986, and the regulations issued thereunder, as the same may be amended from time to time, and any successor provisions of law. Reference to a particular section of the Code shall be deemed to be a reference to any successor to any such section.

“Contract” means that certain Master Contract, as supplemented by the 1997 Supplemental Contract, the 2006 Supplemental Contract, and the 2008 Supplemental Contract, and as otherwise amended or supplemented from time to time.

“Control Event” means that one or more of the circumstances referred to in Section 10.03 hereof has occurred as a result of which all references herein to the 2008 Certificate Insurer and all provisions herein for the benefit of the 2008 Certificate Insurer are of no effect (other than rights of the 2008 Certificate Insurer derived through subrogation and assignment).

“Corporate Trust Office” means the corporate trust office of the Trustee in San Francisco, California, or such other office as may be specified by written notice from the Trustee to the Authority.

“Costs of Issuance” means all items of expense directly or indirectly payable by or reimbursable to the City or the Authority and related to the authorization, execution and delivery of the Contract and the Trust Agreement and the execution, sale and delivery of the 2008 Certificates, including, but not limited to, costs of preparation and reproduction of documents, costs of rating agencies and costs to provide information required by rating agencies, filing and recording fees, initial fees and charges of the Trustee and its counsel, legal fees and charges, fees and disbursements of consultants and professionals, fees and expenses of the underwriter, fees and charges for preparation, execution and safekeeping of the 2008 Certificates, fees and expenses of the Liquidity Facility Provider, fees of the Authority and any other cost, charge or fee in connection with the original execution and delivery of the 2008 Certificates.

“Costs of Issuance Fund” means the fund by that name established pursuant to Section 4.05 hereof.

“Credit Enhancement” means the 2008 Certificate Insurance Policy issued by the 2008 Certificate Insurer. In case a letter of credit is provided as a Liquidity Facility, such letter of credit will also be considered a Credit Enhancement and its issuer, a Credit Enhancement Provider, if such letter of credit is a direct-pay letter of credit that provides for the payment of the principal of, and interest with respect to, the 2008 Certificates as they become due.

“Credit Enhancement Provider” means, with respect to a Credit Enhancement, the issuer or provider thereof.

“Credit Enhancement Provider Failure” means: (i) a failure of a Credit Enhancement Provider to pay any amount due under its Credit Enhancement; (ii) the filing or commencement of any bankruptcy or insolvency proceedings by or against a Credit Enhancement Provider, provided such proceeding has not been dismissed within 60 consecutive days; (iii) the declaration by a Credit Enhancement Provider of a moratorium on the payment of its unsecured debt obligations; or (iv) the written repudiation by a Credit Enhancement Provider of its Credit Enhancement.

“Current Mode” shall have the meaning specified in Section 2.18(a)(i) hereof.

“Daily Mode” means the Mode during which the 2008 Certificates evidence interest at the Daily Rate.

“Daily Rate” means the per annum interest rate with respect to the 2008 Certificates in the Daily Mode determined pursuant to Section 2.15(a) hereof.

“Daily Rate Period” means the period during which the 2008 Certificates in the Daily Mode shall evidence interest at a Daily Rate, which shall be from the Business Day upon which a Daily Rate is set to but not including the next succeeding Business Day.

“Defaulted Interest” means interest evidenced by any 2008 Certificate that is payable but not duly paid on the date due.

“Delayed Remarketing Period” shall have the meaning specified in Section 3.10(b) hereof.

“Delivery Date” means May 30, 2008.

“DTC” means The Depository Trust Company, New York, New York, and its successors and assigns.

“Electronic” means telecopy, facsimile transmission, e-mail transmission or other similar electronic means of communication providing evidence of transmission, including a telephonic communication confirmed by any other method set forth in this definition.

“Eligible Account” means an account that is either (i) maintained with a federal or state-chartered depository institution or trust company that has a Standard & Poor’s short-term debt rating of at least ‘A-2’ (or, if no short-term debt rating, a long-term debt rating of ‘BBB+); or (ii) maintained with the corporate trust department of a federal depository institution or state-chartered depository institution subject to regulations regarding fiduciary funds on deposit similar to Title 12 of the U.S. Code of Federal Regulation Section 9.10(b), which, in either case, has corporate trust powers and is acting in its fiduciary capacity.

“Expiration Date” means the stated expiration date of a Liquidity Facility, as it may be extended from time to time as provided in such Liquidity Facility, or any earlier date on which

such Liquidity Facility shall terminate at the direction of the Authority, expire or be cancelled (other than the date on which a Liquidity Facility shall terminate as a result of an Automatic Termination Event or an event of default under the Reimbursement Agreement entered into in connection with such Liquidity Facility).

“Event of Default” means an event described in Section 8.01 hereof.

“Favorable Opinion of Special Counsel” means, with respect to any action the occurrence of which requires such an opinion, an Opinion of Special Counsel, addressed to the Trustee, to the effect that the action proposed to be taken will not, in and of itself, adversely affect any exclusion from gross income of interest with respect to the 2008 Certificates.

“Federal Securities” shall have the meaning ascribed thereto in the Contract.

“Fiscal Year” means the period beginning on July 1 of each year and ending on the next succeeding June 30, or any other annual accounting period hereafter selected and designated by the Authority as its Fiscal Year.

“Fixed Rate” means the per annum interest rate or interest rates evidenced by the 2008 Certificates in a Fixed Rate Mode determined pursuant to Section 2.16(b) hereof.

“Fixed Rate Certificates” means the 2008 Certificates in a Fixed Rate Mode.

“Fixed Rate Mode” means the Mode during which the 2008 Certificates evidence interest at a Fixed Rate.

“Fixed Rate Period” means, with respect to 2008 Certificates converted to the Fixed Rate Mode, the period from the Mode Change Date upon which the 2008 Certificates were converted to a Fixed Rate Mode to but not including the Maturity Date.

“Fixed Rate Remarketing Agent” means, an investment banking firm or firms selected by the Authority that has or have entered into a written agreement with the Authority to remarket or purchase and remarket the 2008 Certificates upon their being converted to a Fixed Rate Mode in accordance with the terms and provisions set forth herein.

“Flexible Mode” means the Mode during which the 2008 Certificates evidence interest at Flexible Rates.

“Flexible Rate” means, with respect to the 2008 Certificates in a Flexible Mode, the per annum interest rate determined for the 2008 Certificate pursuant to Section 2.14 hereof.

“Flexible Rate Certificates” means the 2008 Certificates in a Flexible Mode.

“Flexible Rate Period” means, with respect to the 2008 Certificates in a Flexible Mode, the period of from 1 to 397 calendar days (which Flexible Rate Period must end on a day preceding a Business Day) during which a Flexible Rate Certificate shall evidence interest at a Flexible Rate, as established by the Remarketing Agent pursuant to Section 2.14 hereof.

“Improvement Fund” means the fund by that name established pursuant to Section 2.02 of the Master Contract.

“Independent Certified Public Accountant” means any certified public accountant or firm of such accountants duly licensed and entitled to practice and practicing as such under the laws of the State, appointed and paid by the Authority, and who, or each of whom—

(1) is in fact independent according to the Statement of Auditing Standards No. 1 and not under the domination of the Authority;

(2) does not have a substantial financial interest, direct or indirect, in the operations of the Authority; and

(3) is not connected with the Authority as a member, officer or employee of the Authority, but who may be regularly retained to audit the accounting records of and make reports thereon to the Authority.

“Information Services” means Financial Information, Inc.’s “Daily Called Bond Service,” 30 Montgomery Street, 10th Floor, Jersey City, New Jersey 07302, Attention: Editor; FIS/Mergent, Inc., 5250 77 Center Drive, Suite 150, Charlotte, North Carolina 28217, Attn: Call Notification; Standard & Poor’s Securities Evaluation, Inc., 55 Water Street, 45th Floor, New York, New York 10041, Attention: Notification Department; Xcitek, 5 Hanover Square, New York, New York 10004; and, in accordance with then current guidelines of the Securities and Exchange Commission, such other addresses and/or such other services providing information with respect to the redemption of bonds or the prepayment of certificates of participation as the Authority may designate in a Certificate of the Authority filed with the Trustee.

“Initial Liquidity Facility” means the Standby Certificate Purchase Agreement, dated as of May 1, 2008, between the Authority and the Initial Liquidity Facility Provider.

“Initial Liquidity Facility Provider” means Bank of America, N.A.

“Insurer Indenture Event of Default” means and includes the occurrence of one or more of the following events:

(a) any principal or interest evidenced by the 2008 Certificates (including Liquidity Provider Certificates or Subrogated Certificates) is not paid by the 2008 Certificate Insurer when, as, and in the amounts required to be paid pursuant to the terms of the 2008 Certificate Insurance Policy; or

(b) (i) any material provision of the 2008 Certificate Insurance Policy relating to the obligation of the 2008 Certificate Insurer to make payments of principal and interest thereunder at any time for any reason ceases to be valid and binding on the 2008 Certificate Insurer in accordance with the terms of the 2008 Certificate Insurance Policy or the New York Department of Insurance, or a court or other governmental authority of appropriate jurisdiction shall find or rule or shall enter an order, judgment or decree that the 2008 Certificate Insurance Policy is not valid and binding on the 2008 Certificate Insurer or (ii) the 2008 Certificate Insurer shall (A) claim in writing that the 2008

Certificate Insurance Policy is not valid and binding on the 2008 Certificate Insurer, (B) repudiate the 2008 Certificate Insurer's obligations under the 2008 Certificate Insurance Policy or (C) initiate legal proceedings seeking an adjudication that the 2008 Certificate Insurance Policy, or any material provision thereof regarding the payment of principal or interest on 2008 Certificates (including Liquidity Provider Certificates) is not valid and binding on the 2008 Certificate Insurer; or

(c) a proceeding is instituted in a court having jurisdiction in the premises seeking an order for relief, rehabilitation, reorganization, conservation, liquidation or dissolution in respect to the 2008 Certificate Insurer or for any substantial part of its property under any applicable bankruptcy, insolvency or other similar law now or hereafter in effect, or for the appointment of a receiver, liquidator, assignee, custodian, trustee or sequestrator (or other similar official) and such proceeding shall not have been dismissed within sixty (60) days or such court enters an order granting the relief sought in such proceeding; or the New York Department of Insurance shall declare a moratorium on the payment of the 2008 Certificate Insurer's debts, or the 2008 Certificate Insurer shall commence a voluntary case under any applicable bankruptcy, insolvency or other similar law now or hereafter in effect, shall consent to the entry of an order for relief in an involuntary case under any such law or shall consent to the appointment of or taking possession by a receiver, liquidator, assignee, trustee, custodian or sequestrator (or other similar official) of the 2008 Certificate Insurer or for any substantial part of its property, or shall make a general assignment for the benefit of creditors, or shall fail generally to pay its debts (provided for purposes of this definition, "debts" shall not include any obligation of the 2008 Certificate Insurer under any insurance policy or surety bond) as they become due, or an order for rehabilitation, liquidation or dissolution of the 2008 Certificate Insurer shall be issued.

"Interest Accrual Period" means the period during which the 2008 Certificates accrue interest payable on the next Interest Payment Date applicable thereto. Each Interest Accrual Period shall commence on (and include) the last Interest Payment Date to which interest has been paid (or, if no interest has been paid, from the date of original authentication and delivery of the 2008 Certificates) to, but not including, the Interest Payment Date on which interest is to be paid. If, at the time of authentication of any 2008 Certificate, interest is in default or overdue with respect to the 2008 Certificates, such 2008 Certificate shall evidence interest from the date to which interest has previously been paid in full or made available for payment in full with respect to the 2008 Certificates.

"Interest Payment Date" means each date on which interest is to be paid and is: (i) with respect to the 2008 Certificates in a Daily Mode or a Weekly Mode, the first Business Day of each month; (ii) with respect to the 2008 Certificates in a Flexible Mode, each Mandatory Purchase Date applicable thereto; (iii) with respect to the 2008 Certificates in a Fixed Rate Mode or a Term Rate Mode, the first day of April or October, which is at least 3 months after the month in which such Long-Term Mode takes effect, and the first day of each April and October thereafter or, upon the receipt by the Trustee of a Favorable Opinion of Special Counsel, any other six-month interval chosen by the Authority (beginning with the first such day which is at least three months after the Mode Change Date) and, with respect to a Term Rate Mode, the final day of the current Interest Period if other than a regular six-month interval; (iv) (without

duplication as to any Interest Payment Date listed above) any Mode Change Date, other than a change between a Daily Mode and a Weekly Mode, and each Maturity Date; and (v) with respect to any Liquidity Provider Certificates, the day set forth in the applicable Reimbursement Agreement.

“Interest Period” means, for the 2008 Certificates in a particular Mode, the period of time that the 2008 Certificates evidence interest at the rate (per annum) which becomes effective at the beginning of such period, and shall include, a Daily Rate Period, a Weekly Rate Period, a Flexible Rate Period, a Term Rate Period, and a Fixed Rate Period. Notwithstanding the preceding sentence, regardless of Mode, so long as any 2008 Certificate is a Liquidity Provider Certificate, the Interest Period shall be determined in accordance with the applicable Liquidity Facility or the applicable Reimbursement Agreement.

“Liquidity Facility” means, as of any time, the Initial Liquidity Facility, the Replacement Liquidity Facility or an Alternate Liquidity Facility, as applicable, which provides for the payment of the purchase price of the 2008 Certificates upon the tender thereof in the event remarketing proceeds are insufficient therefor.

“Liquidity Facility Account” means an Eligible Account by that name established within the 2008 Purchase Fund pursuant to Section 3.09(b) hereof and held in the name of the Trustee for the benefit of the Owners.

“Liquidity Facility Provider” means, with respect to the Replacement Liquidity Facility, the Bank, and with respect to any Alternate Liquidity Facility for the 2008 Certificates, a bank, insurance company, pension fund or other financial institution acceptable to the 2008 Certificate Insurer, including the Bank.

“Liquidity Facility Provider Failure” means: (i) a failure of a Liquidity Facility Provider to pay a properly presented and conforming draw or request for advance; or (ii) the filing or commencement of any bankruptcy or insolvency proceedings by or against a Liquidity Facility Provider, provided such proceeding has not been dismissed within 60 consecutive days; or (iii) the declaration by a Liquidity Facility Provider of a moratorium on the payment of its unsecured debt obligations; or (iv) the written repudiation by a Liquidity Facility Provider of its Liquidity Facility.

“Liquidity Provider Certificates” means any 2008 Certificates purchased by a Liquidity Facility Provider with funds drawn on or advanced under the Liquidity Facility provided by such Liquidity Facility Provider.

“Long-Term Interest Period” means a Term Rate Period or a Fixed Rate Period.

“Long-Term Mode” means a Term Rate Mode or a Fixed Rate Mode.

“Mandatory Purchase Date” means: (i) with respect to a Flexible Rate Certificate, the first Business Day following the last day of each Flexible Rate Period with respect to such Flexible Rate Certificate; (ii) for the 2008 Certificates in a Term Rate Mode, the first Business Day following the last day of each Term Rate Period for such 2008 Certificates; (iii) any Mode Change Date; (iv) any Substitution Date; (v) the fifth Business Day prior to an Expiration Date;

(vi) the date specified by the Trustee following the occurrence of an event of default with respect to the Liquidity Facility or under the related Reimbursement Agreement which requires or gives the Liquidity Facility Provider the option to terminate the Liquidity Facility upon notice and requires that all Outstanding 2008 Certificates secured by such Liquidity Facility be tendered for purchase, which date shall be a Business Day not less than 7 days after the Trustee's receipt of notice of such event of default from the applicable Liquidity Facility Provider and in no event later than the Business Day preceding the termination date specified in the notice of event of default delivered to the Trustee by such Liquidity Facility Provider; (vii) for the 2008 Certificates in a Daily Mode or a Weekly Mode, any Business Day specified by the Authority in a notice delivered to the Trustee and consented to by the Liquidity Facility Provider, which Mandatory Purchase Date shall be not less than twenty (20) days after the Trustee's receipt of such notice from the Authority, and (viii) the Business Day prior to the Cancellation Date.

"Master Contract" means that certain Master Installment Purchase Contract, executed and entered into as a November 1, 1997, by and between the City and the Authority, as the same may be amended or supplemented from time to time.

"Maturity Date" means, with respect to the 2008 Certificates, the maturity date specified for the 2008 Certificates in Section 2.02 hereof or, if Serial Certificates or more than one Term Certificates are established for the 2008 Certificates pursuant to Section 2.18(d) hereof upon a change of the 2008 Certificates to a Fixed Rate Mode, the maturity dates established for such Serial Certificates or Term Certificates.

"Maximum Rate" or "Maximum Interest Rate" means, with respect to all 2008 Certificates other than Liquidity Provider Certificates, a rate of interest of 12% per annum, and with respect to Liquidity Provider Certificates, such rate not greater than 18% as is provided for in the applicable Liquidity Facility; provided, however, that such rate shall not in any event exceed the highest rate then permitted by law.

"Mode" means, as the context may require, the Daily Mode, the Weekly Mode, the Flexible Mode, the Term Rate Mode, or the Fixed Rate Mode.

"Mode Change Date" means with respect to the 2008 Certificates in a particular Mode, the day on which another Mode for the 2008 Certificates begins.

"Mode Change Notice" means the notice from the Authority to the other Notice Parties of the intention of the Authority to change the Mode with respect to the 2008 Certificates.

"Moody's" means Moody's Investors Service Inc., a corporation duly organized and existing under and by virtue of the laws of the State of Delaware, and its successors or assigns, except that if such corporation shall be dissolved or liquidated or shall no longer perform the services of a municipal securities rating agency, then "Moody's" shall be deemed to refer to any other nationally recognized municipal securities rating agency selected by the Authority.

"New Mode" shall have the meaning specified in Section 2.18(a)(i) hereof.

“1997 Certificates” means the \$25,585,000 Refunding Revenue Certificates of Participation (1997 Water Utility System Refinancing Project), evidencing and representing and proportionate interests of the owners thereof in the 1997 Payments to be made by the City.

“1997 Supplemental Contract” means the 1997 Supplemental Installment Purchase Contract, executed and entered into as of November 1, 1997, by and between the City and the Authority, supplementing the Master Contract.

“1997 Payments” means the installment payments required to be made by the City to the Authority under and pursuant to the 1997 Supplemental Contract.

“1997 Trust Agreement” means that certain Trust Agreement, dated as of November 1, 1997, by and between the Authority and State Street Bank and Trust Company, N.A., which has been succeeded by The Bank of New York Trust Company, N.A., as trustee, pursuant to which there was executed and delivered the 1997 Certificates.

“Notice Parties” means the Authority, the City, the Trustee, the Credit Enhancement Provider, if any, the Liquidity Facility Provider, if any, the Remarketing Agent, if any, and the Fixed Rate Remarketing Agent, if any.

“Opinion of Counsel” means a written opinion of counsel of recognized standing in the field of law being addressed in such opinion retained the Authority.

“Outstanding,” when used as of any particular time with reference to 2008 Certificates, means (subject to the provisions of Section 7.02 hereof) all 2008 Certificates except

- (1) 2008 Certificates theretofore cancelled by the Trustee or surrendered to the Trustee for cancellation;
- (2) 2008 Certificates paid or deemed to have been paid within the meaning of Section 9.01 hereof; and
- (3) 2008 Certificates in lieu of or in substitution for which other 2008 Certificates shall have been executed and delivered by the Trustee pursuant hereto.

“Owner” means any person who shall be the registered owner of any Outstanding 2008 Certificate.

“Parity Reserve Fund” means the fund by that name continued pursuant to Section 4.04 hereof.

“Parity Reserve Fund Obligation” means the 1997 Certificates, the 2008 Certificates and any other obligations hereafter issued in connection with a Supplemental Contract.

“Payment Agreement Payments” has the meaning given such term in the Master Contract.

“Payment Agreement Receipts” has the meaning given such term in the Master Contract.

“Permitted Investments” means any of the following obligations if and to the extent then permitted by law:

- (1) Federal Securities;
- (2) Obligations issued by the Resolution Funding Corporation and the Student Loan Marketing Association, or obligations, participations, or other instruments of or issued by, or fully guaranteed as to interest and principal by, the Government National Mortgage Association (excluding stripped mortgage backed securities which are valued at greater than par on the unpaid principal);
- (3) Bills of exchange or time drafts drawn on and accepted by a commercial bank (including the Trustee or any of its affiliates), otherwise known as bankers acceptances, which are eligible for purchase by the Federal Reserve System and which are drawn on any bank the short-term obligations of which are rated in the highest letter and numerical rating category as provided by Moody’s and by S&P; provided, that purchases of eligible bankers acceptances may not exceed 270 days’ maturity;
- (4) Commercial paper of “prime” quality of the highest ranking or of the highest letter and numerical rating category as provided by Moody’s and by S&P, which commercial paper is limited to issuing corporations that are organized and operating within the United States of America and that have total assets in excess of \$500,000,000 and that have an “A1” or higher rating for the issuer’s unsecured debentures, other than commercial paper, as provided by Moody’s and by S&P; provided, that purchases of eligible commercial paper may not exceed 180 days’ maturity nor represent more than 10% of the outstanding commercial paper of an issuing corporation;
- (5) Non-negotiable certificates of deposit issued by a state or national bank (including the Trustee or any of its affiliates) that have maturities of not more than 365 days or deposit accounts with a state or national bank and that are fully insured by the Federal Deposit Insurance Corporation or the short term obligations of which state or national bank are rated no lower that “A1” by Moody’s and “A+” by S&P;
- (6) Any repurchase agreement of any securities enumerated in subdivisions (1) and (2) with any state or national bank (including the Trustee or any of its affiliates) or government bond dealer reporting to, trading with, and recognized as a primary dealer by the Federal Reserve Bank of New York, which agreement is either (A) with any institution which has debt rated no lower than “A1” by Moody’s and “A+” by S&P or whose commercial paper is rated no lower than “P-1” by Moody’s and no lower than “A-1” by S&P; (B) with any corporation or other entity that falls under the jurisdiction of the Federal Bankruptcy Code; provided, that (a) the term of such repurchase agreement is less than one (1) year or due on demand; (b) the Trustee or a third party acting solely as agent for the Trustee has possession of the collateral; (c) the market value of the collateral (as determined at least once in every 14 days) exceeds the principal amount of the repurchase agreement plus accrued interest and the market value of the collateral is maintained at levels acceptable to Moody’s and to S&P; (d) failure to maintain the requisite collateral levels will require the Trustee to liquidate the collateral immediately;

and (e) the repurchase agreement securities are free and clear of any third-party lien or claim; or (C) with financial institutions insured by the Federal Deposit Insurance Corporation or any broker-dealer with "retail customers" which falls under the jurisdiction of the Securities Investors Protection Corporation; provided, that: (a) the market value of the collateral (as determined at least once in every 14 days) exceeds the principal amount of the repurchase agreement plus accrued interest and the market value of the collateral is maintained at levels acceptable to Moody's and to S&P; (b) the Trustee or a third party acting solely as agent for the Trustee has possession of the collateral; (c) the Trustee has a perfected first priority security interest in the collateral; (d) the collateral is free and clear of third-party liens and in the case of a Securities Investors Protection Corporation broker was not acquired pursuant to a repurchase agreement or reverse repurchase agreement; and (e) failure to maintain the requisite collateral percentage will require the Trustee to liquidate the collateral immediately;

(7) Certificates, notes, warrants, bonds or other evidence of indebtedness of the State or any local agencies therein which are rated in the highest short-term rating category or within one of the three highest long-term rating categories by Moody's and by S&P (excluding securities that do not have a fixed par value and/or whose terms do not promise a fixed dollar amount at maturity or call date);

(8) For amounts less than \$100,000, interest-bearing demand or time deposits (including certificates of deposit) in a nationally or state-chartered bank fully insured by the Federal Deposit Insurance Corporation, including the Trustee or any affiliate thereof, and of which an aggregate total of \$100,000 is not exceeded in any one financial institution;

(9) Investments in units of a money-market fund portfolio that is rated in the highest letter and numerical rating category by Moody's and by S&P (including funds for which the Trustee, its affiliates or subsidiaries provide investment advisory or other management services) and that is composed of obligations guaranteed by the full faith and credit of the United States of America or repurchase agreements collateralized by such obligations;

(10) A guaranteed investment contract with a financial institution or insurance company (or guaranteed by a financial institution or insurance company) which has at the date of execution thereof an outstanding issue of unsecured, uninsured and unguaranteed debt obligations or a claims paying ability rated within the two highest rating categories of any Rating Agency;

(11) Other investments approved in writing by the 2008 Certificate Insurer (or, if a Control Event has occurred, the Bank); and

(12) The Local Agency Investment Fund, the California Asset Management Program, or similar pooled fund operated by or on behalf of the State and which is authorized to accept investments by or on behalf of the Authority of the moneys held by the Trustee in any of the accounts or funds established pursuant hereto to the extent deposits and withdrawals may be made by the Trustee directly.

“Person” shall mean an individual, a corporation, an association, a joint venture, a partnership, a trust, an unincorporated organization or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

“Prepayment Date” means the date fixed for prepayment of any 2008 Certificate in any notice of prepayment given in accordance with the terms hereof.

“Purchase Date” means (i) for a 2008 Certificate in the Daily Mode or the Weekly Mode, any Business Day selected by the Beneficial Owner of said 2008 Certificate pursuant to the provisions of Section 3.01 hereof, and (ii) any Mandatory Purchase Date.

“Purchase Price” means an amount equal to the principal amount of the 2008 Certificates purchased on any Purchase Date, plus accrued interest to such Purchase Date (unless such Purchase Date is also an Interest Payment Date, in which case the Purchase Price shall not include accrued interest, which shall be paid in the normal course).

“Rate Determination Date” means any date on which the interest rate with respect to the 2008 Certificates shall be determined, which: (i) in the case of a Flexible Mode, shall be the first day of an Interest Period; (ii) in the case of a Daily Mode, shall be each Business Day commencing with the first day (which must be a Business Day) the 2008 Certificates become subject to the Daily Mode; (iii) in the case of the initial conversion to a Weekly Mode, shall be no later than the Business Day prior to the Mode Change Date for the 2008 Certificates, and thereafter, shall be each Wednesday or, if Wednesday is not a Business Day, then the Business Day next succeeding such Wednesday; (iv) in the case of a Term Rate Mode, shall be a Business Day no earlier than 15 Business Days and no later than the Business Day next preceding the first day of an Interest Period for the 2008 Certificates, as determined by the Remarketing Agent; and (v) in the case of a Fixed Rate Mode, shall be a date determined by the Remarketing Agent which shall be at least one Business Day prior to the Mode Change Date.

“Rating Agencies” means Moody’s and S&P, and their respective successors or assigns, or any other nationally recognized securities rating agency or agencies rating the 2008 Certificates at the request of the City.

“Rating Confirmation Notice” shall mean a written notice from the Rating Agencies then rating the 2008 Certificates, confirming that the rating on the 2008 Certificates (without giving effect to any Liquidity Facility) will not be lowered or withdrawn (other than a withdrawal of a short-term rating upon a change to a Fixed Rate Mode) as a result of the action proposed to be taken.

“Record Date” means: (i) with respect to the 2008 Certificates in a Short-Term Mode, the last Business Day before each Interest Payment Date; and (ii) with respect to the 2008 Certificates in a Long-Term Mode, the 15th day (whether or not a Business Day) of the month next preceding each Interest Payment Date.

“Reimbursement Agreement” means any reimbursement agreement, credit agreement, line of credit agreement, standby purchase agreement or other agreement, between a Credit Enhancement Provider or a Liquidity Facility Provider, as applicable, and the Authority and/or

the City, as the same may be amended from time to time pursuant to its terms, including the Reimbursement Agreement, dated as of July 1, 2011, by and between the City and the Bank.

“Remarketing Agent” means each Person selected by the Authority to act as remarketing agent for the 2008 Certificates pursuant to Section 3.12 hereof and approved by the 2008 Certificate Insurer (or, if a Control Event has occurred, the Bank).

“Remarketing Agreement” means an agreement approved by the 2008 Certificate Insurer, providing for the remarketing of the 2008 Certificates tendered for purchase, as the same may be amended from time to time pursuant to its terms.

“Remarketing Proceeds Account” means an Eligible Account by that name established within the 2008 Purchase Fund pursuant to Section 3.09(a) hereof and held in the name of the Trustee for the benefit of the Owners.

“Replacement Liquidity Facility” means the irrevocable, direct-pay letter of credit issued by the Bank with respect to the 2008 Certificates on the Substitution Date.

“Required Stated Amount” means, (i) in the case of each Liquidity Facility, at any time of calculation with respect to the 2008 Certificates, an amount equal to the aggregate principal amount of the 2008 Certificates then Outstanding together with interest accruing thereon (assuming an annual rate of interest equal to the Maximum Rate) for the minimum period specified by the Rating Agencies then rating the 2008 Certificates, as necessary to maintain the short-term rating of the 2008 Certificates, or (ii) in the case of each Credit Enhancement (other than a Credit Enhancement in the form of an insurance policy), at any time of calculation with respect to the 2008 Certificates, an amount equal to the aggregate principal amount of the 2008 Certificates then Outstanding together with interest accruing thereon (assuming an annual rate of interest equal to the Maximum Rate) for the minimum period specified by the Rating Agencies then rating the 2008 Certificates, as necessary to maintain the short-term rating (or, if no short term rating is then in effect, the rating) of the 2008 Certificates.

“Representation Letter” means the letter of representation to The Depository Trust Company, New York, New York, from the Authority.

“Reserve Funding Instruments” shall have the meaning given to such term in Section 4.04 hereof, including the 2008 Parity Reserve Fund Insurance Policy.

“Reserve Fund Requirement” shall have the meaning ascribed thereto in the Contract.

“S&P” means Standard & Poor’s Ratings Services, a division of The McGraw Hill Company, and its successors or assigns, except that if such entity shall be dissolved or liquidated or shall no longer perform the services of a municipal securities rating agency, then “S&P” shall be deemed to refer to any other nationally recognized municipal securities rating agency selected by the Authority.

“Securities Depositories” means: The Depository Trust Company, 55 Water Street, 50<sup>th</sup> Floor, New York, New York 10041-0099, Attention: Call Notification Department, Fax: (212) 855-7232; or, in accordance with then-current guidelines of the Securities and Exchange

Commission, such other securities depositaries as the Authority may designate in a Certificate of the Authority to the Trustee.

“Serial Certificate” means any 2008 Certificate not subject to mandatory prepayment from Sinking Fund Payments.

“Short-Term Mode” means the Daily Mode, the Weekly Mode or the Flexible Mode.

“Sinking Fund Payments” means the payments required under Section 2.03(a) hereof to be deposited in the 2008 Sinking Fund Subaccount under Section 4.03(b) hereof.

“Special Counsel” means any firm of nationally recognized municipal bond attorneys selected by the Authority and experienced in the issuance of municipal bonds and matters relating to the exclusion of the interest thereon from gross income for federal income tax purposes.

“State” means the State of California.

“Subrogated Certificate” means any Certificate of Participation with respect to which, pursuant to Section 10.05 of the Trust Agreement, the Bank or other credit enhancement provider, to the extent it has paid the principal of such Certificate of Participation from a drawing under the Replacement Liquidity Facility or other credit enhancement, has become subrogated to, and the assignee of, the rights to receive payment of such principal from the City pursuant to the Trust Agreement and has become the Owner of such Certificate of Participation.

“Substitution Date” means the date on which an Alternate Liquidity Facility is substituted for the Liquidity Facility then in effect.

“Supplemental Contract” shall have the meaning given such term in the Contract.

“Supplemental Trust Agreement” means any trust agreement then in full force and effect which has been duly executed and delivered by the Authority and the Trustee amendatory hereof or supplemental hereto; but only if and to the extent that such Supplemental Trust Agreement is specifically authorized hereunder.

“Tax Certificate” means, collectively, the Tax Certificate concerning certain matters pertaining to the use and investment of proceeds of the 2008 Certificates, executed and delivered by the City on the date of delivery of the 2008 Certificates, including any and all exhibits attached thereto.

“Tender Notice Deadline” means: (i) during the Daily Mode, 11:00 a.m. New York City time on any Business Day; and (ii) during the Weekly Mode, 5:00 p.m. New York City time on the Business Day 7 days prior to the applicable Purchase Date.

“Tender Notice” means a notice delivered by Electronic means or in writing that states: (i) the principal amount of the 2008 Certificates to be purchased pursuant to Section 3.01 hereof; (ii) the Purchase Date on which such 2008 Certificates are to be purchased; (iii) applicable

payment instructions with respect to such 2008 Certificates being tendered for purchase; and (iv) an irrevocable demand for such purchase.

“Term Certificates” means the 2008 Certificates subject to mandatory prepayment from Sinking Fund Payments.

“Term Rate” means the per annum interest rate for the 2008 Certificates in the Term Rate Mode determined pursuant to Section 2.16(a) hereof.

“Term Rate Mode” means the Mode during which the 2008 Certificates evidence interest at a Term Rate.

“Term Rate Period” means the period from (and including) the Mode Change Date or the date of initial conversion of the 2008 Certificates to a Term Rate Mode, as applicable, to (but excluding) the last day of the first period that 2008 Certificates shall be in the Term Rate Mode as established by the Authority pursuant to Section 2.16(a) hereof and, thereafter, the period from (and including) the beginning date of each successive Interest Rate Period selected for the 2008 Certificates by the Authority pursuant to Section 2.16(a) hereof while the 2008 Certificates are in the Term Rate Mode to (but excluding) the commencement date of the next succeeding Interest Period, including another Term Rate Period. Except as otherwise provided in this Trust Agreement, an Interest Period for the 2008 Certificates in the Term Rate Mode must be at least 180 days in length.

“Trust Agreement” means this Trust Agreement, dated as of May 1, 2008, between the Authority and the Trustee, as originally executed and as it may from time to time be amended or supplemented by all Supplemental Trust Agreements executed pursuant to the provisions hereof.

“Trustee” means The Bank of New York Mellon Trust Company, N.A., or any other association or corporation which may at any time be substituted in its place as provided in Section 6.01 hereof.

“2006 Certificates” means the Water Revenue Certificates of Participation 2006 Series A.

“2006 Supplemental Contract” means the 2006 Supplemental Installment Purchase Contract, dated as of November 1, 2006, by and between the City and the Authority, and consented to by the Trustee and Financial Guaranty Insurance Company.

“2006 Trust Agreement” means that certain Trust Agreement, dated as of November 1, 2006, by and between the Authority and the Trustee, delivered in connection with the 2006 Certificates.

“2008 Certificate Insurance Policy” means the financial guaranty insurance policy issued by the 2008 Certificate Insurer guaranteeing the scheduled payment of principal of and interest evidenced and represented by the 2008 Certificates.

“2008 Certificate Insurer” means Assured Guaranty Corp., its successors and assigns.

“2008 Certificates” means all of the Water Refunding Revenue Certificates of Participation, 2008 Series A, evidencing and representing proportionate interests of the owners thereof in the 2008 Payments to be made by the City, and executed and delivered in accordance with Article II hereof.

“2008 Debt Service Fund” means the fund by that name established pursuant to Section 4.02 hereof.

“2008 Interest Account” means the account by that name established within the 2008 Debt Service Fund pursuant to Section 4.03(a) hereof.

“2008 Interest Rate Swap Agreement” has the meaning given such term in the 2008 Supplemental Contract.

“2008 Parity Reserve Fund Insurance Policy” means the reserve fund financial guaranty insurance policy issued by the 2008 Certificate Insurer and deposited in the Parity Reserve Fund pursuant to Section 2.12 hereof.

“2008 Payments” means the installment payments of interest, principal, and prepayment premium, if any, payable by the City under and pursuant to the 2008 Supplemental Contract.

“2008 Prepayment Subaccount” means the subaccount by that name established within the 2008 Principal Account of the 2008 Debt Service Fund pursuant to Section 4.03(b) hereof.

“2008 Principal Account” means the account by that name established within the 2008 Debt Service Fund pursuant to Section 4.03(b) hereof.

“2008 Project” means the refinancing of improvements to the Water Utility System described in Exhibit A to the 2008 Supplemental Contract.

“2008 Purchase Fund” means the fund by that name established pursuant to Section 3.09 hereof.

“2008 Liquidity Facility Payment Account” means the account by that name established pursuant to Section 4.08 hereof.

“2008 Sinking Fund Subaccount” means the subaccount by that name within the 2008 Principal Account of the 2008 Debt Service Fund established pursuant to Section 4.03(b) hereof.

“2008 Supplemental Contract” means that certain 2008 Supplemental Installment Purchase Contract, dated as of May 1, 2008, by and between the City and the Authority, supplementing the Master Contract.

“Weekly Mode” means the Mode during which the 2008 Certificates evidence interest at the Weekly Rate.

“Weekly Rate” means the per annum interest rate with respect to the 2008 Certificates in the Weekly Mode determined pursuant to Section 2.15(b) hereof.

“Weekly Rate Period” means the period during which the 2008 Certificates evidence interest at a Weekly Rate, which shall be the period commencing on Thursday of each week to and including Wednesday of the following week, except the first Weekly Rate Period which shall be from the Mode Change Date for the 2008 Certificates to and including the Wednesday of the following week and the last Weekly Rate Period which shall be from and including the Thursday of the week prior to the Mode Change Date to and including the day next preceding the Mode Change Date.

“Written Request of the Authority” means an instrument in writing signed by the Auditor and Treasurer of the Authority or by any other officer of the Authority duly authorized by the Authority for that purpose.

Section 1.02. Equal Security. In consideration of the acceptance of the 2008 Certificates by the Owners thereof, this Trust Agreement shall be deemed to be and shall constitute a contract between the Authority and the Owners from time to time of all 2008 Certificates authorized, executed, and delivered hereunder and then Outstanding to secure the full and final payment of the interest, principal, and prepayment premiums, if any, evidenced and represented by the 2008 Certificates which may from time to time be authorized, executed, issued and delivered hereunder, subject to the agreements, conditions, covenants and provisions contained herein; and all agreements and covenants set forth herein to be performed by or on behalf of the Trustee shall be for the equal and proportionate benefit, protection and security of all Owners without distinction, preference or priority as to security or otherwise of any 2008 Certificates over any other 2008 Certificates by reason of the number or date thereof or the time of authorization, sale, execution, or delivery thereof or for any cause whatsoever, except as expressly provided herein or therein.

Section 1.03. New York City Time. All references herein to a particular time of day shall be New York City time unless the context clearly otherwise requires.

## ARTICLE II

### THE 2008 CERTIFICATES

Section 2.01. Conditions and Terms of 2008 Certificates. The Trustee is hereby authorized and directed to execute and deliver the 2008 Certificates in the aggregate principal amount of \$47,625,000, aggregating the principal installments of the 2008 Payments, and each evidencing and representing a proportionate interest in the 2008 Payments.

Section 2.02. Terms of the 2008 Certificates.

(a) The 2008 Certificates shall be issued as fully registered securities certificates without coupons in Authorized Denominations. The 2008 Certificates shall be registered initially in the name of “Cede & Co.,” as nominee of DTC, the initial Securities Depository, and shall be evidenced by one certificate in the total aggregate principal amount of the 2008 Certificates. Registered ownership of the 2008 Certificates, or any portion thereof, may not thereafter be transferred except as set forth in Section 2.06 hereof.

(b) The 2008 Certificates shall be dated the Delivery Date.

(c) Except as otherwise provided in the Liquidity Facility or the Reimbursement Agreement, or, in the case of 2008 Certificates being converted to a Fixed Rate, except as otherwise provided in Section 2.18(d) hereof, the 2008 Certificates shall mature on October 1, 2036.

(d) The 2008 Certificates shall be subject to prepayment as provided in Section 2.03 hereof and optional and mandatory tender for purchase as provided in Article III.

(e) The Trustee shall identify all payments (whether made by check or by wire transfer) of interest, principal, Purchase Price and Prepayment Price by CUSIP number of the 2008 Certificates.

(f) During each Interest Period for each Mode, the interest rate or rates with respect to the 2008 Certificates shall be determined in accordance with this Article II and shall be payable on the applicable Interest Payment Date for such Interest Period; provided that the interest rate or rates shall not exceed the Maximum Rate. All 2008 Certificates shall evidence interest in the same Mode, but need not evidence interest at the same rate at any one time. Interest with respect to the 2008 Certificates accruing at the Daily Rate, Weekly Rate or Flexible Rate shall be computed upon the basis of a 365- or 366-day year, as applicable, for the actual number of days elapsed. Interest with respect to the 2008 Certificates accruing at a Fixed Rate or a Term Rate shall be computed upon the basis of a 360-day year, consisting of twelve 30-day months. Each 2008 Certificate shall evidence interest on overdue principal and, to the extent permitted by law, on overdue interest at the rate evidenced by such 2008 Certificate on the date on which such principal became due and payable. Notwithstanding the foregoing, the interest rate and payment terms of Liquidity Provider Certificates shall be governed by the provisions of the Liquidity Facility or related Reimbursement Agreement, as applicable.

(g) Interest evidenced by each 2008 Certificate shall accrue from and including the Interest Accrual Date immediately preceding the date of authentication thereof, or, if such date of authentication shall be an Interest Accrual Date, from such Interest Accrual Date or if such date of authentication shall be prior to the second Interest Accrual Date, from the Delivery Date; provided, however, that if interest evidenced by the 2008 Certificates shall be in default, interest on the 2008 Certificates issued in exchange for 2008 Certificates surrendered for registration of transfer or exchange shall accrue from the date to which interest has been paid in full with respect to the 2008 Certificates or, if no interest has been paid with respect to the 2008 Certificates, from the Delivery Date.

(h) Payment of interest evidenced by the 2008 Certificates shall be made to the person appearing on the registration books of the Trustee as the Owner thereof as of the close of business on the applicable Record Date, such interest to be payable on each Interest Payment Date by the Trustee (i) by check mailed on such Interest Payment Date to such Owner's address as it appears on the registration books of the Trustee at the close of business on the Record Date or (ii) by wire transfer to any Owner of at least \$1,000,000 aggregate principal amount of 2008 Certificates or the Liquidity Facility Provider (in the case of Liquidity Provider Certificates) according to the written instructions provided by such Owner or the Liquidity Provider, as the case may be, on or prior to the applicable Record Date to the Trustee, which written instructions

shall remain in effect until revised by such Owner or Liquidity Facility Provider, as the case may be, by an instrument in writing delivered to the Trustee.

(i) If for any reason, the Liquidity Provider Certificates remain in book-entry and are not assigned a separate CUSIP number, the Trustee shall pay the principal of, prepayment premium, if any, and interest with respect to the 2008 Certificates (including the Liquidity Provider Certificates) in accordance with the letter of representations with DTC computed at the Basic Certificate Rate; and the Authority shall pay to the Trustee for payment to the Liquidity Facility provider outside the book-entry system the remainder of (i) the interest then due with respect to Liquidity Provider Certificates computed at the applicable interest rate minus (ii) the interest that would then be due with respect to Liquidity Provider Certificates if such interest were computed at the Basic Certificate Rate.

(j) The principal evidenced and represented by the 2008 Certificates other than Liquidity Provider Certificates shall be payable in lawful money of the United States of America upon the surrender thereof on the respective 2008 Certificate Payment Date or on prepayment prior thereto at the Corporate Trust Office of the Trustee. The principal evidenced and represented by Liquidity Provider Certificates shall be payable in lawful money of the United States of America by wire transfer to the Liquidity Facility Provider according to the written instructions provided by the Liquidity Provider on or prior to the applicable 2008 Certificate Payment Date to the Trustee, which written instructions shall remain in effect until revised by the Liquidity Facility Provider by an instrument in writing delivered to the Trustee.

(k) The first Mode for the 2008 Certificates shall be the Weekly Mode. The first Weekly Rate Period for the 2008 Certificates shall be the period commencing on and including the Delivery Date and ending on and including June 4, 2008. The First Interest Payment Date is June 2, 2008. The Mode for the 2008 Certificates may be changed in accordance with this Article II.

(l) In the absence of manifest error, the determination of any Daily Rate, Weekly Rate, Flexible Rate, Term Rate and Fixed Rate by the Remarketing Agent, the determination of each Flexible Rate Period for any 2008 Certificate in a Flexible Mode by the Remarketing Agent and the determination of the length of each Term Rate Period by the Authority shall be conclusive and binding upon the Authority, the other Notice Parties and each Owner.

(m) In the absence of manifest error, the record of interest rates maintained by the Trustee shall be conclusive and binding upon the Authority, the other Notice Parties and each Owner.

### Section 2.03. Prepayment of Certificates.

(a) Mandatory Sinking Fund Prepayment. Except in the event of serialization of the 2008 Certificates in accordance with Section 2.18(d) hereof, the 2008 Certificates are subject to mandatory prepayment from Sinking Fund Payments prior to their Maturity Date, in part by lot, on October 1 of each year on and after October 1, 2008, in accordance with the schedule set forth below upon notice as hereinafter provided, from and in the amount of the principal installment of the 2008 Payments due and payable on such dates, at a prepayment price equal to the sum of the

principal amount evidenced and represented thereby plus accrued and unpaid interest evidenced and represented thereby to the Prepayment Date, without a prepayment premium.

Certificates Sinking Fund Payments

Mandatory Sinking Fund Payment Date (October 1)	Sinking Fund Payment	Mandatory Sinking Fund Payment Date (October 1)	Sinking Fund Payment
2008	\$290,000	2023	\$2,300,000
2009	285,000	2024	2,410,000
2010	285,000	2025	2,515,000
2011	285,000	2026	2,595,000
2012	310,000	2027	2,705,000
2013	310,000	2028	2,810,000
2014	340,000	2029	2,945,000
2015	340,000	2030	3,055,000
2016	365,000	2031	3,185,000
2017	365,000	2032	3,295,000
2018	395,000	2033	3,430,000
2019	395,000	2034	3,570,000
2020	395,000	2035	3,705,000
2021	425,000	2036	3,870,000
2022	450,000		

Notwithstanding the foregoing, no 2008 Certificate (other than a Liquidity Provider Certificate) shall be optionally prepaid while any Liquidity Provider Certificate is Outstanding unless all Outstanding Liquidity Provider Certificates are prepaid or purchased by the Trustee and cancelled concurrently with such prepayment or purchase.

If for any reason, the Liquidity Provider Certificates remain in book-entry but have not been assigned a separate CUSIP number, the Trustee shall apply the amounts in the 2008 Sinking Fund Subaccount set aside for prepayment to the purchase from the Liquidity Facility provider of Liquidity Provider Certificates in an aggregate principal amount not in excess of the principal amount intended to be prepaid at a purchase price equal to the prepayment price specified above. The Liquidity Provider Certificates so purchased shall be cancelled by the Trustee, and the principal amount thereof shall be credited against the principal amount of the 2008 Certificates otherwise required to be prepaid.

Notwithstanding the foregoing, if any such 2008 Certificates have been optionally prepaid pursuant to Section 2.03(c) hereof, the amounts of such Sinking Fund Payments shall be reduced as directed by the Authority, or if not so directed, proportionately in increments of Authorized Denominations by the principal amount evidenced and represented by all such 2008 Certificates so optionally prepaid.

All such Sinking Fund Payments shall be deposited in the 2008 Sinking Fund Subaccount of the 2008 Principal Account established pursuant to Section 4.03 hereof. On each Sinking

Fund Payment date, the Trustee shall apply the Sinking Fund Payment required on such date to the mandatory prepayment or payment of Term Certificates, upon the notice and in the manner provided in this Section 2.03(a) hereof; provided that, at any time prior to giving notice of such prepayment, the Trustee may apply moneys in the 2008 Sinking Fund Subaccount to the purchase of Term Certificates at public or private sale, as and when and at such prices (including brokerage and other charges) as directed in writing by the Authority, except that the purchase price shall not exceed the prepayment price that would be payable for Term Certificates upon prepayment by application of such Sinking Fund Payment. If, during the 12-month period immediately preceding said Sinking Fund Payment date, the Trustee has purchased Term Certificates with moneys in the 2008 Sinking Fund Subaccount, or, during said period and prior to giving said notice of prepayment, the City or the Authority has deposited Term Certificates with the Trustee (together with a request of the Authority or the City to apply such 2008 Certificates so deposited to the Sinking Fund Payment due on said Sinking Fund Payment date), or Term Certificates were at any time purchased or prepaid by the Trustee from the 2006 Prepayment Account and allocable to said Sinking Fund Payment, such 2008 Certificates so purchased, deposited, or prepaid shall be applied, to the extent of the full principal amount evidenced and represented thereby, to reduce said Sinking Fund Payment.

(b) Mandatory Prepayment of Liquidity Provider Certificates. Any Liquidity Provider Certificates from time to time Outstanding shall be subject to mandatory prepayment in the amounts and at the times and at the prepayment prices specified therefor in the Liquidity Facility with the Liquidity Facility Provider applicable thereto.

(c) Optional Prepayment.

(i) Each 2008 Certificate in a Daily Mode or a Weekly Mode shall be subject to prepayment at the option of the Authority, in whole or in part, in Authorized Denominations on any Business Day, at a prepayment price equal to 100% of the principal amount thereof, plus, accrued interest, if any, to the Prepayment Date, without premium.

(ii) Flexible Rate Certificates are not subject to optional prepayment prior to their respective Mandatory Purchase Dates. Flexible Rate Certificates shall be subject to prepayment at the option of the Authority in whole or in part on their respective Mandatory Purchase Dates at a prepayment price equal to 100% of the principal amount thereof, without premium.

(iii) Each 2008 Certificate in a Term Rate Mode shall be subject to prepayment at the option of the Authority, in whole or in part, on each Mandatory Purchase Date applicable to the 2008 Certificates in a Term Rate Mode, at a prepayment price equal to 100% of the principal amount thereof, without premium.

(iv) Each Certificate in a Term Rate Mode or a Fixed Rate Mode is subject to prepayment in whole or in part on any date (and if in part, in such order of maturity as the Authority shall specify and within a maturity by lot or by such other method as the Trustee determines to be fair and reasonable and in Authorized Denominations) commencing on the Interest Payment Date next following the tenth anniversary of the

change to a Term Rate Mode or a Fixed Mode at a prepayment price equal to 100% of the principal amount of 2008 Certificates being prepaid, together with accrued interest, if any, to the Prepayment Date, without premium. If the length of the Term Rate Period or the Fixed Rate Period for the 2008 Certificates is less than ten (10) years, then the 2008 Certificates shall not be subject to optional prepayment during the Term Rate Period or Fixed Rate Period, as applicable.

(v) In connection with a change to a Term Rate Mode or a Fixed Rate Mode for the 2008 Certificates, the Authority may waive or otherwise alter its rights to direct the prepayment of the 2008 Certificates set forth in (c)(iv) above; provided that notice describing such waiver or alteration shall be submitted to the Trustee and the Remarketing Agent, or Fixed Rate Remarketing Agent, as applicable, together with a Favorable Opinion of Special Counsel.

(d) Reserved.

(e) Selection of 2008 Certificates. If less than all of the Outstanding 2008 Certificates are to be prepaid at any one time, the Authority shall designate the Certificate Payment Dates or portions thereof of the 2008 Certificates to be prepaid; provided, that any Liquidity Provider Certificates that remain outstanding shall be selected for prepayment prior to 2008 Certificates that are not Liquidity Provider Certificates. If less than all Outstanding 2008 Certificates of any particular Certificate Payment Date are to be prepaid at any one time, the Trustee shall select the 2008 Certificates of such Certificate Payment Date to be prepaid by lot, except that if any 2008 Certificate or portion thereof to be prepaid is a Term Certificate, the Authority may specify in a Written Request of the Authority filed with the Trustee, the particular Sinking Fund Payments for such Term Certificate to be prepaid. For purposes of such selection, 2008 Certificates of each Certificate Payment Date shall be deemed to be composed of Authorized Denominations and any such Authorized Denomination may be separately prepaid. If the Authority elects to optionally prepay 2008 Certificates pursuant to Section 2.03(c) hereof, it will notify the Trustee of the prepayment date and the principal amount evidenced and represented by the 2008 Certificates of each Certificate Payment Date to be prepaid on such prepayment date at least 45 days prior to such prepayment date; provided, that the Trustee may, at its option, waive any such notice or accept any notice received at a later date.

(f) Notice of Prepayment. Notice of prepayment shall be mailed by the Trustee, not less than 30 nor more than 60 days prior to the prepayment date to (i) the respective Owners of the 2008 Certificates designated for prepayment at their addresses appearing on the registration books of the Trustee, (ii) the Securities Depositories and (iii) one or more Information Services. Notice of prepayment to the Securities Depositories and the Information Services shall be given by first-class mail, certified mail, overnight delivery or facsimile transmission or by other approved means. Each notice of prepayment shall state the date of such notice, the prepayment price, the place of prepayment (including the name and appropriate address of the Trustee), the CUSIP number (if any) of the 2008 Certificates to be prepaid, and, if less than all of the 2008 Certificates maturing on any one Certificate Payment Date are to be prepaid, the distinctive certificate numbers of the 2008 Certificates of such Certificate Payment Date to be prepaid and, in the case of 2008 Certificates to be prepaid in part only, the respective portions of the principal amount evidenced and represented thereby to be prepaid. Each such notice shall also state that

on said date there will become due and payable on each of said 2008 Certificates the prepayment price thereof and in the case of a 2008 Certificate to be prepaid in part only, the specified portion of the principal amount evidenced and represented thereby to be prepaid, together with accrued and unpaid interest evidenced and represented thereby to the prepayment date, and that from and after such prepayment date interest evidenced and represented thereby shall cease to accrue, and shall require that such 2008 Certificates be then surrendered at the address of the Trustee specified in the prepayment notice. Failure to receive such notice shall not invalidate any of the proceedings taken in connection with such prepayment.

Any prepayment may be cancelled if the notice of such prepayment has not been mailed to the respective Owners of the 2008 Certificates or if such notice expressly conditioned the prepayment upon the occurrence of one or more events. Notice of any such cancellation shall be given in the same manner as the notice of prepayment was given at least 3 Business Days prior to the date scheduled for prepayment.

If notice of prepayment has been duly given as aforesaid and money for the payment of the prepayment price of the 2008 Certificates called for prepayment is held by the Trustee, then on the prepayment date designated in such notice, 2008 Certificates so called for prepayment shall become due and payable, and from and after the date so designated interest evidenced and represented by such 2008 Certificates shall cease to accrue, and the Owners of such 2008 Certificates shall have no rights in respect thereof except to receive payment of the prepayment price thereof.

All 2008 Certificates prepaid pursuant to the provisions of this Section shall be cancelled and destroyed by the Trustee and shall not be redelivered.

(g) No Notice of Prepayment. Notwithstanding any other provision of this Trust Agreement to the contrary, no notice of prepayment is required to be given with respect to any prepayment occurring on a Mandatory Purchase Date or prepayment of Liquidity Provider Certificates.

(h) Mandatory Purchase in Lieu of Prepayment. Each Owner, by purchase and acceptance of any 2008 Certificate irrevocably grants to the Authority the option to purchase such 2008 Certificate on any date such 2008 Certificate is subject to optional prepayment provided in (c) above at a purchase price equal to the prepayment price then applicable to such 2008 Certificate, plus accrued interest thereon to the date of purchase. In order to exercise such option, the Authority shall deliver to the Trustee a Favorable Opinion of Special Counsel and shall direct the Trustee to provide notice of mandatory purchase in lieu of prepayment, such notice to be provided, as and to the extent applicable, in accordance with the provisions set forth in Section 3.02 hereof. On the date fixed for purchase of any 2008 Certificate pursuant to this Section 2.03(h), the Authority shall pay the purchase price of such 2008 Certificate to the Trustee in immediately available funds and the Trustee shall pay the same to the Owners of the 2008 Certificates being purchased against delivery thereof. All 2008 Certificates so purchased shall be delivered to the Trustee to hold for the benefit of the Authority or for cancellation upon the receipt of such instructions from the Authority. Without the prior written consent of the 2008 Certificate Insurer, no 2008 Certificates shall be purchased in lieu of prepayment by the

Authority, the City or any of its affiliates unless such 2008 Certificates are redeemed, defeased or cancelled.

Notwithstanding any other provision of this Trust Agreement, the purchase price of any 2008 Certificate subject to mandatory purchase in lieu of prepayment pursuant to this Section 2.03(h) shall be paid solely by the Authority and such 2008 Certificate shall not be eligible to be purchased and shall not be purchased from a drawing on any Liquidity Facility. In the event that the Authority lacks sufficient funds to pay the purchase price of any 2008 Certificate subject to mandatory purchase in lieu of prepayment pursuant to this Section 2.03(h) on the date fixed for such purchase, the Authority shall cancel such mandatory purchase in lieu of prepayment and shall return each such 2008 Certificate to the Owner who shall have tendered such 2008 Certificate for mandatory purchase in lieu of prepayment pursuant to this Section 2.03(h). The Trustee shall give notice that such mandatory purchase was not effected promptly following the date fixed for such purchase. Any failure to pay the purchase price of any 2008 Certificate subject to mandatory purchase pursuant to this Section 2.03(h) shall not constitute an Event of Default under this Trust Agreement.

Section 2.04. Form of 2008 Certificates. The 2008 Certificates while in Weekly Mode shall be substantially in the form set forth in Exhibit A hereto attached and by this reference herein incorporated. Upon a change in Mode of the 2008 Certificates to another Mode, and upon any subsequent change from one Mode to another Mode, a new form of 2008 Certificate shall be prepared, if and to the extent necessary, which contains the terms of the 2008 Certificates applicable in the new Mode.

Section 2.05. Execution of 2008 Certificates. The 2008 Certificates shall be executed by the Trustee by the manual signature of an authorized officer or signatory of the Trustee.

Section 2.06. Transfer and Payment of 2008 Certificates. Any 2008 Certificates may, in accordance with its terms, be transferred in the books required to be kept pursuant to the provisions of Section 2.08 hereof by the person in whose name it is registered, in person or by his duly authorized attorney, upon surrender of such 2008 Certificates at the Corporate Trust Office of the Trustee for cancellation accompanied by delivery of a duly executed written instrument of transfer in a form acceptable to the Trustee. Whenever any 2008 Certificate or 2008 Certificates shall be surrendered for transfer, the Trustee shall execute and deliver to the transferee a new 2008 Certificate or 2008 Certificates of the same Certificate Payment Date evidencing and representing a like aggregate principal amount in Authorized Denominations. The Trustee shall require the payment by the Owner requesting such transfer of any tax or other governmental charge required to be paid with respect to such transfer as a condition precedent to the exercise of such privilege.

The Trustee may deem and treat the registered owner of any 2008 Certificates as the absolute owner of such 2008 Certificates for the purpose of receiving payment thereof and for all other purposes, whether such 2008 Certificates shall be overdue or not, and the Trustee shall not be affected by any notice or knowledge to the contrary; and payment of the interest and principal and prepayment premium, if any, evidenced and represented by such 2008 Certificates shall be made only to such registered owner, which payments shall be valid and effectual to satisfy and discharge liability on such 2008 Certificates to the extent of the sum or sums so paid.

Except with respect to tenders pursuant to Sections 3.01 and 3.02 herein, the Trustee shall not be required to register the transfer of any 2008 Certificate during the period commencing on the date 15 days preceding the selection of 2008 Certificates for prepayment and ending on the date of mailing of notice of such prepayment, or any 2008 Certificate which has been selected for prepayment in whole or in part, from and after the day of mailing of a notice of prepayment of such 2008 Certificates selected for prepayment in whole or in part as provided in Section 2.03 hereof.

Section 2.07. Exchange of Certificates. 2008 Certificates may be exchanged at the Corporate Trust Office of the Trustee for 2008 Certificates evidencing and representing a like aggregate principal amount of 2008 Certificates of the same Certificate Payment Date of other Authorized Denominations. The Trustee shall require the payment by the Owner requesting such exchange of any tax or other governmental charge required to be paid with respect to such exchange as a condition precedent to the exercise of such privilege.

Except with respect to tenders pursuant to Sections 3.01 and 3.02 herein, the Trustee shall not be required to exchange any 2008 Certificate during the 15-day period preceding the selection of 2008 Certificates for prepayment, or any 2008 Certificate which has been selected for prepayment in whole or in part, from and after the day of mailing of a notice of prepayment of such 2008 Certificates selected for prepayment in whole or in part as provided in Section 2.03 hereof.

Section 2.08. Certificate Registration Books. The Trustee will keep at its Corporate Trust Office sufficient books for the registration and transfer of the 2008 Certificates which shall at all times be open to inspection by the Authority during regular business hours with reasonable prior notice, and upon presentation for such purpose the Trustee shall, under such reasonable regulations as it may prescribe, register or transfer the 2008 Certificates in such books as hereinabove provided.

Section 2.09. Mutilated, Destroyed, Stolen or Lost Certificates. If any 2008 Certificate shall become mutilated the Trustee, at the expense of the Owner, shall thereupon execute and deliver a new 2008 Certificate of like tenor and amount in exchange and substitution for the 2008 Certificate so mutilated, but only upon surrender to the Trustee of the 2008 Certificate so mutilated. Every mutilated 2008 Certificate so surrendered to the Trustee shall be cancelled and destroyed.

If any 2008 Certificate shall be lost, destroyed or stolen, evidence of such loss, destruction or theft may be submitted to the Trustee and, if such evidence is satisfactory to the Trustee and indemnity satisfactory to the Trustee has been given, the Trustee, at the expense of the Owner, shall thereupon execute and deliver a new 2008 Certificate of like tenor in lieu of and in substitution for the 2008 Certificate so lost, destroyed or stolen.

The Trustee may require payment of a reasonable sum for each new 2008 Certificate delivered under this Section 2.09 and of the expenses which may be incurred by the Authority and the Trustee in the premises. Any 2008 Certificate executed and delivered under the provisions of this Section in lieu of any 2008 Certificate alleged to be lost, destroyed or stolen shall be equally and proportionately entitled to the benefits of this Trust Agreement with all other

2008 Certificates secured by this Trust Agreement. The Trustee shall not be required to treat both the original 2008 Certificate and any replacement 2008 Certificate as being Outstanding for the purpose of determining the principal amount of 2008 Certificates which may be executed and delivered hereunder or for the purpose of determining any percentage of 2008 Certificates Outstanding hereunder, but both the original and replacement 2008 Certificate shall be treated as one and the same.

Section 2.10. Temporary Certificates. The 2008 Certificates executed and delivered under this Trust Agreement may be initially executed and delivered in temporary form exchangeable for definitive 2008 Certificates when ready for delivery. The temporary 2008 Certificates may be printed, lithographed or typewritten, shall be of such denominations as may be determined by the Trustee, shall be in fully registered form and may contain such reference to any of the provisions of this Trust Agreement as may be appropriate. Every temporary 2008 Certificate shall be executed and delivered by the Trustee, upon the same conditions and terms and in substantially the same manner as definitive 2008 Certificates. If the Trustee executes and delivers temporary 2008 Certificates it will execute and furnish definitive 2008 Certificates and thereupon the temporary 2008 Certificates may be surrendered, for cancellation, in exchange therefor at the Corporate Trust Office of the Trustee, and the Trustee shall deliver in exchange for such temporary 2008 Certificates definitive 2008 Certificates evidencing and representing an equal aggregate principal amount of 2008 Certificates of Authorized Denominations. Until so exchanged, the temporary 2008 Certificates shall be entitled to the same benefits under this Trust Agreement as definitive 2008 Certificates delivered hereunder.

Section 2.11. Use of Book-Entry System for Certificates.

(a) The 2008 Certificates initially shall be delivered in the form of a single executed fully registered securities certificate for each stated Maturity Date of such 2008 Certificates, representing the aggregate principal amount evidenced and represented by the 2008 Certificates of such Maturity Date. Upon initial delivery, the ownership of all such 2008 Certificates shall be registered in the registration records maintained by the Trustee pursuant to Section 2.08 hereof in the name of Cede & Co., as nominee of DTC, or such other nominee as DTC shall request pursuant to the Representation Letter. The Trustee may treat DTC (or its nominee) as the sole and exclusive owner of the 2008 Certificates registered in its name for the purposes of payment of the principal or prepayment price and interest evidenced and represented by such 2008 Certificates, selecting the 2008 Certificates or portions thereof to be prepaid, giving any notice permitted or required to be given to Owners hereunder, registering the transfer of 2008 Certificates, obtaining any consent or other action to be taken by Owners of the 2008 Certificates and for all other purposes whatsoever; and the Trustee shall not be affected by any notice to the contrary. Neither the Trustee nor the Authority shall have any responsibility or obligation to any Participant (which shall mean, for purposes of this Section, securities brokers and dealers, banks, trust companies, clearing corporations and other entities, some of whom directly or indirectly own DTC), any person claiming a beneficial ownership interest in the 2008 Certificates under or through DTC or any Participant, or any other person which is not shown on the registration records as being an Owner of 2008 Certificates, with respect to (i) the accuracy of any records maintained by DTC or any Participant, (ii) the payment by DTC or any Participant of any amount in respect of the principal or prepayment price or interest evidenced and represented by the 2008 Certificates (iii) any notice which is permitted or required to be given to Owners of

2008 Certificates hereunder, (iv) the selection by DTC or any Participant of any person to receive payment in the event of a partial prepayment of the 2008 Certificates, or (v) any consent given or other action taken by DTC as Owner of 2008 Certificates. Notwithstanding anything to the contrary herein, the Trustee shall pay all principal, prepayment premium, if any, and interest evidenced and represented by the 2008 Certificates only at the times, to the accounts, at the addresses and otherwise in accordance with the Representation Letter, and all such payments shall be valid and effective to satisfy fully and discharge the principal, prepayment premium, if any, and interest evidenced and represented by the 2008 Certificates to the extent of the sum or sums so paid. Upon delivery by DTC to the Trustee of written notice to the effect that DTC has determined to substitute a new nominee in place of its then existing nominee, the 2008 Certificates will be transferable to such new nominee in accordance with subsection (c) of this Section.

(b) In the event that the Authority determines that it is in the best interests of the beneficial owners of the 2008 Certificates that they be able to obtain securities certificates, the Trustee shall, upon the written instruction of the Authority, so notify DTC, whereupon DTC shall notify the Participants of the availability through DTC of securities certificates. In such event, the 2008 Certificates will be transferable in accordance with subsection (c) of this Section. DTC may determine to discontinue providing its services with respect to the 2008 Certificates at any time by giving written notice of such discontinuance to the Authority and the Trustee and discharging its responsibilities with respect thereto under applicable law. In such event, the 2008 Certificates will be transferable in accordance with subsection (c) of this Section. Whenever DTC requests the Authority and the Trustee to do so, the Trustee and the Authority will cooperate with DTC in taking appropriate action after reasonable notice to arrange for another securities depository to maintain custody of all certificates evidencing the 2008 Certificates then Outstanding. In such event, the 2008 Certificates will be transferable to such securities depository in accordance with subsection (c) of this Section, and thereafter, all references in this Trust Agreement to DTC or its nominee shall be deemed to refer to such successor securities depository and its nominee, as appropriate.

(c) In the event that any transfer or exchange of 2008 Certificates is authorized under subsection (a) or (b) of this Section, such transfer or exchange shall be accomplished upon receipt by the Trustee from the registered owner thereof of the 2008 Certificates to be transferred or exchanged and appropriate instruments of transfer to the permitted transferee, all in accordance with the applicable provisions of Sections 2.06 and 2.07 hereof. In the event securities certificates are delivered to Owners other than Cede & Co., its successor as nominee for DTC as Owner of all the 2008 Certificates, another securities depository as Owner of all the 2008 Certificates, or the nominee of such successor securities depository, the provisions of Sections 2.06 and 2.07 hereof shall also apply to, among other things, the registration, exchange and transfer of the 2008 Certificates and the method of payment of principal, prepayment premium, if any, and interest evidenced and represented by the 2008 Certificates.

(d) Liquidity Provider Certificates. Notwithstanding any other provisions hereof, the Trustee shall take all necessary action to obtain a separate CUSIP number and to qualify Liquidity Provider Certificates for book-entry in accordance with the procedures of DTC. If for any reason the Liquidity Provider Certificates are not assigned a separate CUSIP number or if a separate CUSIP number has been assigned but the Liquidity Provider so elects, at the request of

the Liquidity Facility Provider, Liquidity Provider Certificates shall be registered in the name of the Liquidity Facility Provider or its nominees or registered assigns, and not in the name of the Depository, DTC, Cede & Co. or other nominee or its registered assign. In such case, the Trustee shall take all necessary action to withdraw Liquidity Provider Certificates from the Depository in order to register Liquidity Provider Certificates in the name of the Liquidity Facility Provider, or the nominee or registered assigns thereof.

Section 2.12. Authorization of Delivery of 2008 Certificates; Application of Proceeds. On the Delivery Date, the Trustee authorized the execution and delivery of the 2008 Certificates to the purchaser thereof upon the Written Request of the Authority and upon receipt of the proceeds of the sale thereof. Upon receipt of the proceeds of the sale of the 2008 Certificates from the purchaser thereof (in the amount of \$46,581,988.19 (representing the \$47,625,000.00 aggregate principal amount of the 2008 Certificates, less underwriter's discount of \$153,920.63, and less \$826,615.80 transferred by the purchaser at the request of the Authority to the 2008 Certificate Insurer as payment of the premium for the 2008 Certificate Insurance Policy and \$62,475.38 transferred by the purchaser at the request of the Authority to the 2008 Certificate Insurer as payment of the premium for the 2008 Parity Reserve Fund Insurance Policy), the Trustee set aside and deposited the proceeds received from such sale in the following respective accounts or funds or with the following respective persons, in the following order of priority:

- (a) the Trustee deposited to the 2006 Debt Service Fund, established pursuant to Section 4.03 of the 2006 Trust Agreement, the amount of \$46,275,000.00;
- (b) the Trustee deposited to the Parity Reserve Fund, created pursuant to the 1997 Trust Agreement, the amount of \$36.57; and
- (c) the Trustee deposited the remainder of the proceeds of sale of the 2008 Certificates (such amount being \$306,951.62) in the Costs of Issuance Fund established pursuant to Section 4.05 hereof.

Simultaneously with the deposit of proceeds, the Trustee (i) retained in the Parity Reserve Fund, created pursuant to the 1997 Trust Agreement, which fund was continued pursuant to Section 4.04 hereof, the amount of \$1,834,515.50 from amounts in the Parity Reserve Fund deposited from the proceeds 2006 Certificates and (ii) deposited in the Parity Reserve Fund the 2008 Parity Reserve Fund Insurance Policy, together being an amount sufficient to cause the balance on deposit in, or credited to the Parity Reserve Fund to be equal to the Reserve Fund Requirement upon delivery of the 2008 Certificates.

Section 2.13. Reserved.

Section 2.14. Determination of Flexible Rates and Interest Periods During Flexible Mode. An Interest Period for the 2008 Certificates in the Flexible Mode shall be of such duration of from one to 397 calendar days, ending on a day preceding a Business Day or the Maturity Date, as the Remarketing Agent shall determine in accordance with the provisions of this Section 2.14. In making the determinations with respect to Interest Periods, subject to limitations imposed by the immediately preceding sentence, on each Rate Determination Date for a Flexible Rate Certificate, the Remarketing Agent shall select the Interest Period that would

result in the Remarketing Agent being able to remarket the 2008 Certificates at par in the secondary market at the lowest average interest cost under then-existing marketing conditions; provided, however, that if the Remarketing Agent has received notice from the Authority to the effect that the Mode for the 2008 Certificates is to be changed from the Flexible Mode to any other Mode, the Remarketing Agent shall select Interest Periods that do not extend beyond the resulting Mode Change Date. The Flexible Rate for the 2008 Certificates in a Flexible Mode shall be the rate of interest per annum determined by the Remarketing Agent to be the minimum interest rate which, if evidenced by the 2008 Certificates, would enable the Remarketing Agent to sell the 2008 Certificates under then existing market conditions, including length of Interest Period, on the effective date of such rate at a price equal to the principal amount thereof. Each 2008 Certificate in a Flexible Mode may evidence interest at a different Flexible Rate and may have an Interest Period within the Flexible Mode which differs from the Interest Period applicable to any 2008 Certificate in a Flexible Mode.

The Trustee, in consultation with the Remarketing Agent, shall take such actions as shall be necessary to distinguish 2008 Certificates having different Flexible Rate Periods, which actions may include obtaining different CUSIP numbers if determined desirable by the Trustee or the Remarketing Agent.

By 1:00 p.m. New York City time on each Rate Determination Date, the Remarketing Agent, with respect to each 2008 Certificate in the Flexible Mode that is subject to adjustment on such Rate Determination Date, shall determine the Flexible Rate for the Interest Period then selected for such 2008 Certificate and shall give notice of the Interest Period, the Purchase Date and the Flexible Rate for such 2008 Certificate, such notice to be given by Electronic means to the Trustee and the Authority. The Remarketing Agent shall make the Flexible Rate and Interest Period available after 2:00 p.m. New York City time on each Rate Determination Date by telephone or Electronic means to any Beneficial Owner or Notice Party other than the Authority requesting such information.

In the event the use of the Book-Entry System is discontinued, in order to receive payment of the Purchase Price of any 2008 Certificate in the Flexible Mode, the Owner of such 2008 Certificate must present such 2008 Certificate to the Trustee, by 12:00 noon New York City time on the applicable Mandatory Purchase Date. Upon receipt of such 2008 Certificate by 12:00 noon New York City time on a Mandatory Purchase Date, the Trustee shall pay the Purchase Price to such Owner by 2:30 p.m. New York City time on such Mandatory Purchase Date.

Section 2.15. Determination of Interest Rates During the Daily Mode and the Weekly Mode. The interest rate for the 2008 Certificates during the Daily Mode or Weekly Mode shall be the rate of interest per annum determined by the Remarketing Agent on and as of the applicable Rate Determination Date as the minimum rate of interest which, in the opinion of the Remarketing Agent under then-existing market conditions, would result in the sale of the 2008 Certificates in the Daily Rate Period or Weekly Rate Period, as applicable, at a price equal to 100% of the principal amount thereof.

(a) During the Daily Mode, the Remarketing Agent shall establish the Daily Rate by 10:00 a.m. New York City time on each Rate Determination Date. The Daily

Rate for any day during the Daily Mode which is not a Business Day shall be the Daily Rate established on the immediately preceding Rate Determination Date. The Remarketing Agent shall make the Daily Rate available no less frequently than once each week by telephone or Electronic means to the Authority, each other Notice Party and any Beneficial Owner requesting such rate.

(b) During the Weekly Mode, the Remarketing Agent shall establish the Weekly Rate by 4:00 p.m. New York City time on each Rate Determination Date. The Weekly Rate shall be in effect during the applicable Weekly Rate Period. The Remarketing Agent shall make the Weekly Rate available no later than 5:00 p.m. New York City time on the Business Day following the Rate Determination Date by telephone or Electronic means to the Authority, each other Notice Party and any Beneficial Owner requesting such rate.

Section 2.16. Determination of Term Rates and Fixed Rates.

(a) Term Rates. The interest rate for the 2008 Certificates in the Term Rate Mode shall be the minimum rate which, in the opinion of the Remarketing Agent, would result in a sale of the 2008 Certificates, under then existing market conditions, at a price equal to 100% of the principal amount thereof on the Rate Determination Date for a Term Rate Period of the duration selected by the Authority, written notice of which shall have been delivered by the Authority to the Remarketing Agent prior to such Rate Determination Date. Notwithstanding the foregoing, if the Authority shall deliver a Favorable Opinion of Special Counsel, the interest rate set for some or all of the affected 2008 Certificates may include a premium or a discount. In no event shall any Term Rate be greater than the Maximum Rate and no Term Rate Period may extend beyond the Maturity Date.

The Term Rate shall be determined by the Remarketing Agent not later than 4:00 p.m. New York City time on the Rate Determination Date and the Remarketing Agent shall make the Term Rate available by telephone or Electronic means after 5:00 p.m. New York City time on the Rate Determination Date to the Authority and each other Notice Party requesting such Term Rate. A copy of each such notice shall be provided to the 2008 Certificate Insurer.

Except as is otherwise provided in Section 2.17 hereof, once the 2008 Certificates are changed to a Term Rate Mode, the 2008 Certificates shall continue in the Term Rate Mode until changed to another Mode in accordance with Section 2.18 hereof. If the Authority shall have failed to select a new Term Rate Period prior to the applicable Rate Determination Date for such new Term Rate Period, the new Term Rate Period shall be the same length as the current Term Rate Period; provided however, that no Term Rate Period may extend beyond the Maturity Date.

(b) Fixed Rates. The Fixed Rate for the 2008 Certificates when being converted from a Short-Term Mode or a Term Rate Mode to the Fixed Rate Mode shall be determined by the Fixed Rate Remarketing Agent in the following manner: not later than 4:00 p.m. New York City time on the applicable Rate Determination Date, the Fixed Rate Remarketing Agent shall determine the Fixed Rate or Fixed Rates, as applicable. The Fixed Rate or Fixed Rates shall be the minimum interest rate(s) which, in the opinion of the applicable Fixed Rate Remarketing Agent, will result in a sale of the 2008 Certificates at a price equal to the principal amount

thereof on the Rate Determination Date. Notwithstanding the foregoing, if the Authority shall deliver a Favorable Opinion of Special Counsel, the interest rate set for some or all of the 2008 Certificates may include a premium or a discount. The Fixed Rate Remarketing Agent shall make the Fixed Rate or Fixed Rates, as applicable, available by telephone or by Electronic means after 5:00 p.m. New York City time on the Rate Determination Date to the Authority and each other Notice Party requesting notice of such Fixed Rate or Fixed Rates. A copy of each such notice shall be provided to the 2008 Certificate Insurer. The Fixed Rate or Rates, as applicable, so established for the 2008 Certificates shall remain in effect until the Maturity Date or Maturity Dates, as applicable, of the 2008 Certificates.

Section 2.17. Alternate Rates. When the 2008 Certificates are in a Daily Mode, a Weekly Mode, a Flexible Rate Mode or a Term Rate Mode, the following provisions shall apply in the event (i) the Remarketing Agent fails or is unable to determine the interest rate for the 2008 Certificates or to determine the interest rate or Flexible Rate Period for the 2008 Certificates within the Flexible Mode, (ii) the method by which the Remarketing Agent determines the interest rate or Interest Period with respect to the 2008 Certificates (or the selection by the Authority of the duration of a Term Rate Period for the 2008 Certificates) shall be held to be unenforceable by a court of law of competent jurisdiction, or (iii) the Remarketing Agent suspends its remarketing effort in accordance with the provisions of the Remarketing Agreement. The provisions set forth in this Section shall continue to apply until such time as the Remarketing Agent (or the Authority, if applicable) resumes making such determinations. In the case of clause (ii) above, the Remarketing Agent (or the Authority, if applicable) shall resume making such determination at such time as there is delivered to the Remarketing Agent or the Authority, as applicable, an opinion of Special Counsel to the effect that there are no longer any legal prohibitions against the Remarketing Agent or Authority, as applicable, making such determinations.

The following shall be the methods by which the interest rates and, in the case of the Flexible Rate Mode and Term Rate Modes, the Interest Periods, shall be determined for the 2008 Certificates or for any Flexible Rate Certificate as to which any of the events described in clauses (i), (ii) or (iii) above shall be applicable. Such methods shall be applicable from and after the date any of the events described in clauses (i), (ii) or (iii) of the immediately preceding paragraph shall become applicable until such time as the events described in clauses (i), (ii) or (iii) of the immediately preceding paragraph are no longer applicable to the 2008 Certificates or any Flexible Rate Certificate. Notwithstanding any other provision herein, these provisions shall not apply with respect to the selection of the length of the Term Rate Period for the 2008 Certificates in a Term Rate Mode if the Authority fails to select the length of the Term Rate Period for the 2008 Certificates for a reason other than as described in clause (ii) of the immediately preceding paragraph.

(a) For Flexible Rate Certificates, the next Interest Period shall be from, and including, the first day following the last day of the current Interest Period for the applicable Flexible Rate Certificates to, but excluding, the next succeeding Business Day, and thereafter the Interest Period for such Flexible Rate Certificate shall commence on each Business Day and extend to, but exclude, the next succeeding Business Day. For each such Interest Period, the interest rate for such Flexible Rate Certificates shall be the applicable Alternate Rate in effect on the Business Day that begins an Interest Period.

(b) If the 2008 Certificates are in a Daily Mode or a Weekly Mode, then the 2008 Certificates shall evidence interest during each subsequent Interest Period for the 2008 Certificates at the Alternate Rate in effect on the first day of such Interest Period.

(c) If the 2008 Certificates are in a Term Rate Mode, then the 2008 Certificates shall automatically convert to a Flexible Rate Mode, with an Interest Period commencing on the first day following the last day of the current Interest Period for the 2008 Certificates to, but excluding, the next succeeding Business Day, and thereafter the Interest Period for the 2008 Certificates shall commence on each Business Day and extend to, but exclude, the next succeeding Business Day. For each such Interest Period, the interest rate for the 2008 Certificates shall be the applicable Alternate Rate in effect at the beginning of each such Interest Period.

Section 2.18. Changes in Mode. Subject to compliance with the provisions set forth in this Section, the Authority may elect to effect a change in Mode with respect the 2008 Certificates (other than the 2008 Certificates in a Fixed Rate Mode); provided that all the 2008 Certificates of any series shall be converted.

(a) Changes to Modes Other Than Fixed Rate Mode. At the option of the Authority, the 2008 Certificates (other than the 2008 Certificates being changed to a Fixed Rate Mode, which shall be governed by the provisions set forth in Section 2.18(d) hereof) may be changed from one Mode to another Mode (other than a Fixed Rate Mode) as set forth below:

(i) Notice by Authority. At least five (5) Business Days (or such shorter time as may be agreed to by the Authority, the Trustee and the Remarketing Agent) prior to the date that notice of the proposed Mode Change Date is required to be given to the Owners by the Trustee as specified below, the Authority shall give written notice to each of the Notice Parties of its intention to effect a change in the Mode from the Mode then prevailing (for purposes of this Section, the "Current Mode") to another Mode (for purposes of this Section, the "New Mode") which shall be specified in such written notice. Such notice to the Notice Parties shall specify the proposed Mode Change Date and shall also include a statement as to whether a Liquidity Facility is expected to be in effect with respect to the 2008 Certificates following such change and, if a Liquidity Facility is expected to be in effect, such notice shall identify the anticipated provider of such Liquidity Facility. If the change is to a Term Rate Mode, such notice shall specify the length of the initial Term Rate Period.

(ii) Notice to Owners. Notice of the proposed change in Mode, unless otherwise specified in Section 2.18(d) hereof, shall be given by the Trustee to the Owners of the 2008 Certificates not less than the 15th day next preceding the applicable Mode Change Date; provided that no notice need be given for a Mode Change Date occurring on the first Business Day following the last day of a Flexible Rate Period or a Term Rate Mode or on a Substitution Date. Such notice shall state the Mode to which the conversion will be made and the proposed Mode Change Date and, if applicable, shall be combined with the notice of mandatory purchase required to be delivered by the Trustee pursuant to Section 3.02 hereof. If the Book-Entry System is no longer in effect, such notice shall also provide information with respect to required delivery of physical 2008

Certificates and procedures for payment of Purchase Price. Notwithstanding any other provision of this Trust Agreement, the Trustee shall not mail such written notice if the 2008 Certificates are being converted from a Flexible Mode until the Trustee shall have received a written confirmation from the Remarketing Agent to the effect that no Interest Period for the 2008 Certificates extends beyond the proposed Mode Change Date. The Trustee shall provide a copy of such notice to the Authority and to each of the other Notice Parties.

(iii) Determination of Interest Rates and Interest Periods. The New Mode shall commence on the Mode Change Date and the interest rate(s), together, in the case of a change to the Flexible Mode, with the Interest Period or Interest Period(s), as applicable, shall be determined by the Remarketing Agent (or the Authority in the case of the Interest Period for the 2008 Certificates being converted to a Term Rate Mode) in the manner provided in Section 2.14, Section 2.15 and Section 2.16 hereof, as applicable.

(iv) Conditions Precedent:

(A) The Mode Change Date shall be: (1) in the case of a change from a Flexible Mode, the next Mandatory Purchase Date for all of the Flexible Rate 2008 Certificates; (2) in the case of a change from a Daily Mode or a Weekly Mode, any Business Day; and (3) in the case of a change from a Term Rate Mode to another Mode, or from a Term Rate Period to a Term Rate Period of a different duration, the Mode Change Date shall be limited to (aa) any Interest Payment Date on which the 2008 Certificates are subject to optional prepayment or (bb) the last Interest Payment Date of the current Term Rate Period. The 2008 Certificates shall be subject to mandatory tender for purchase on such Mode Change Date in accordance with Section 3.02 hereof, and, except as is otherwise provided herein, the 2008 Certificates shall be purchased on the Mode Change Date at a Purchase Price equal to 100% of the principal amount thereof; provided, however, that if the 2008 Certificates are to be purchased on an Interest Payment Date other than the last Interest Payment Date applicable to the 2008 Certificates, and if the 2008 Certificates would otherwise be subject to optional prepayment on such Mode Change Date at a prepayment price of more than 100% of the principal amount thereof, then the 2008 Certificates shall be purchased at a Purchase Price equal to such prepayment price.

(B) If the 2008 Certificates to be converted are in the Flexible Mode, no Interest Period for the 2008 Certificates set after delivery by the Authority to the Remarketing Agent of the notice of the intention to effect a change in Mode shall extend beyond the day preceding the proposed Mode Change Date.

(C) As and to the extent applicable, the Authority shall select a Remarketing Agent for the 2008 Certificates, and shall provide for the delivery of a Liquidity Facility if required.

(D) The Authority shall have obtained and provided to the Trustee the written consent of the 2008 Certificate Insurer to the change in Mode.

(E) The following items shall have been delivered to the Authority, Trustee, the 2008 Certificate Insurer and the Remarketing Agent on or prior to the Mode Change Date:

(1) in the case of a change from any Mode other than a change from a Daily Mode to a Weekly Mode or a change from a Weekly Mode to a Daily Mode, a Favorable Opinion of Special Counsel dated the Mode Change Date;

(2) if there is to be a Liquidity Facility delivered in connection with such change, the items required by Section 3.11 hereof; and

(3) a notice from the Rating Agencies of the rating(s) to be assigned to the 2008 Certificates on such Mode Change Date.

(v) Rescission of Election. The Authority may rescind any election by it to change a Mode in accordance with this Section 2.18(a) as provided in Section 2.18(f) hereof.

(b) Reserved.

(c) Reserved.

(d) Change to Fixed Rate Mode. At the option of the Authority, the 2008 Certificates (other than the 2008 Certificates in a Fixed Rate Mode) may be converted to a Fixed Rate Mode. Any such conversion shall be made as set forth below.

(i) Mode Change Date Provisions. The Mode Change Date shall be:

(A) in the case of a change from a Flexible Mode, the next Mandatory Purchase Date for the Flexible Rate 2008 Certificates of the 2008 Certificates;

(B) in the case of a change from a Daily Mode or a Weekly Mode, any Business Day; and

(C) in the case of a change from a Term Rate Mode, the Mode Change Date shall be limited to (1) any Interest Payment Date on which the 2008 Certificates are subject to optional prepayment or (2) the next Mandatory Purchase Date for the 2008 Certificates being converted, as the case may be. The 2008 Certificates in a Term Rate Mode shall be subject to mandatory tender for purchase pursuant to Section 3.02 hereof and shall be purchased on such Mode Change Date at a Purchase Price equal to 100% of the principal amount thereof; provided that if the 2008 Certificates would otherwise be subject to optional prepayment on such Mode Change Date at a prepayment price of more than 100% of the principal amount thereof, the 2008 Certificates shall be purchased at a Purchase Price equal to such prepayment price.

(ii) Serialization Provisions. Upon conversion of the 2008 Certificates to a Fixed Rate Mode, unless otherwise directed by the Authority, the 2008 Certificates will be converted to Serial Certificates maturing in such years and such principal amounts as correspond to the years and principal amounts set forth in the mandatory Sinking Fund Payment schedule set forth in Section 2.03 hereof

(iii) Notice by Authority. At least 5 Business Days (or such shorter time as may be agreed to by the Trustee, and the Remarketing Agent, if any) prior to the date that notice of the Mode Change Date is required to be given to the Owners by the Trustee as specified in paragraph (iii) below, the Authority shall give written notice to each of the Notice Parties. Such notice shall state that the Mode will be changed to the Fixed Rate Mode, shall set forth the proposed Mode Change Date, and shall be accompanied by the appointment of one or more firms of investment bankers to remarket the 2008 Certificates being changed to the Fixed Rate Mode (such firm or firms of investment bankers being hereinafter referred to as the "Fixed Rate Remarketing Agent"). Together with such notice, the Authority shall file with the Trustee and the 2008 Certificate Insurer a Favorable Opinion of Special Counsel. No conversion to a Fixed Rate Mode shall occur unless the Authority shall also file with the Trustee and the 2008 Certificate Insurer a Favorable Opinion of Special Counsel to the same effect dated the Mode Change Date.

(iv) Notice to Owners. Not less than the 15th day next preceding the Mode Change Date, the Trustee shall mail notice of such proposed change to the Owners of the 2008 Certificates, such notice to state that the Mode on the 2008 Certificates will be changed to a Fixed Rate Mode and to set forth the proposed Mode Change Date. Such notice shall be combined with the notice of mandatory purchase required to be delivered by the Trustee pursuant to Section 3.02 hereof. If the Book-Entry System is no longer in effect, such notice shall also provide information with respect to required delivery of physical 2008 Certificates and the procedures for payment of Purchase Price. Notwithstanding any other provision of this Trust Agreement, the Trustee shall not mail such written notice if the 2008 Certificates are being converted from a Flexible Mode until the Trustee shall have received a written confirmation from the Remarketing Agent to the effect that no Interest Period for the 2008 Certificates extends beyond the proposed Mode Change Date. The Trustee shall provide a copy of such notice to the Authority and to each of the other Notice Parties.

(v) General Provisions Applying to Change to Fixed Rate Mode. The change to a Fixed Rate Mode shall not occur unless the Authority shall have selected a Fixed Rate Remarketing Agent to remarket the 2008 Certificates being changed to the Fixed Rate Mode and the following items shall have been delivered to the Authority and each of the Notice Parties, such items to be delivered on or prior to the Mode Change Date:

- (A) a Favorable Opinion of Special Counsel dated the Mode Change Date;
- (B) the written consent of the 2008 Certificate Insurer to the change in Mode; and

(C) notice from the Rating Agencies of the rating(s) to be assigned the 2008 Certificates on such Mode Change Date.

(vi) Determination of Fixed Rates. The Fixed Rate (or Fixed Rates in the case of Serial Certificates) for the 2008 Certificates shall be established by the applicable Fixed Rate Remarketing Agent on the Rate Determination Date applicable thereto. Such Fixed Rate Remarketing Agent shall set the interest rate or interest rates with respect to the 2008 Certificates in accordance with the provisions set forth in Section 2.16(b) hereof. Such Fixed Rate or Fixed Rates, as applicable, shall remain in effect until the Maturity Date or Maturity Dates, as applicable, of the 2008 Certificates. The applicable Remarketing Agent shall make the Fixed Rate or Rates available by telephone or Electronic means not later than 5:00 p.m., New York City time, on the Rate Determination Date to the Authority, the Trustee and each of the other Notice Parties requesting such notice.

(vii) Modification of Serialization Provisions, Prepayment Provisions and Price. Upon conversion of the 2008 Certificates to a Fixed Rate Mode, the 2008 Certificates shall be subject to the serialization provisions set forth in subsection (ii) above, shall be subject to the optional prepayment and mandatory sinking fund prepayment provisions set forth in Section 2.03 hereof and shall be remarketed at par. Notwithstanding the foregoing or any other provision of this Trust Agreement to the contrary, the Authority may elect to change the serialization provisions, the optional prepayment provisions or the mandatory sinking fund prepayment provisions and/or remarket some or all of the 2008 Certificates at a premium or discount to par if the Authority shall file with the Trustee and the 2008 Certificate Insurer a Favorable Opinion of Special Counsel.

(viii) Rescission of Election. The Authority may rescind any election by it to change a Mode in accordance with this Section 2.18(d) as provided in Section 2.18(f) hereof.

(e) Failure to Satisfy Conditions Precedent to a Mode Change. In the event that the Authority has not withdrawn any election by it to change a Mode as provided herein and the conditions described above in subsections (a), (b), (c) or (d) of this Section, as applicable, have not been satisfied by the applicable Mode Change Date, then the New Mode shall not take effect (although any mandatory purchase shall be made on such date if notice has been sent to the Owners stating that the 2008 Certificates would be subject to mandatory purchase on such date). If the failed change in Mode was from a Flexible Mode, the 2008 Certificates shall remain in the Flexible Mode with interest rates and Interest Periods to be established by the Remarketing Agent on the failed Mode Change Date in accordance with Section 2.14 hereof. If the failed change in Mode was from a Daily Mode, the 2008 Certificates shall remain in the Daily Mode, and if the failed change in Mode was from a Weekly Mode, the 2008 Certificates shall remain in the Weekly Mode, in each case with interest rates established in accordance with the applicable provisions of Section 2.15 hereof on and as of the failed Mode Change Date. If the failed change in Mode was from a Term Rate Mode, then the 2008 Certificates shall stay in the Term Rate Mode for an Interest Period ending on the following Interest Payment Date for the 2008

Certificates in the Term Rate Mode and the interest rate shall be established by the Remarketing Agent on the failed Mode Change Date in accordance with Section 2.16(a) hereof.

(f) Rescission of Election. Notwithstanding anything herein to the contrary, the Authority may rescind any election by it to change a Mode as described above prior to the Mode Change Date by giving written notice thereof to the Notice Parties prior to such Mode Change Date. If the Trustee receives notice of such rescission prior to the time the Trustee has given notice to the Owners of the 2008 Certificates, then such notice of change in Mode shall be of no force and effect. If the Trustee receives notice from the Authority of rescission of a Mode change after the Trustee has given notice thereof to the Owners of the 2008 Certificates, then if the proposed Mode Change Date would have been a Mandatory Purchase Date, such date shall continue to be a Mandatory Purchase Date.

If the proposed change in Mode was from a Flexible Mode, the 2008 Certificates shall remain in the Flexible Mode with interest rates and Interest Periods to be established by the Remarketing Agent on the proposed Mode Change Date in accordance with Section 2.14 hereof. If the proposed change in Mode was from a Daily Mode, the 2008 Certificates shall remain in the Daily Mode, and if the proposed change in Mode was from a Weekly Mode, the 2008 Certificates shall remain in the Weekly Mode, in each case with interest rates established in accordance with the applicable provisions of Section 2.15 hereof on and as of the proposed Mode Change Date. If the proposed change in Mode was from a Term Rate Mode, then the 2008 Certificates shall stay in the Term Rate Mode for an Interest Period ending on the following Interest Payment Date for the 2008 Certificates in the Term Rate Mode and the interest rate shall be established by the Remarketing Agent on the proposed Mode Change Date in accordance with Section 2.16(a) hereof. If the Remarketing Agent is unable to determine the interest rate on the proposed Mode Change Date, the provisions of Section 2.17 shall apply.

(g) Form of Notices. Upon request, the form of any notice from the Trustee to the Owners of the 2008 Certificates required by this Section 2.18 and by Section 3.02 shall be furnished by the Authority to the Trustee.

### ARTICLE III

#### TENDERS OF 2008 CERTIFICATES; REMARKETING

Section 3.01. Optional Tenders of Certificates in a Daily Mode or a Weekly Mode. Subject to Section 3.06 hereof, during any Daily Mode for the 2008 Certificates and during any Weekly Mode for the 2008 Certificates, any 2008 Certificate or portion thereof in a principal amount equal to an Authorized Denomination shall be purchased on any Business Day at a price equal to the Purchase Price, upon delivery of a Tender Notice to the Trustee by the Tender Notice Deadline. Immediately upon receipt of a Tender Notice, the Trustee shall notify the Remarketing Agent and provide the Remarketing Agent with a copy of such Tender Notice. Notwithstanding any other provision of this Trust Agreement to the contrary, the provisions set forth in this Section 3.01 shall not apply to any Certificate in a Delayed Remarketing Period.

Section 3.02. Mandatory Tender for Purchase on Mandatory Purchase Date. The 2008 Certificates shall be subject to mandatory purchase on each Mandatory Purchase Date applicable

to the 2008 Certificates. The Trustee shall give notice of each such mandatory purchase, such notice to be given by mail to the Owners of the 2008 Certificates subject to mandatory purchase no less than 15 days prior to the applicable Mandatory Purchase Date, provided that, if the mandatory purchase is directed as a result of an event of default under the Liquidity Facility, such notice may be given no less than 10 days prior to the applicable Mandatory Purchase Date or as late as the Mandatory Purchase Date. No notice shall be required to be given nor shall any notice be given with respect to any 2008 Certificate in a Flexible Rate Mode in connection with the Mandatory Purchase Date occurring at the end of each Interest Period for the 2008 Certificates. The form of the notice of mandatory purchase shall be provided to the Trustee by the Authority.

Any notice to be given pursuant to this Section 3.02 shall state the Mandatory Purchase Date, shall set forth the Purchase Price applicable on such Mandatory Purchase Date, and shall identify the 2008 Certificates to be purchased. Such notice shall also state that interest on the 2008 Certificates subject to mandatory purchase shall cease to accrue from and after the Mandatory Purchase Date. The failure to mail such notice with respect to any 2008 Certificate shall not affect the validity of the mandatory purchase of any other 2008 Certificate with respect to which notice was so mailed. Any notice mailed will be conclusively presumed to have been given, whether or not actually received by any Owner. If the Book-Entry System is no longer in effect, such notice shall also provide information with respect to required delivery of physical certificates and the procedures for payment of Purchase Price. A copy of any notice delivered by the Trustee pursuant to this Section 3.02 shall also be provided to each of the Notice Parties.

Section 3.03. Purchases of Certificates in Daily Mode, Weekly Mode, Flexible Mode and Term Rate Mode; Payment of Purchase Price; Notices.

(a) On each date on which 2008 Certificates in a Daily Mode, a Weekly Mode, a Flexible Mode or a Term Rate Mode are to be purchased:

(i) the Remarketing Agent shall notify the Trustee and the Authority by 12:00 noon New York City time of the principal amount of such tendered 2008 Certificates it has remarketed and of the principal amount of such tendered 2008 Certificates it has not remarketed, such notice to be provided by Electronic means;

(ii) subject to Section 3.06(b)(ii), the Remarketing Agent shall cause the proceeds of the remarketing by the Remarketing Agent of such tendered 2008 Certificates to be paid to the Trustee in immediately available funds not later than 11:15 a.m., New York City time, on the Purchase Date for such tendered 2008 Certificates;

(iii) the Remarketing Agent shall notify the Trustee by Electronic means not later than 1:00 p.m. New York City time of such information as may be necessary to register and deliver such remarketed 2008 Certificates, such notice to be provided by Electronic means; and

(iv) if the affected 2008 Certificates are no longer in the Book-Entry System, the Trustee shall authenticate new 2008 Certificates for the respective purchasers thereof

which shall be available for pick-up by the Remarketing Agent not later than 2:30 p.m. New York City time.

(b) On each date on which a 2008 Certificate is to be purchased, the Trustee shall draw on the applicable Liquidity Facility, if any, by 12:00 p.m. New York City time in an amount equal to the Purchase Price of all such 2008 Certificates less remarketing proceeds received per Section 3.03(a)(ii) for payment by 3:00 p.m. New York City time and shall notify the 2008 Certificate Insurer of such draw; provided, however, that if the draw is in connection with a Mandatory Purchase Date resulting from a Substitution Date, the draw shall be made on the existing Liquidity Facility that is being replaced. In no event shall the Trustee draw on a Liquidity Facility to pay the Purchase Price of any 2008 Certificate not covered by such Liquidity Facility or to pay the Purchase Price of a 2008 Certificate owned by the Authority or the City.

(c) If the Trustee is notified in writing by a Liquidity Facility Provider that an Automatic Termination Event has occurred, with respect to its Liquidity Facility, then the Trustee shall provide prompt written notice thereof to the Owners of the 2008 Certificates to which such Liquidity Facility relates and shall provide copy of such notice to each of the Notice Parties.

(d) If the Trustee does not have funds in the applicable Remarketing Proceeds Account and the applicable Liquidity Facility Account sufficient to pay the Purchase Price of such 2008 Certificates on any Purchase Date, the Trustee shall give the Authority notice of such insufficiency by 2:45 p.m. New York City time on such Purchase Date.

Section 3.04. Source of Funds for Purchase of 2008 Certificates in Daily Mode, Weekly Mode, Flexible Mode, or Term Rate Mode. By 3:00 p.m. New York City time on the date on which a 2008 Certificate in a Daily Mode, a Weekly Mode, a Flexible Mode or a Term Rate Mode is to be purchased, the Trustee shall purchase tendered 2008 Certificates from the tendering Owners at the applicable Purchase Price by wire transfer in immediately available funds. Except as otherwise provided in the case of the payment of a mandatory purchase price pursuant to Section 3.02, funds for the payment of such Purchase Price shall be derived solely from the following sources in the order of priority indicated and neither the Trustee nor the Remarketing Agent shall be obligated to provide funds from any other source:

(a) immediately available funds on deposit in the Remarketing Proceeds Account excluding funds received from the Authority or the City;

(b) immediately available funds on deposit in the applicable Liquidity Facility Account, if any; and

(c) in the Authority's sole discretion, moneys provided by the Authority that may lawfully be used for such purpose.

Notwithstanding the foregoing, any mandatory purchase of the 2008 Certificates made at the direction of the provider of the Liquidity Facility shall be payable solely from funds drawn under the Liquidity Facility and deposited into the Liquidity Facility Payment Account established

pursuant to Section 4.08 hereof, and any amounts mentioned in clause (a) or clause (c) above shall be used to reimburse the Bank for such payment.

Section 3.05. Delivery of Certificates in Daily Mode, Weekly Mode, Flexible Mode or Term Rate Mode. On each date on which a 2008 Certificate in a Daily Mode, a Weekly Mode, a Flexible Mode or a Term Rate Mode is to be purchased, such 2008 Certificate shall be delivered as follows:

(a) Each 2008 Certificate sold by the Remarketing Agent and for which payment has been received as described in Section 3.04(a) hereof shall be delivered by the Remarketing Agent to the purchaser of such Certificate by 3:00 p.m. New York City time; and

(b) Each 2008 Certificate purchased by the Trustee with moneys described in Section 3.04(b) hereof or purchased from proceeds from the 2008 Liquidity Facility Payment Account shall be registered immediately in the name of the applicable Liquidity Facility Provider or its nominee (which may be the Securities Depository) as provided in Section 2.11(d), if any, on or before 3:00 p.m. New York City time. The Trustee shall not release any Liquidity Provider Certificates unless the Trustee shall have received evidence that the Liquidity Facility has been reinstated to an amount equal to the principal amount of unremarketed 2008 Certificates, including Liquidity Provider Certificates, plus interest at the Maximum Rate for the number of days required under the Liquidity Facility.

(c) Each 2008 Certificate purchased by the Authority with moneys described in Section 3.04(c) hereof shall be registered immediately in the name of the Authority or its nominee on or before 3:00 p.m. New York City time. Any 2008 Certificate so owned by the Authority shall continue to be Outstanding under the terms of this Trust Agreement and be subject to all of the terms and conditions of the Trust Agreement and shall be subject to remarketing by the applicable Remarketing Agent; provided, however, that the Authority shall not be considered a Owner for the purpose of voting such 2008 Certificates under this Trust Agreement.

Section 3.06. Book-Entry Tenders.

(a) Notwithstanding any other provision of this Trust Agreement to the contrary, all tenders for purchase of 2008 Certificates during any period in which 2008 Certificates so tendered are registered in the name of Cede & Co. (or the nominee of any successor Securities Depository) shall be subject to the terms and conditions set forth in the Representations Letter and to any regulations promulgated by DTC (or any successor Securities Depository). For so long as the 2008 Certificates are registered in the name of Cede & Co., as nominee for DTC, the tender option rights of Owners of 2008 Certificates may be exercised only by a Direct Participant of DTC (as such term is described in Schedule A attached to the Representation Letter) acting, directly or indirectly, on behalf of a Beneficial Owner of 2008 Certificates by giving notice of its election to tender 2008 Certificates or portions thereof at the times and in the manner described above. Beneficial Owners will not have any rights to tender 2008 Certificates directly to the Trustee.

Procedures under which a Beneficial Owner may direct a Direct Participant of DTC, or an Indirect Participant of DTC (as such term is described in Schedule A attached to the Representation Letter) acting through a director participant of DTC, to exercise a tender option right in respect of 2008 Certificates or portions thereof in an amount equal to all or a portion of such Beneficial Owner's beneficial ownership interest therein, shall be governed by standing instructions and customary practices determined by such Direct Participant or Indirect Participant. For so long as the 2008 Certificates are registered in the name of Cede & Co., as nominee for DTC, delivery of the 2008 Certificates required to be tendered for purchase shall be effected by the transfer in the Book-Entry System on the applicable Purchase Date of a book-entry credit to the account of the Trustee of a beneficial interest in such 2008 Certificates.

(b) Notwithstanding anything expressed or implied herein to the contrary, so long as the Book-Entry System for the 2008 Certificates is maintained by the Authority:

(i) there shall be no requirement of physical delivery to, or by, the applicable Remarketing Agent or the Trustee of:

(A) any 2008 Certificates subject to optional or mandatory purchase as a condition to the payment of the Purchase Price therefor;

(B) any 2008 Certificates that have become Liquidity Facility Certificates; or

(C) any remarketing proceeds of such 2008 Certificates or Liquidity Facility Certificates to any Owner other than the Securities Depository or its nominee, as applicable; and

(ii) except as provided in (iii) below, the Trustee shall not have any responsibility for paying the Purchase Price of any tendered 2008 Certificate or for remitting remarketing proceeds to any person and such remarketing proceeds may be remitted directly to the Securities Depository by the applicable Remarketing Agent; and

(iii) the Trustee's sole responsibilities in connection with the purchase and remarketing of a tendered 2008 Certificate shall be:

(A) to draw upon the Liquidity Facility (1) in the event the Remarketing Agent for the 2008 Certificates notifies the Trustee as provided herein that any of the 2008 Certificates have not been remarketed on or before the Purchase Date therefor, which draw shall be in an amount equal to the difference between such Purchase Price and any remarketing proceeds received by the Remarketing Agent in connection with a partial remarketing of such 2008 Certificates, or (2) if no such notice is received, the entire amount of the Purchase Price, and to remit the amount so drawn to or upon the order of the Securities Depository for the benefit of the tendering Beneficial Owners;

(B) remit any proceeds derived from the remarketing of a Liquidity Facility Certificate to the applicable Liquidity Facility Provider; and

(C) remit any funds deposited by the Authority for the payment of the Purchase Price of tendered 2008 Certificates to the Securities Depository for the benefit of the tendering Beneficial Owners.

(iv) If the Trustee is party to a custodian or custody agreement with the Liquidity Provider with respect to Liquidity Provider Certificates, the Trustee in its capacity as custodian for the Liquidity Provider shall hold and release Liquidity Provider Certificates in accordance with the terms of such agreement.

Section 3.07. Tender Provisions Applicable Upon Discontinuation of Book-Entry System. If at any time the 2008 Certificates shall no longer be in the Book-Entry System, the procedures set forth below shall apply.

(a) Each 2008 Certificate shall be delivered (with all necessary endorsements) at or before 12:00 noon New York City time on the Purchase Date at the corporate trust office of the Trustee; provided, however, that payment of the Purchase Price shall be made pursuant to this Section 3.07(a) only if the 2008 Certificate so delivered to the Trustee conforms in all respects to the description thereof in the notice provided pursuant to Section 3.01 or Section 3.02 hereof, as applicable. Payment of the Purchase Price with respect to purchases pursuant to the provisions set forth in this Section shall be made to the Owners of tendered 2008 Certificates by wire transfer in immediately available funds by the Trustee by 3:00 p.m. New York City time on the Purchase Date.

(b) The Trustee shall hold all 2008 Certificates properly tendered to it for purchase hereunder as agent and bailee of, and in escrow for the benefit of, the respective Owners of the 2008 Certificates that shall have so tendered such 2008 Certificates until moneys representing the Purchase Price of such 2008 Certificates shall have been delivered to or for the account of or to the order of such Owners.

(c) If a 2008 Certificate to be purchased is not delivered by the Owner to the Trustee by 12:00 noon New York City time on the date in which such 2008 Certificate is to be purchased, the provisions set forth in Section 3.08 hereof shall apply.

(d) If the Trustee is party to a custodian or custody agreement with the Liquidity Provider with respect to Liquidity Provider Certificates, the Trustee in its capacity as custodian for the Liquidity Provider shall hold and release Liquidity Provider Certificates in accordance with the terms of such agreement.

Section 3.08. Certificates Deemed Purchased. If funds sufficient to pay the Purchase Price of any Certificate are held by the Trustee on any Purchase Date, such 2008 Certificate shall be deemed to have been purchased and shall be purchased according to the terms hereof, for all purposes of this Trust Agreement, irrespective of whether or not such 2008 Certificate shall have been delivered to the Trustee, and neither the former Owner of such 2008 Certificate nor any other person shall have any claim thereon, under this Trust Agreement or otherwise, for any amount other than the Purchase Price thereof.

In the event any 2008 Certificate purchased according to the terms hereof shall not be presented to the Trustee, the Trustee shall segregate and hold uninvested the moneys for the

Purchase Price of such 2008 Certificate in trust, without liability for interest thereon, for the benefit of the former Owners of such 2008 Certificate, who shall, except as provided in the following sentence, thereafter be restricted exclusively to such moneys for the satisfaction of any claim for the Purchase Price of such 2008 Certificate. Any moneys which the Trustee shall segregate and hold in trust for the payment of the Purchase Price of any 2008 Certificate and remaining unclaimed for two (2) years after the date of purchase shall be paid to the Authority. After the payment of such unclaimed moneys to the Authority, the former Owner of such 2008 Certificate shall look only to the Authority for the payment thereof.

Section 3.09. Establishment of 2008 Purchase Fund. The Trustee shall create, establish and maintain, a separate fund to be designated as the "2008 Purchase Fund" (the "2008 Purchase Fund"). Moneys deposited in the 2008 Purchase Fund shall be kept separate from and not commingled with other moneys deposited hereunder or with any other moneys of the Authority. The Trustee shall further create, establish and maintain separate accounts within the 2008 Purchase Fund, such separate account to be designated as the "Remarketing Proceeds Account," the "Liquidity Facility Account" and the and the "Authority Account." The 2008 Purchase Fund shall be held in trust solely for the benefit of the Owners of tendered 2008 Certificates and the Trustee shall not have any interest in, claim on or right to, any accounts within the 2008 Purchase Fund or the 2008 Purchase Fund.

(a) Remarketing Proceeds Account. Upon receipt of the proceeds of a remarketing of any 2008 Certificate on the date such 2008 Certificate is to be purchased, the Trustee shall deposit such remarketing proceeds in the Remarketing Proceeds Account, such remarketing proceeds to be applied to the payment of the Purchase Price of such 2008 Certificate. The Authority shall not have any right, title or interest in any of the funds held on deposit in any Remarketing Proceeds Account nor any remarketing proceeds held for any period of time by any Remarketing Agent.

(b) Liquidity Facility Account. Upon receipt of the proceeds of a draw on a Liquidity Facility, the Trustee shall deposit such Liquidity Facility proceeds in the applicable Liquidity Facility Account, such Liquidity Facility proceeds to be applied to the payment of the Purchase Price of the 2008 Certificates to the extent that the moneys on deposit in the Remarketing Proceeds Account shall not be sufficient. Any amounts deposited in a Liquidity Facility Account and not needed for the payment of the Purchase Price of the 2008 Certificates shall be immediately returned to the applicable Liquidity Facility Provider.

(c) Authority Account. Upon receipt of funds from the Authority provided at its sole discretion pursuant to Section 3.04(c) hereof, the Trustee shall deposit such funds in the Authority Account, such funds to be applied to the payment of the Purchase Price of the 2008 Certificates. Any amounts deposited in an Authority Account and not needed for the payment of the Purchase Price of the 2008 Certificates shall be immediately returned to the Authority.

(d) Investment of Funds on Deposit in the 2008 Purchase Funds. Amounts held in the Remarketing Proceeds Account, the Liquidity Facility Account and the

Authority Account shall not be commingled with any other funds held by the Trustee and shall be held uninvested.

(e) Eligible Accounts. Each of the Remarketing Proceeds Account and the Liquidity Facility Account shall meet the requirements of an Eligible Account and be held in the name of the Trustee for the benefit of the Owners. In the event the Remarketing Proceeds Account or the Liquidity Facility Account no longer meet the requirements of an Eligible Account, the Trustee shall promptly (and, in any case, within not more than 30 calendar days) move such account to another financial institution such that each account will meet the requirements of an Eligible Account.

Section 3.10. Insufficient Funds for Tenders; Delayed Remarketing Period.

(a) If sufficient funds are not available to pay the Purchase Price of all tendered 2008 Certificates to be purchased on any Purchase Date (such 2008 Certificates being hereinafter referred to as the "Tendered Certificates"): (i) no purchase of such Tendered Certificates shall be consummated on such Purchase Date; (ii) all such Tendered Certificates shall be returned to the Owners thereof; (iii) all remarketing proceeds shall be returned to the applicable Remarketing Agent for return to the persons providing such moneys; and (iv) such insufficiency and the failure to pay the Purchase Price on any Payment Date shall not constitute an Event of Default under this Trust Agreement.

(b) All such Tendered Certificates shall evidence interest at the Maximum Rate during the period of time (such period of time being hereinafter referred to as a "Delayed Remarketing Period") from and including the applicable Purchase Date to (but not including) the date that all such Tendered Certificates are successfully remarketed.

(c) The Authority may direct the conversion of such Tendered Certificates to a different Mode during a Delayed Remarketing Period in accordance with Section 2.18 hereof; provided that the Authority shall not be required to comply with the notice requirements described in Section 2.18 hereof.

(d) During a Delayed Remarketing Period, the Remarketing Agent shall continue to use its best efforts to remarket such Tendered Certificates. Once the Remarketing Agent has advised the Trustee that it has a good faith belief that it is able to remarket all of such Tendered Certificates, the Trustee shall give written notice by mail to the Owners of such Tendered Certificates not later than five (5) Business Days prior to the proposed Purchase Date, which notice shall state: (i) that such Tendered Certificates will be subject to mandatory tender for purchase on the proposed Purchase Date; (ii) the proposed Purchase Date; (iii) the Mode applicable to such Tendered Certificates from and after the proposed Purchase Date; (iv) the procedures for such mandatory tender for purchase; (v) the Purchase Price applicable to such Tendered Certificates; and (vi) the consequences of a failed remarketing.

(e) During a Delayed Remarketing Period, the Trustee may, upon direction of the Authority, apply amounts on deposit in the 2008 Prepayment Subaccount of the 2008 Principal Account to the prepayment of such Tendered Certificates, as a whole or in part on any Business Day during such Delayed Remarketing Period, at a prepayment price equal to the principal

amount thereof, together with interest accrued thereon to the date fixed for prepayment, without premium. Notwithstanding any provisions herein to the contrary, the Trustee shall give five (5) Business Days' notice of such prepayment to the Owners of the 2008 Certificates to be prepaid.

(f) During a Delayed Remarketing Period, interest on such Tendered Certificates shall be paid to the Owners thereof (i) on the first Business Day of each calendar month occurring during such Delayed Remarketing Period and (ii) on the day after the last day of such Delayed Remarketing Period.

Section 3.11. Liquidity Facility; Alternate Liquidity Facility.

(a) The Authority shall provide a Liquidity Facility approved by the 2008 Certificate Insurer for the 2008 Certificates in a Daily Mode, a Weekly Mode, a Flexible Mode and in a Term Rate Mode. Each such Liquidity Facility (and any Alternate Liquidity Facility provided in replacement thereof) shall provide for the purchase of the 2008 Certificates upon their optional or mandatory tender in accordance with Section 3.01 and Section 3.02 hereof. Any Liquidity Facility (or Alternate Liquidity Facility) shall be a facility provided by a Liquidity Facility Provider in an amount equal to the Required Stated Amount.

(b) If a Liquidity Facility is in effect with respect to the 2008 Certificates, on each date on which a 2008 Certificate is to be purchased, the Trustee, by demand given by Electronic means before 12:30 p.m. New York City time, shall draw on the applicable Liquidity Facility in accordance with the terms thereof so as to receive thereunder by 2:30 p.m. New York City time on such date an amount, in immediately available funds, sufficient, together with the proceeds of the remarketing of such 2008 Certificates on such date, to enable the Trustee to pay the Purchase Price in connection therewith. The proceeds of such draw shall be paid to the Trustee, who shall deposit said proceeds in the applicable Liquidity Facility Account pursuant to Section 3.09(b) hereof or, in the case of the Replacement Liquidity Facility, the 2008 Liquidity Facility Payment Account.

(c) If the Authority shall have delivered a Liquidity Facility to the Trustee in accordance with subsection (a) of this Section, the Authority: (i) shall maintain such Liquidity Facility or an Alternate Liquidity Facility, in an amount equal to the Required Stated Amount prior to its termination; and (ii) shall not voluntarily terminate such Liquidity Facility or any Alternate Liquidity Facility without providing at least 30 days written notice to the Trustee and each of the other Notice Parties.

(d) The Authority may provide an Alternate Liquidity Facility approved by the 2008 Certificate Insurer with respect to the 2008 Certificates on any Business Day not later than the 5<sup>th</sup> Business Day prior to the Expiration Date of the Liquidity Facility then in effect for the 2008 Certificates. The Authority shall give at least 30 days' written notice to the Trustee and each of the Notice Parties of its intent to furnish an Alternate Liquidity Facility to the Trustee, which notice shall specify the nature of such Liquidity Facility, the identity of the Liquidity Facility Provider and the proposed Substitution Date. The Trustee shall give notice of each Mandatory Purchase Date resulting from the proposed delivery of an Alternate Liquidity Facility in accordance with the provisions set forth in Section 3.02 hereof.

(e) On or before the Substitution Date, there shall be delivered to the Trustee: (i) the Alternate Liquidity Facility in substitution for the Liquidity Facility then in effect, (ii) a Favorable Opinion of Special Counsel which shall also be filed with the 2008 Certificate Insurer and (iii) a written Opinion of Counsel for the provider of Alternate Liquidity Facility to the effect that such Alternate Liquidity Facility is a legal, valid, and binding obligation of the provider thereof and covering such other matters as the Authority shall require. Upon the satisfaction of the conditions described in the preceding sentence, the Trustee shall accept such Alternate Liquidity Facility and shall surrender the Liquidity Facility then in effect to the provider thereof on the Substitution Date; provided, however, that if there are insufficient remarketing proceeds to pay the Purchase Price of all 2008 Certificates subject to mandatory purchase on such Substitution Date, the Trustee shall not surrender the Liquidity Facility then in effect until the Trustee shall have drawn upon the existing Liquidity Facility to pay the Purchase Price for the 2008 Certificates subject to mandatory purchase on such Substitution Date. Notwithstanding any other provision of this Trust Agreement to the contrary, if any condition precedent to the substitution of an Alternate Liquidity Facility is not satisfied, the substitution shall not occur but the affected 2008 Certificates shall remain subject to mandatory purchase on the proposed Substitution Date.

(f) In addition to the notice provided pursuant to Section 3.11(d) hereof, the Trustee shall give written notice to the Owners of the 2008 Certificates and each of the Notice Parties of the extension of the Expiration Date of any Liquidity Facility, such notice to be given by mail as promptly as possible upon receipt by the Trustee of notification of such extension.

#### Section 3.12. Appointment of Remarketing Agent.

(a) While the 2008 Certificates are in a Mode which requires the appointment of a Remarketing Agent, the Authority shall appoint a Remarketing Agent for the 2008 Certificates. Any Remarketing Agent shall be approved by the 2008 Certificate Insurer, shall be a member of the National Association of Securities Dealers, Inc., shall have a capitalization of at least \$50,000,000 and shall be authorized by law to perform all the duties set forth herein.

(b) By acceptance of appointment as Remarketing Agent for the 2008 Certificates, the Remarketing Agent shall be deemed to have agreed: (i) to remarket the 2008 Certificates in accordance with the provisions set forth herein; (ii) to keep such books and records as shall be consistent with prudent industry practice; and (iii) to make such books and records available for inspection by each of the Notice Parties at all reasonable times.

(c) The Remarketing Agent may at any time resign and be discharged of the duties and obligations created herein as set forth in the Remarketing Agreement entered into by such Remarketing Agent and the Authority. The Remarketing Agent may suspend its remarketing efforts in accordance with the provisions set forth in Remarketing Agreement entered into by the Remarketing Agent and the Authority. The Remarketing Agent may be removed at any time, at the direction of the Authority in accordance with the provisions set forth in the Remarketing Agreement entered into by the Remarketing Agent and the Authority. The Authority shall provide written notice to each of the Notice Parties of the appointment of any successor Remarketing Agent.

(d) If the Remarketing Agent consolidates with, merges or converts into, or transfers all or substantially all of its assets, to another entity meeting the requirements specified in subparagraph (a) above, the resulting, surviving or transferee entity shall be the successor Remarketing Agent without any further act.

### Section 3.13. Duties of Remarketing Agent.

(a) Each Remarketing Agent shall use its best efforts to offer for sale at the par amount thereof: (i) all 2008 Certificates (or portions thereof to be remarketed) for which notice of optional tender pursuant to Section 3.01 hereof has been given; (ii) all 2008 Certificates that are required to be purchased (A) on a Mandatory Purchase Date described in clauses (i), (ii), (iii), (iv) or (vii) of the definition of Mandatory Purchase Date set forth in Section 1.01 hereof and (B) on a Mandatory Purchase Date described in clause (v) of the definition of Mandatory Purchase Date set forth in Section 1.01 hereof if no Liquidity Facility is required to be delivered by the Authority in connection with such Mandatory Purchase Date; and (iii) all Liquidity Facility Certificates that are: (A) purchased on a Purchase Date described above in clause (i) or (ii) of this Section 3.13, (B) with respect to which the Liquidity Facility Provider has provided notice that it is ready to reinstate the Available Amount, such notice to have been provided to the Authority, the Trustee and the Remarketing Agent, (C) with respect to which an Alternate Liquidity Facility is in effect, or (D) which are being marketed as Fixed Rate Certificates (if the Remarketing Agent shall have been engaged to be the Fixed Rate Remarketing Agent).

If a notice of prepayment or a notice of mandatory purchase shall have been given with respect to a 2008 Certificate, the Remarketing Agent shall provide a copy of such notice to each Person to which such Certificate is remarketed.

Notwithstanding any provision of this Trust Agreement to the contrary, if there shall have occurred and be continuing (i) a Control Event and no other Credit Enhancement Provider Failure or Liquidity Facility Provider Failure, the Remarketing Agent shall continue remarketing 2008 Certificates or (ii) a Control Event and either another Credit Enhancement Provider Failure or a Liquidity Facility Provider Failure, the Remarketing Agent shall not be required to remarket 2008 Certificates.

## ARTICLE IV

### 2008 PAYMENTS; 2008 PROJECT

Section 4.01. 2008 Payments Held in Trust. The 2008 Payments shall be held in trust by the Trustee for the benefit of the Owners from time to time of the 2008 Certificates and each Credit Enhancement Provider, but shall nonetheless be disbursed, allocated and applied solely for the uses and purposes provided herein.

Section 4.02. Deposit of 2008 Payments. The Trustee hereby agrees to establish, maintain and hold in trust a separate fund designated as the 2008 Debt Service Fund, for so long as any 2008 Certificates shall be Outstanding hereunder. All 2008 Payments (except as otherwise provided) received by the Trustee shall be immediately deposited in the 2008 Debt Service Fund and shall be disbursed and applied only as hereinafter provided.

Section 4.03. Establishment and Maintenance of Accounts for Use of Money in the 2008 Debt Service Fund. All money in the 2008 Debt Service Fund shall be set aside by the Trustee in the following respective special accounts within the 2008 Debt Service Fund (each of which is hereby created and each of which the Trustee hereby agrees and covenants to maintain) in the following order of priority:

- (a) 2008 Interest Account (with a 2008 Fees Subaccount therein), and
- (b) 2008 Principal Account (with a 2008 Prepayment Subaccount and a 2008 Sinking Fund Subaccount therein).

All money in each of such accounts and subaccounts shall be held in trust by the Trustee for the benefit of the Owners and each Credit Enhancement Provider and shall be applied, used and withdrawn only for the purposes hereinafter authorized in this Section.

(a) 2008 Interest Account. On the Delivery Date, the Trustee shall deposit in the 2008 Interest Account any Payment Agreement Receipts relating to the 2008 Interest Rate Swap Agreement which the City has directed under the 2008 Interest Rate Swap Agreement to be transferred to the Trustee for deposit in the 2008 Interest Account and any amounts transferred to the Trustee pursuant to Section 2.03 of the 2008 Supplemental Contract for the payment of payments due under the 2008 Interest Rate Swap Agreement. On the Business Day immediately preceding each Interest Payment Date, the Trustee shall set aside from the 2008 Debt Service Fund and deposit in the 2008 Interest Account that amount of money which is equal to the amount of interest evidenced and represented by the 2008 Certificates becoming due and payable on each such Interest Payment Date, unless such amounts are required to be used to reimburse the Bank pursuant to clause (c) below. The Trustee will also apply amounts on deposit in the 2008 Fees Subaccount to pay on behalf of the City, the Payment Agreement Payments required to be paid under the 2008 Interest Rate Swap Agreement and to pay the Remarketing Agent fees as the same shall become due on each due date therefor until such 2008 Fees Subaccount shall be depleted (expected to be on or about November 29, 2008). Investment earnings on amounts on deposit in the 2008 Fees Subaccount shall be transferred to the City for deposit in the Revenue Fund.

No deposit need be made in the 2008 Interest Account if the amount contained therein (exclusive of amounts transferred for the payment of amounts due under the 2008 Interest Rate Swap Agreement) is at least equal to the aggregate amount of interest evidenced and represented by the 2008 Certificates becoming due and payable on such Interest Payment Date.

Except as otherwise provided herein, all money in the 2008 Interest Account shall be used and withdrawn by the Trustee solely for the purpose of paying the interest (including accrued interest evidenced and represented by any 2008 Certificates purchased or prepaid prior to their respective Certificate Payment Date) with respect to the 2008 Certificates as it shall become due and payable, or for reimbursing the Bank and paying the Payment Agreement Payments due under the 2008 Interest Rate Swap Agreement as they shall become due and payable. The Trustee shall be under no obligation to calculate the amount of Payment Agreement Payments due under the 2008 Interest Rate Swap Agreement and shall be entitled to

rely conclusively on the information received by it with respect to the amount of the Payment Agreement Payments due and owing by the City.

(b) 2008 Principal Account. On the Business Day immediately preceding each October 1, commencing on October 1, 2008, the Trustee shall set aside from the 2008 Debt Service Fund and deposit in the 2008 Principal Subaccount an amount of money equal to the principal amount evidenced and represented by the Outstanding Serial Certificates with a Certificate Payment Date of such October 1, and in the 2008 Sinking Fund Subaccount in the 2008 Principal Account the amount of all Sinking Fund Payments required to be made on such October 1.

Amounts to be applied to the optional prepayment of the principal component of the 2008 Certificates pursuant to Section 2.03(c) hereof shall be deposited in the 2008 Prepayment Subaccount of the 2008 Principal Account.

No deposit need be made in the 2008 Principal Account if the amount contained therein is at least equal to the aggregate amount of the principal evidenced and represented by the Outstanding Serial Certificates with a Certificate Payment Date of such October 1 and the amount contained in the 2008 Sinking Fund Subaccount therein is at least equal to the aggregate amount of all Sinking Fund Payments required to be made on such October 1.

All money in the 2008 Principal Account shall be used and withdrawn by the Trustee solely for the purpose of paying the principal evidenced and represented by the Serial Certificates as they shall become due and payable, whether at their respective Certificate Payment Dates or on prior prepayment, and all money in the 2008 Sinking Fund Subaccount of the 2008 Principal Account shall be used and withdrawn by the Trustee only to purchase or to prepay or to pay Term Certificates, and with respect to the 2008 Sinking Fund Subaccount, on each Sinking Fund Payment date, the Trustee shall apply the Sinking Fund Payment required on that date to the prepayment (or payment at Certificate Payment Date, as the case may be) of the Term Certificates upon the notice and in the manner provided in Article II; provided, that at any time prior to giving such notice of such prepayment, the Trustee may, upon the Written Request of the Authority and receipt of moneys sufficient therefor, purchase for cancellation Term Certificates in accordance with Section 2.03(a) hereof, and provided further that so long as the Liquidity Facility is in place, amounts in the 2008 Principal Account shall be used as provided in clause (c) below.

(c) Notwithstanding anything herein to the contrary, all monies in the 2008 Debt Service Fund, including the 2008 Interest Account and the 2008 Principal Account, shall be used to reimburse any draws on the Liquidity Facility pursuant to Section 4.08 hereof.

Section 4.04. Parity Reserve Fund. The Parity Reserve Fund created pursuant to Section 3.04 of the 1997 Trust Agreement is hereby continued. The Trustee hereby agrees and covenants to maintain the Parity Reserve Fund so long as the Contract has not been discharged in accordance with its terms or any 2008 Certificates remain Outstanding hereunder. Amounts on deposit in the Parity Reserve Fund are pledged to the payment of the 1997 Certificates, the 2008 Certificates (including Liquidity Provider Certificates and Subrogated Certificates) and any other obligations hereafter issued in connection with a Supplemental Contract and shall be applied

only for such purposes as hereinafter provided. The Trustee shall deposit in the Parity Reserve Fund from the proceeds of the 2008 Certificates, the amount specified in Section 2.12, such amount being sufficient to cause the balance on deposit in or credited to the Parity Reserve Fund, to be equal to the Reserve Fund Requirement upon delivery of the 2008 Certificates. The Trustee shall deposit in the Parity Reserve Fund such other amounts transferred to the Trustee by the City pursuant to Section 2.04(b)(2) of the Contract, as directed by the Authority in a Written Request of the Authority. Moneys on deposit in the Parity Reserve Fund shall be transferred by the Trustee to the 2008 Debt Service Fund to pay principal and interest evidenced and represented by the 2008 Certificates on any Interest Payment Date or to reimburse the Liquidity Facility Provider for any unreimbursed drawing made under the Liquidity Facility to pay such principal and interest on any such Interest Payment Date in the event amounts on deposit therein are insufficient for such purposes. The Trustee shall also, from such amounts on deposit in the Parity Reserve Fund, transfer or cause to be transferred to any applicable debt service fund established under the 1997 Trust Agreement and under any other trust agreement under which any obligations are issued in connection with a Supplemental Contract, without preference or priority between transfers made pursuant to this sentence and the preceding sentence, and in the event of any insufficiency of such moneys ratably without discrimination or preference, that sum or sums, if any, equal to the amount required to be deposited therein pursuant to such trust agreement under which any obligations are issued in connection with a Supplemental Contract. All investments in the Parity Reserve Fund shall (notwithstanding anything in the 1997 Trust Agreement to the contrary) be valued on or before October 1 of each year at the lesser of the cost or market value thereof. Following such valuation, any moneys on deposit in the Parity Reserve Fund representing an excess of the Reserve Fund Requirement will be transferred by the Trustee to the City for deposit in the Revenue Fund. The Trustee may create such subaccounts in the Parity Reserve Fund as may be necessary or convenient for the purposes of this Section 4.04.

The Reserve Fund Requirement may be provided by one or more surety bonds, insurance policies, or letters of credit as described in the definition of Reserve Fund Requirement ("Reserve Funding Instruments") set forth in the Contract.

Notwithstanding anything to the contrary contained in this Trust Agreement, at any time one or more Reserve Funding Instruments are on deposit in the Parity Reserve Fund, the Trustee shall: (i) withdraw and use all cash, if any, on deposit in the Parity Reserve Fund prior to using and withdrawing any amounts derived from payments under any Reserve Funding Instruments; and (ii) draw on all Reserve Funding Instruments on a pro rata basis based on the draw limit of each Reserve Funding Instrument. Amounts received by the Trustee from the City pursuant to Section 2.04(c)(2) of the Master Contract as a replenishment of amounts withdrawn from the Parity Reserve Fund shall be applied (i) first on a pro rata basis to reimburse draws on any Reserve Funding Instruments and (ii) to replenish cash withdrawn from the Parity Reserve Fund.

In the event the 2008 Certificate Insurance Policy is cancelled in accordance with the Reimbursement Agreement between the Bank and the City, any Reserve Funding Instrument provided by the 2008 Certificate Insurer will be cancelled concurrently therewith.

Section 4.05. Establishment and Application of Costs of Issuance Fund. The Trustee hereby agrees to establish, maintain and hold in trust a separate fund designated as the Costs of Issuance Fund, which fund is hereby created and which fund the Authority hereby agrees to

maintain with the Trustee until November 29, 2008. The Trustee shall deposit to the Costs of Issuance Fund the amounts specified in Section 2.12 hereof. All money in the Costs of Issuance Fund shall be used and withdrawn by the Trustee to pay the Costs of Issuance relating to the 2008 Certificates upon receipt of a Written Request of the Authority filed with the Trustee, each of which shall be sequentially numbered and shall state the person to whom payment is to be made, the amount to be paid, the purpose for which the obligation was incurred and that such payment is a proper charge against said fund. On November 29, 2008, or upon the earlier Written Request of the Authority, any remaining balance in the Costs of Issuance Fund shall be transferred to the City for deposit in the 2008 Debt Service Fund.

Section 4.06. Deposit and Investments of Money in Accounts and Funds. All money held by the Trustee in any of the accounts or funds established pursuant hereto shall be invested in Permitted Investments at the Written Request of the Authority filed with the Trustee which such Permitted Investments shall, as nearly as practicable, mature on or before the dates on which such money is anticipated to be needed for disbursement hereunder, and the Trustee shall have no liability or responsibility for any loss resulting from any investment made in accordance herewith; provided, that if no such Written Request is received by the Trustee, the Trustee shall invest such money in those Permitted Investments described in clause (9) of the definition thereof provided, however, that any such investment shall be made by the Trustee only if, prior to the date on which such investment is to be made, the Trustee shall have received a Written Request of the Authority specifying a specific money market fund and, if no such Written Request of the Authority is so received, the Trustee shall hold such moneys uninvested. Except as otherwise provided herein with respect to the Parity Reserve Fund, all interest or profits received on any money so invested shall be deposited in the 2008 Debt Service Fund.

The Authority acknowledges that to the extent regulations of the Comptroller of the Currency or other applicable regulatory entity grant the Authority the right to receive brokerage confirmations of security transactions as they occur, the Authority specifically waives receipt of such confirmations to the extent permitted by law. The Trustee will furnish the Authority periodic cash transaction statements which include detail for all investment transactions made by the Trustee hereunder.

The Trustee or any of its affiliates may act as principal or agent, sponsor, advisor or manager in connection with any investments made by the Trustee hereunder. For investment purposes, the Trustee may commingle the funds and accounts established hereunder, but shall account for each separately.

The Trustee shall not be liable for any loss from any Permitted Investment acquired, held, or disposed of at the written request of the Authority. Any Permitted Investments that are registered securities shall be registered in the name of the Trustee.

Section 4.07. Assignment to Trustee; Enforcement of Obligations.

(a) The Authority hereby transfers, assigns and sets over to the Trustee all of the 2008 Payments and any and all rights and privileges it has under the Contract, including, without limitation, the right to collect and receive directly all of the 2008 Payments, and any 2008 Payments collected or received by the Authority shall be deemed to be held, and to have been

collected or received, by the Authority as the agent of the Trustee, and shall forthwith be paid by the Authority to the Trustee.

The Trustee also shall, subject to the provisions of the Trust Agreement, take all steps, actions and proceedings required to be taken as provided in any Opinion of Counsel delivered to it, reasonably necessary to maintain in force for the benefit of the Owners of the 2008 Certificates and each Credit Enhancement Provider the Trustee's rights in and priority to the following security granted to it for the payment of the 2008 Certificates: the Trustee's rights as assignee of the 2008 Payments under the Contract and as beneficiary of any other rights to security for the 2008 Certificates which the Trustee may receive in the future.

(b) The Trustee may, in performing the obligations set out in Section 4.07(a) above, rely and shall be protected in acting or refraining from acting upon an Opinion of Counsel furnished by the City.

Section 4.08. 2008 Liquidity Facility Payment Account; Payment of Principal and Interest and Mandatory Purchase Price of the 2008 Certificates. The Trustee shall establish and maintain a separate fund known as the "2008 Liquidity Facility Payment Account" and shall, (i) in each Business Day preceding each Interest Payment Date of the 2008 Certificates, before 5:00 P.M. New York City time on such day, draw on the Liquidity Facility in accordance with the terms thereof so as to receive by 1:00 P.M. New York City time on said Interest Payment Date, an amount, in immediately available funds, equal to the amount of interest and principal, if any (including any Sinking Fund Payment) due on such date, payable with respect to the 2008 Certificates on such Interest Payment Date, and (ii) on each Mandatory Purchase Date, before 12:00 P.M. New York City time draw on the Liquidity Facility in accordance with the terms thereof so as to receive by 3:00 P.M. New York City time on said Interest Payment Date, an amount, in immediately available funds, equal to the amount of the interest and principal due on such date, payable with respect to the 2008 Certificates. All monies held in the 2008 Liquidity Facility Account shall be held uninvested in trust for the benefit of the Owners of the 2008 Certificates.

Funds for the payment of interest and principal, if any, payable with respect to the 2008 Certificates on such Interest Payment Date or Mandatory Purchase Date shall be derived from the immediately available funds on deposit in the 2008 Liquidity Facility Payment Account received from the Bank from draws under the Liquidity Facility, and not from amounts on deposit in the 2008 Interest Account, the 2008 Principal Account or any other account established hereunder. The Liquidity Facility Provider will be reimbursed from such draws from amounts on deposit in the 2008 Interest Account, the 2008 Principal Account or, in the case of a Mandatory Purchase Date, amounts in the Remarketing Account, if any.

If the Liquidity Facility Provider shall make a payment under the Liquidity Facility and is not reimbursed by the Trustee from amounts on deposit in the 2008 Interest Account or 2008 Principal Account or Parity Reserve Fund, its rights with respect to the 2008 Certificates so paid or interest thereon so paid shall be as set forth in Section 10.05 hereof, including its rights to demand payment of such amounts under the 2008 Certificate Insurance Policy. If the Liquidity Facility Provider fails to pay under the Liquidity Facility upon the presentation of a proper draw request by the Trustee and the City has not defaulted under the related Reimbursement

Agreement, to the extent available, amounts on deposit in the 2008 Interest Account, the 2008 Principal Account and the Parity Reserve Fund will be applied to the payment of regularly scheduled interest and principal payable on the applicable Interest Payment Date with respect to the 2008 Certificates.

## ARTICLE V

### COVENANTS OF THE AUTHORITY AND THE TRUSTEE

Section 5.01. Compliance with Trust Agreement. The Trustee will not execute or deliver any 2008 Certificates in any manner other than in accordance with the provisions hereby; and the Authority will not suffer or permit any default by it to occur hereunder, but will faithfully comply with, keep, observe and perform all the agreements and covenants to be observed or performed by it contained herein and in the 2008 Certificates.

Section 5.02. Observance of Laws and Regulations. The Authority and the Trustee will faithfully comply with, keep, observe and perform all valid and lawful obligations or regulations now or hereafter imposed on them by contract, or prescribed by any law of the United States of America or of the State of California, or by any officer, board or commission having jurisdiction or control, as a condition of the continued enjoyment of each and every franchise, right or privilege now owned or hereafter acquired by them, including their right to exist and carry on their respective businesses, to the end that such franchises, rights and privileges shall be maintained and preserved and shall not become abandoned, forfeited or in any manner impaired.

Section 5.03. Accounting Records and Reports. The Trustee will keep or cause to be kept proper books of record and accounts in which complete and correct entries shall be made of all transactions made by the Trustee relating to the receipts, disbursements, allocation and application of the 2008 Payments and the proceeds of the 2008 Certificates, and such books shall be available for inspection by the Authority, at reasonable hours and under reasonable conditions. Not more than 180 days after the close of each Fiscal Year, the Trustee shall furnish or cause to be furnished to the Authority and the 2008 Certificate Insurer a complete financial statement covering receipts, disbursements, allocation and application of 2008 Payments received by the Trustee for such Fiscal Year. The Authority shall keep or cause to be kept such information as required under the Tax Certificate.

Section 5.04. Prosecution and Defense of Suits. The Authority will defend against every suit, action or proceeding at any time brought against the Trustee upon any claim to the extent arising out of the receipt, application or disbursement of any of the 2008 Payments and the proceeds of the 2008 Certificates or to the extent involving the failure of the Authority to fulfill its obligations hereunder; provided that the Trustee or any affected Owner at its election may appear in and defend any such suit, action or proceeding. The Authority will indemnify and hold harmless the Trustee against any and all liability claimed or asserted by any person to the extent arising out of such failure by the Authority, and will indemnify and hold harmless the Trustee against any attorney's fees or other expenses which it may incur in connection with any litigation to which it may become a party by reason of its actions hereunder, except for any loss, cost, damage or expense resulting from the active or passive negligence, willful misconduct or breach of duty by the Trustee. Notwithstanding any contrary provision hereof, this covenant shall

remain in full force and effect even though all 2008 Certificates secured hereby may have been fully paid and satisfied.

Section 5.05. Amendments to Contract. Except for any Supplemental Contract delivered in accordance with the terms of the Contract, the Authority shall not supplement, amend, modify or terminate any of the terms of the Contract, or consent to any such supplement, amendment, modification or termination, without the prior written consent of the Trustee, which such consent shall be given only if (a) such supplement, amendment, modification or termination will not materially adversely affect the interests of the Owners or result in any material impairment of the security hereby given for the payment of the 2008 Certificates, or (b) the Trustee first obtains the written consent of the Owners of a majority in aggregate principal amount evidenced and represented by the 2008 Certificates then Outstanding to such supplement, amendment, modification or termination; provided, that no such supplement, amendment, modification or termination shall reduce the amount of 2008 Payments to be made to the Authority or the Trustee by the City pursuant to the Contract, or extend the time for making such 2008 Payments in any manner that would require the amendment of the Trust Agreement in any manner not in compliance with Section 7.01 hereof, or permit the creation of any lien prior to or on a parity with the lien created hereby on the 2008 Payments without the written consent of all of the Owners of the 2008 Certificates then Outstanding.

Section 5.06. Recording and Filing. The Trustee upon receipt of a Written Request of the Authority, at the expense of the Authority, shall file, record, register, renew, refile and rerecord all such documents, including financing statements (or continuation statements in connection therewith), all in such manner, at such times and in such places as may be required and to the extent permitted by law in order to fully perfect, preserve and protect the security of the Owners and the rights and interests of the Trustee; provided, however, that the Trustee will not be required to execute a special or general consent to service of process, or to qualify as a foreign corporation in connection with any such filing, recording, registration, refile or rerecording in any jurisdiction in which it is not now so subject.

Section 5.07. Further Assurances. Whenever and so often as reasonably requested to do so by the Trustee or any Owner, the Authority will promptly execute and deliver or cause to be executed and delivered all such other and further assurances, documents or instruments, and promptly do or cause to be done all such other and further things as may be necessary or reasonably required in order to further and more fully vest in the Trustee and the Owners all rights, interests, powers, benefits, privileges and advantages conferred or intended to be conferred upon them hereby.

## ARTICLE VI

### THE TRUSTEE

#### Section 6.01. The Trustee.

(a) The Bank of New York Mellon Trust Company, N.A., shall serve as the Trustee for the purpose of receiving all money which the Authority is required to deposit with the Trustee hereunder and for the purpose of allocating, applying and using such money as provided

herein and for the purpose of paying the interest and principal and prepayment premiums, if any, evidenced and represented by the 2008 Certificates presented for payment, and for the purpose of canceling all paid or prepaid 2008 Certificates as provided herein. The Authority agrees that it will at all times maintain a Trustee having a corporate trust office in either San Francisco, California or Los Angeles, California.

(b) The Authority may at any time, unless there exists any Event of Default as defined in Section 8.01 hereof, remove the Trustee initially appointed and any successor thereto and may appoint a successor or successors thereto by an instrument in writing; provided that any successor appointed under this Trust Agreement shall be approved by the 2008 Certificate Insurer and shall be a bank, national banking association with trust powers or trust company doing business and having a principal office in either San Francisco, California or Los Angeles, California, having (or if such bank, national banking association or trust company is a member of a bank holding company system, its bank holding company has) a combined capital (exclusive of borrowed capital) and surplus of at least \$50,000,000 and subject to supervision or examination by federal or state authority. If such bank, national banking association or trust company publishes a report of condition at least annually, pursuant to law or to the requirements of any supervising or examining authority above referred to, then for the purpose of this Section the combined capital and surplus of such bank, national banking association or trust company shall be deemed to be its combined capital and surplus as set forth in its most recent report of condition so published. The Trustee may at any time resign by giving written notice of such resignation to the Authority and by mailing to the Owners notice of such resignation. Upon receiving such notice of resignation, the Authority shall promptly appoint a successor Trustee by an instrument in writing. Any removal or resignation of a Trustee and appointment of a successor Trustee shall become effective only upon the acceptance of appointment by the successor Trustee. If, within 30 days after notice of the removal or resignation of the Trustee no successor Trustee shall have been appointed and shall have accepted such appointment, the removed or resigning Trustee may petition any court of competent jurisdiction for the appointment of a successor Trustee, which court may thereupon, after such notice, if any, as it may deem proper and prescribe and as may be required by law, appoint a successor Trustee having the qualifications required hereby. Any successor trustee shall signify its acceptance of the duties under this Trust Agreement by an instrument in writing provided to the Authority and the Notice Parties.

(c) In the event that the Trustee breaches its obligations hereunder or under any other financing document in connection with the issuance of the 2008 Certificates, at the request of the 2008 Certificate Insurer, the Authority shall remove and replace the Trustee in accordance with the terms of the foregoing clause (b).

(d) The Trustee shall only hold the duties set forth in this Trust Agreement and no duties shall be implied against the Trustee. Following the occurrence of an Event of Default, the Trustee shall exercise such of the rights and powers vested in it hereby, and use the same degree of care and skill in their exercise, as a prudent person would exercise or use under the circumstances in the conduct of his own affairs.

Section 6.02. Liability of the Trustee.

(a) The recitals of facts, agreements and covenants herein and in the 2008 Certificates shall be taken as recitals of facts, agreements and covenants of the Authority, and the Trustee assumes no responsibility for the correctness of the same or makes any representation as to the sufficiency or validity hereof or of the 2008 Certificates, or shall incur any responsibility in respect thereof other than in connection with the rights or obligations assigned to or imposed upon it herein, in the 2008 Certificates or in law or equity. The Trustee shall not be liable in connection with the performance of its duties hereunder except for its own active or passive negligence or willful misconduct.

(b) The Trustee shall not be liable for any error of judgment made in good faith by a responsible officer, unless it shall be proved that the Trustee was negligent in ascertaining the pertinent facts.

(c) The Trustee shall not be liable with respect to any action taken or omitted to be taken by it in good faith in accordance with the direction of the Owners of not less than a majority in aggregate principal amount of the 2008 Certificates at the time Outstanding, relating to the time, method and place of conducting any proceeding for any remedy available to the Trustee, or exercising any trust or power conferred upon the Trustee hereunder.

(d) The Trustee shall be under no obligation to exercise any of the rights or powers vested in it hereby at the request, order or direction of any of the Owners pursuant to the provisions hereof unless such Owners shall have offered to the Trustee reasonable security or indemnity against the costs, expenses and liabilities that may be incurred therein or thereby. The Trustee has no obligation or liability to the Owners for the payment of interest, principal or prepayment premium, if any, evidenced and represented by the 2008 Certificates from its own funds; but rather the Trustee's obligations shall be limited to the performance of its duties hereunder.

(e) The Trustee shall not be deemed to have knowledge of any default hereunder or default under the Contract unless and until it shall have actual knowledge thereof or shall have received written notice thereof at its Corporate Trust Office. Except as otherwise expressly provided herein, the Trustee shall not be bound to ascertain or inquire as to the performance or observance of any of the terms, conditions, covenants or agreements herein or of any of the documents executed in connection with the 2008 Certificates or as to the existence of a default hereunder.

(f) The Trustee shall be entitled to advice of counsel and other professionals concerning all matters of trust and its duty hereunder, but the Trustee shall not be answerable for the professional malpractice of any attorney-at-law or certified public accountant in connection with the rendering of his professional advice in accordance with the terms hereof, if such attorney-at-law or certified public accountant was selected by the Trustee with due care.

(g) The Trustee shall not be concerned with or accountable to anyone for the subsequent use or application of any moneys which shall be released or withdrawn in accordance with the provisions hereof.

(h) Whether or not therein expressly so provided, every provision hereof or of the Contract or any related documents relating to the conduct or affecting the liability of or affording protection to the Trustee shall be subject to the provisions of this article.

(i) The Trustee makes no representation or warranty, express or implied, as to the title, value, design, compliance with specifications or legal requirements, quality, durability, operation, condition, merchantability or fitness for any particular purpose for the use contemplated by the Authority or City of the 2008 Project. In no event shall the Trustee be liable for incidental, indirect, special or consequential damages in connection with or arising from the Contract or this Trust Agreement for the existence, furnishing or use of the 2008 Project.

(j) The Trustee shall be protected in acting upon any notice, requisition, resolution, request, consent, order, certificate, facsimile transmission, electronic mail, report, opinion, bond or other paper or document believed by it to be genuine and to have been signed or presented by the proper party or parties. The Trustee may consult with counsel, who may be counsel of or to the Authority, with regard to legal questions, and the opinion of such counsel shall be full and complete authorization and protection in respect of any action taken or suffered by it hereunder in good faith and in accordance therewith.

(k) Whenever in the administration of its rights and obligations hereunder the Trustee shall deem it necessary or desirable that a matter be established or proved prior to taking or suffering any action hereunder, such matter (unless other evidence in respect thereof be herein specifically prescribed) may, in the absence of bad faith on the part of the Trustee, be deemed to be conclusively proved and established by a Certificate of the Authority, which certificate shall be full warrant to the Trustee for any action taken or suffered under the provisions hereof upon the faith thereof, but in its discretion the Trustee may in lieu thereof accept other evidence of such matter or may require such additional evidence as it may deem reasonable.

(l) No provision of this Trust Agreement shall require the Trustee to expend or risk its own funds or otherwise incur any financial liability in the performance of any of its duties hereunder, or in the exercise of its rights or powers.

(m) The Trustee shall have no responsibility, opinion or liability with respect to any information, statement or recital in any offering memorandum or other disclosure material prepared or distributed with respect to the execution and delivery of the 2008 Certificates.

(n) All immunities, indemnifications and releases from liability granted herein to the Trustee shall extend to the directors, employees, officers and agents thereof.

(o) Any company into which the Trustee may be merged or converted or with which it may be consolidated or any company resulting from any merger, conversion or consolidation to which it shall be a party or any company to which the Trustee may sell or transfer all or substantially all of its corporate trust business, so long as such company shall meet the requirements set forth in Section 6.01 hereof, shall be the successor to the Trustee and vested with all of the title to the trust estate and all of the trusts, powers, discretions, immunities, privileges and all other matters as was its predecessor, without the execution or filing of any paper or further act, anything herein to the contrary notwithstanding.

(p) The Trustee may become the owner or pledgee of any 2008 Certificates with the same rights it would have if it were not Trustee.

(q) The Trustee shall not be considered in breach of or in default in its obligations hereunder or progress in respect thereto in the event of enforced delay (“unavoidable delay”) in the performance of such obligations due to unforeseeable causes beyond its control and without its fault or negligence, including, but not limited to, acts of God or of the public enemy or terrorists, acts of a government, acts of the other party, fires, floods, epidemics, quarantine restrictions, strikes, freight embargoes, earthquakes, explosion, mob violence, riot, inability to procure or general sabotage or rationing of labor, equipment, facilities, sources of energy, material or supplies in the open market, litigation or arbitration involving a party or others relating to zoning or other governmental action or inaction pertaining to the project, malicious mischief, condemnation, and unusually severe weather or delays of suppliers or subcontractors due to such causes or any similar event and/or occurrences beyond the control of the Trustee.

(r) The Trustee agrees to accept and act upon instructions or directions pursuant to this Trust Agreement sent by unsecured e-mail, facsimile transmission or other similar unsecured electronic methods, provided, however, that, the Trustee shall have received an incumbency certificate listing persons designated to give such instructions or directions and containing specimen signatures of such designated persons, which such incumbency certificate shall be amended and replaced whenever a person is to be added or deleted from the listing. If the Authority elects to give the Trustee e-mail or facsimile instructions (or instructions by a similar electronic method) and the Trustee in its discretion elects to act upon such instructions, the Trustee’s understanding of such instructions shall be deemed controlling. The Trustee shall not be liable for any losses, costs or expenses arising directly or indirectly from the Trustee’s reliance upon and compliance with such instructions notwithstanding such instructions conflict or are inconsistent with a subsequent written instruction. The Authority agrees to assume all risks arising out of the use of such electronic methods to submit instructions and directions to the Trustee, including without limitation the risk of the Trustee acting on unauthorized instructions, and the risk of interception and misuse by third parties.

(s) The permissive right of the Trustee to do things enumerated in this Indenture shall not be construed as a duty and it shall not be answerable for other than its negligence or willful misconduct.

Section 6.03. Compensation and Indemnification of Trustee. The Authority covenants to pay to the Trustee from time to time, and the Trustee shall be entitled to, reasonable compensation for all services rendered by it in the exercise and performance of any of the powers and duties hereunder of the Trustee, and the Authority will pay or reimburse the Trustee upon its request for all expenses, disbursements and advances incurred or made by the Trustee in accordance with any of the provisions hereof (including the reasonable compensation and the expenses and disbursements of its counsel and of all persons not regularly in its employ) except any such expense, disbursement or advance as may arise from its negligence, default or willful misconduct. The Authority, to the extent permitted by law, shall indemnify, defend and hold harmless the Trustee against any loss, damages, liability or expense incurred without negligence, default or willful misconduct on the part of the Trustee arising out of or in connection with (i) the acceptance or administration of the trusts created hereby, or the exercise or performance of any

of its powers or duties hereunder, or (ii) any untrue statement or alleged untrue statement of any material fact or omission or alleged omission to state a material fact necessary to make the statements made, in the light of the circumstances under which they were made, not misleading in any official statement or other offering circular utilized in connection with the sale of any of the 2008 Certificates, including costs and expenses (including attorneys' fees) of defending itself against any claim or liability in connection with the exercise or performance of any of its powers hereunder; provided, however, that the Trustee shall in no event condition any draw upon the Liquidity Facility, any request for payment under the Credit Enhancement or any payment to Owners from such draws under the Liquidity Facility or such payments under the Credit Enhancement upon the provision of any indemnification for such performance. The rights of the Trustee and the obligations of the Authority under this Section shall survive the discharge of the 2008 Certificates and the Trust Agreement and the resignation or removal of the Trustee.

## ARTICLE VII

### AMENDMENT OF THE TRUST AGREEMENT

Section 7.01. Amendment of the Trust Agreement. The Trust Agreement and the rights and obligations of the Authority and of the Owners may be amended at any time by a Supplemental Trust Agreement which shall become binding when the written consents of the Owners of a majority in aggregate principal amount of the 2008 Certificates then Outstanding, exclusive of 2008 Certificates disqualified as provided in Section 7.02 hereof, are filed with the Trustee; provided, that before executing any such Supplemental Trust Agreement the Trustee may first obtain at the Authority's expense an Opinion of Counsel that such Supplemental Trust Agreement complies with the provisions of the Trust Agreement, on which opinion the Trustee may conclusively rely. No such amendment shall (1) extend the Certificate Payment Date of, or change the payment dates of, or reduce the rate of interest or principal or prepayment premium, if any, evidenced and represented by any 2008 Certificate without the express written consent of the Owner of such Certificate, or (2) reduce the percentage of 2008 Certificates required for the written consent to any such amendment, or (3) modify any rights or obligations of the Trustee without its prior written assent thereto.

The Trust Agreement and the rights and obligations of the Authority and of the Owners may also be amended at any time by a Supplemental Trust Agreement which shall become binding upon adoption without the consent of any Owners, but only to the extent permitted by law, for any purpose that will not materially adversely affect the interests of the Owners, including (without limitation) for any one or more of the following purposes:

- (a) to add to the agreements and covenants required herein to be performed by the Authority other agreements and covenants thereafter to be performed by the Authority, or to surrender any right or power reserved herein to or conferred herein on the Authority;
- (b) to make such provisions for the purpose of curing any ambiguity or of correcting, curing or supplementing any defective provision contained herein or in regard to questions arising hereunder which the Authority may deem desirable or necessary and not inconsistent herewith;

(c) to add to the agreements and covenants required herein, such agreements and covenants as may be necessary to qualify the Trust Agreement under the Trust Indenture Act of 1939;

(d) to make any amendments or supplements necessary or appropriate to preserve or protect the exclusion of interest evidenced and represented by the 2008 Certificates from gross income for federal income tax purposes under the Code or the exemption of such interest from State of California personal income taxes;

(e) to make such amendments or supplements as may be necessary or appropriate to maintain any then current rating on the 2008 Certificates by any of the Rating Agencies;

(f) to add to the rights of the Trustee;

(g) to modify, alter, amend or supplement this Trust Agreement in any other respect, including amendments which would otherwise be described in the first paragraph of this Section 7.01, if the effective date of such amendments is a date on which all 2008 Certificates affected thereby are subject to mandatory tender for purchase pursuant to the provisions of this Trust Agreement or if notice of the proposed amendments is given to Owners of the affected 2008 Certificates at least thirty (30) days before the proposed effective date of such amendments and, on or before such effective date, such Owners have the right to demand purchase of their 2008 Certificates pursuant to the provisions of this Trust Agreement; or

(h) for any other purpose that does not materially and adversely affect the interests of the Owners of the 2008 Certificates.

Section 7.02. Disqualified Certificates. 2008 Certificates owned or held by or for the account of the Authority or the City shall not be deemed Outstanding for the purpose of any consent or other action or any calculation of Outstanding 2008 Certificates provided in this article, and shall not be entitled to consent to or take any other action provided in this article. Upon request of the Trustee, the Authority and the City shall specify in a certificate to the Trustee those 2008 Certificates disqualified pursuant to this Section and the Trustee may conclusively rely on such certificate.

Section 7.03. Endorsement or Replacement of Certificates After Amendment. After the effective date of any action taken as hereinabove provided, the Authority may determine that the 2008 Certificates may bear a notation by endorsement in form approved by the Authority as to such action, and in that case upon demand of the Owner of any Outstanding 2008 Certificates and presentation of such Owner's 2008 Certificate for such purpose at the Corporate Trust Office of the Trustee a suitable notation as to such action shall be made on such Certificate. If the Authority shall so determine, new 2008 Certificates so modified as, in the opinion of the Authority, shall be necessary to conform to such action shall be prepared and executed, and in that case upon demand of the Owner of any Outstanding 2008 Certificate a new 2008 Certificate or Certificates shall be exchanged at the Corporate Trust Office of the Trustee without cost to

each Owner for its 2008 Certificate or 2008 Certificates then Outstanding upon surrender of such Outstanding 2008 Certificates.

Section 7.04. Amendment by Mutual Consent. Subject to Section 10.02 hereof, the provisions of this article shall not prevent any Owner from accepting any amendment as to the particular 2008 Certificates held by him, provided that due notation thereof is made on such 2008 Certificates.

Section 7.05. Consent of Liquidity Facility Provider. Notwithstanding anything to the contrary contained in this Trust Agreement, this Trust Agreement may not be amended without the prior written consents of the Liquidity Facility Provider and 2008 Certificate Insurer.

Section 7.06. Notice. The Trustee shall give notice to the Rating Agencies of any amendments pursuant to this Article VII.

## ARTICLE VIII

### EVENTS OF DEFAULT AND REMEDIES OF OWNERS

Section 8.01. Events of Default: Acceleration; Waiver of Default. If an Event of Default (as that term is defined in the Contract) shall happen, then such Event of Default shall constitute a default hereunder, and in each and every such case during the continuance of such Event of Default the Trustee after receiving indemnification to its satisfaction or the Owners of not less than a majority in aggregate principal amount of the 2008 Certificates then Outstanding shall exercise the remedies provided to the Authority in the Contract; provided, that nothing contained herein shall affect or impact the right of action of any Owner to institute suit directly against the City to enforce payment of the obligation evidenced and represented by such Owner's 2008 Certificates. In determining whether a payment default has occurred hereunder, or whether a payment on the 2008 Certificates has been made hereunder, no effect shall be given to payments made under the 2008 Certificate Insurance Policy. Upon the occurrence of any Event of Default, the Trustee shall give notice to the Credit Enhancement Provider and the Liquidity Facility Provider.

Section 8.02. Other Remedies of the Trustee. The Trustee shall have the right—

(a) by mandamus or other action or proceeding or suit at law or in equity to enforce the Authority's rights under the Contract against the City or any director, officer or employee thereof, and to compel the City or any such director, officer or employee to perform or carry out its or his duties under law and the agreements and covenants required to be performed by it or him contained in the Contract;

(b) by suit in equity to enjoin any acts or things which are unlawful or violate the rights of the Trustee; or

(c) by suit in equity upon the happening of any Event of Default hereunder to enforce the Authority's rights under the Contract to require the City and its directors, officers and employees to account as the trustee of an express trust.

Section 8.03. Non-Waiver. A waiver of any default or breach of any duty or contract by the Trustee shall not affect any subsequent default or breach of duty or contract or impair any rights or remedies on any such subsequent default or breach of duty or contract. No delay or omission by the Trustee to exercise any right or remedy accruing upon any default or breach of duty or contract shall impair any such right or remedy or shall be construed to be a waiver of any such default or breach of duty or contract or any acquiescence therein, and every right or remedy conferred upon the Trustee by law or by this article may be enforced and exercised from time to time and as often as shall be deemed expedient by the Trustee.

If any action, proceeding or suit to enforce any right or to exercise any remedy is abandoned or determined adversely to the Trustee, the Trustee, and the City shall be restored to their former positions, rights and remedies as if such action, proceeding or suit had not been brought or taken.

Section 8.04. Remedies Not Exclusive. No remedy herein conferred upon or reserved to the Trustee or the Owners is intended to be exclusive of any other remedy, and each such remedy shall be cumulative and shall be in addition to every other remedy given hereunder or now or hereafter existing in law or in equity or by statute or otherwise and may be exercised without exhausting and without regard to any other remedy conferred by law.

Section 8.05. No Liability by the City to the Owners. Except for the payment when due of the 2008 Payments and the performance of the other agreements and covenants required to be performed by it contained in the Contract, the City shall not have any obligation or liability to the Owners with respect to the Trust Agreement or the preparation, execution, delivery or transfer of the 2008 Certificates or the disbursement of the 2008 Payments by the Trustee to the Owners, or with respect to the performance by the Trustee of any right or obligation required to be performed by it contained herein.

Section 8.06. No Liability by the Trustee to the Owners. Except as expressly provided herein, the Trustee shall not have any obligation or liability to the Owners with respect to the payment when due of the 2008 Payments by the City, or with respect to the performance by the City of the other agreements and covenants required to be performed by its contained in the Contract.

Section 8.07. Control of Remedies by Credit Enhancement Provider or Liquidity Facility Provider. As long as no Control Event has occurred, notwithstanding anything in this Trust Agreement to the contrary, the 2008 Certificate Insurer shall have the right to direct all remedies upon the occurrence of an Event of Default. If a Control Event has occurred and the Bank's Credit Enhancement is in effect, notwithstanding anything in this Trust Agreement to the contrary, the Bank shall have the right to direct all remedies upon the occurrence of an Event of Default. If a Control Event has occurred and the Bank's Credit Enhancement is no longer in effect, notwithstanding anything in this Trust Agreement to the contrary, the Liquidity Facility Provider shall have the right to direct all remedies upon the occurrence of an Event of Default.

Notwithstanding the foregoing, if a Liquidity Facility is in effect, and the Provider thereof has failed to honor its payment obligations under the Liquidity Facility in respect of the purchase price of Certificates upon tender thereof, fifty-one percent (51%) of the Certificate

holders of the Certificates enhanced by such Liquidity Facility (excluding Certificates owned by the City and Bank Certificates), shall have the right at any time, by an instrument or instruments in writing executed and delivered to the Trustee, to direct the method and place of conducting all proceedings to be taken in connection with the enforcement of such payment obligations; provided that such direction shall be in accordance with applicable law.

Section 8.08. Application of Funds in case of an Event of Default. All moneys received by the Trustee pursuant to any right given or action taken under the provisions of this Article VIII shall be deposited into the 2008 Debt Service Fund and shall be applied by the Trustee in the following order upon presentation and surrender of the several 2008 Certificates: First, Costs and Expenses: to the payment of reasonable fees and expenses of the Trustee (including reasonable fees and disbursements of its counsel) incurred in and about the performance of its powers and duties under this Trust Agreement; Second, Interest: to the payment to the persons entitled thereto of all installments of interest then due or which have accreted in the order of the maturity of such installment, and, if the amount available shall not be sufficient to pay in full any installment or installments maturing on the same date, then to the payment thereof ratably, according to the amounts due thereon, to the persons entitled thereto, without any discrimination or preference; and Third, Principal: to the payment to the persons entitled thereto of the unpaid principal of any 2008 Certificates that shall have become due, whether at maturity or by call for prepayment, in the order of their due dates, with interest on the overdue principal and interest at a rate equal to the rate paid with respect to the 2008 Certificates and, if the amount available shall not be sufficient to pay in full all the amounts due with respect to the 2008 Certificates on any date, together with such interest, then to the payment thereof ratably, according to the amounts of principal due on such date to the persons entitled thereto, without any discrimination or preference.

## ARTICLE IX

### DEFEASANCE

Section 9.01. Discharge of Trust Agreement. When the obligations of the City under the Contract shall cease pursuant to Article VI of the Contract (except for the right of the Trustee and the obligation of the City to have the money and Federal Securities mentioned therein applied to the payment of 2008 Payments as therein set forth) and (i) the 2008 Certificates are in Fixed Rate Mode at the time moneys or Federal Securities are deposited, (ii) the deposit of money and Federal Securities is sufficient to pay the 2008 Certificates at the Maximum Rate to the earlier of the first possible tender or redemption date, (iii) the City shall have received a Rating Confirmation Notice on any 2008 Certificate that shall remain Outstanding following such redemption, and (iv) all other sums payable hereunder, including to the 2008 Certificate Insurer and Bank, have been paid, then and in such case the obligations created by this Trust Agreement shall thereupon cease, terminate and become void except for the right of the Owners and the obligation of the Trustee to apply such moneys and Federal Securities to the payment of the 2008 Certificates as herein set forth and the right of the Trustee to collect any fees or expenses due hereunder and the Trustee shall turn over to the City, as an overpayment of 2008 Payments, all balances remaining in any other funds or accounts other than moneys and Federal Securities held for the payment of the 2008 Certificates at maturity or on prepayment, which moneys and Federal Securities shall continue to be held by the Trustee in trust for the benefit of

the Owners and shall be applied by the Trustee to the payment, when due, of the principal and interest and premium if any represented by the 2008 Certificates, and after such payment, this Trust Agreement shall become void.

If moneys or Federal Securities are deposited with and held by the Trustee as hereinabove provided, the Trustee shall mail a notice, first-class postage prepaid, to the Owners at the addresses listed on the registration books kept by the Trustee pursuant to Section 2.08 hereof, stating that (a) moneys or Federal Securities are so held by it, and (b) that this Trust Agreement has been released in accordance with the provisions of this Section.

In connection with any defeasance of any of the 2008 Certificates pursuant to this Article, the 2008 Certificate Insurer (or, if a Control Event has occurred, the Bank) shall receive (i) a Favorable Opinion of Special Counsel and (ii) an escrow agreement and an Opinion of Counsel regarding the validity and enforceability of the escrow agreement, such escrow agreement shall provide that: (1) any substitution of securities shall require a verification by an independent certified public accountant and the prior written consent of the 2008 Certificate Insurer; (2) the Authority will not exercise any optional redemption of the 2008 Certificates secured by the escrow agreement or any other redemption other than mandatory sinking fund redemptions unless (a) the right to make any such redemption has been expressly reserved in the escrow agreement and such reservation has been disclosed in detail in the official statement for the refunding obligations, and (b) as a condition of any such redemption there shall be provided to the 2008 Certificate Insurer (or, if a Control Event has occurred, the Bank) a verification of an independent certified public accountant as to the sufficiency of escrow receipts without reinvestment to meet the escrow requirements remaining following such redemption; and (3) the Authority shall not amend the escrow agreement or enter into a forward purchase agreement or other agreement with respect to rights in the escrow without the prior written consent of the 2008 Certificate Insurer (or, if a Control Event has occurred, the Bank).

Notice of discharge of the Trust Agreement under this Article IX shall be provided to the Rating Agencies by the Trustee.

Notwithstanding the provisions of this Section: (i) amounts of principal of and interest on any 2008 Certificates paid by the 2008 Certificate Insurer under the 2008 Certificate Insurance Policy shall not be deemed to have been paid for purposes of this Trust Agreement and such 2008 Certificates shall remain Outstanding and such amounts shall continue to be due and owing until paid; and (ii) this Trust Agreement shall not be discharged unless all amounts due or to become due to the 2008 Certificate Insurer hereunder or under the 2008 Certificate Insurance Policy have been paid in full or duly provided for.

Section 9.02. Deposit of Money or Securities with Trustee. Whenever in this Trust Agreement or the Contract it is provided or permitted that there be deposited with or held in trust by the Trustee money or securities (certified to be sufficient by a report of an Independent Certified Public Accountant) in the necessary amount to pay or prepay any 2008 Certificates, the money or securities to be so deposited or held may include money or securities held by the Trustee in the funds and accounts established pursuant to this Trust Agreement and shall be --

(a) lawful money of the United States of America in an amount equal to the principal amount represented by such 2008 Certificates and all unpaid interest represented thereby to maturity, except that, in the case of 2008 Certificates which are to be prepaid prior to maturity and in respect of which notice of such prepayment shall have been given as in Article II provided or provision satisfactory to the Trustee shall have been made for the giving of such notice, the amount to be deposited or held shall be the principal amount plus accrued interest to such date of prepayment plus a prepayment premium, if any, represented by such 2008 Certificates; or

(b) Federal Securities which are not subject to redemption except by the holder thereof prior to maturity (including any such securities issued or held in book-entry form) or municipal obligations which have been defeased under irrevocable escrow instructions with Federal Securities and which are rated in the highest rating category by the Rating Agencies, the principal of and interest on which when due will provide, in its opinion of an Independent Certified Public Accountant, delivered to the Trustee, money sufficient to pay the principal plus prepayment premium, if any, plus all accrued interest to maturity or to the prepayment date, as the case may be, represented by the 2008 Certificates to be paid or prepaid, as such amounts become due, provided that, in the case of 2008 Certificates which are to be prepaid prior to the maturity thereof, notice of such prepayment shall have been given as in Article II provided or provision satisfactory to the Trustee shall have been made for the giving of such notice;

provided, in each case, that the Trustee shall have been irrevocably instructed (by the terms of this Trust Agreement and the Contract or by Written Request of the City) to apply such money to the payment of such principal plus prepayment premium, if any, plus interest represented by such 2008 Certificates.

Section 9.03. Unclaimed Money. Anything contained herein to the contrary notwithstanding, any money held by the Trustee in trust for the payment and discharge of any of the 2008 Certificates which remains unclaimed for two years after the date when such 2008 Certificates have become due and payable, either at their stated Certificate Payment Dates or by call for prepayment prior to Certificate Payment Date, if such money was held by the Trustee at such date, or for two years after the date of deposit of such money if deposited with the Trustee after the date when such Certificates have become due and payable, shall be repaid by the Trustee to the City as its absolute property free from trust, and the Trustee shall thereupon be released and discharged with respect thereto and the Owners shall look only to the City for the payment of the 2008 Payments evidenced and represented by such 2008 Certificates; provided, however, that before being required to make any such payment to the City, the Trustee shall, at the request of and at the expense of the City, cause to be mailed to all Owners and the Securities Depositories and the Information Services a notice that such money remains unclaimed and that, after a date named in such notice, which date shall not be less than 30 days after the date of the first publication of each such notice, the balance of such money then unclaimed will be returned to the City.

## ARTICLE X

### CERTIFICATE INSURANCE PROVISIONS

Section 10.01. Payment Under the 2008 Certificate Insurance Policy. The payment when due of the principal and interest with respect to the 2008 Certificates shall be insured by the 2008 Certificate Insurance Policy. As long as the 2008 Certificate Insurance Policy shall be in full force and effect, the Authority and the Trustee agree to comply with the following provisions with respect to the 2008 Certificates:

(a) In the event that, on the second Business Day, and again on the Business Day, prior to an interest payment date for the 2008 Certificates the Trustee has not received sufficient moneys to pay all of the principal and interest with respect to the 2008 Certificates (including amounts required to reimburse the Bank for the payment of such principal and interest) due on the second following, or following, Business Day, as the case may be, the Trustee shall promptly on such Business Day moneys are not received, notify the 2008 Certificate Insurer or its designee on the same Business Day by telephone, electronic mail or facsimile, confirmed in writing by registered or certified mail of the amount of the deficiency, the obligations which such deficiency is applicable and whether such obligations will be deficient as to principal or interest or both. If the deficiency is cured in whole or in part prior to or on the interest payment date, the Trustee shall so notify the 2008 Certificate Insurer or its designee.

(b) The Trustee shall, after giving notice to the 2008 Certificate Insurer, as provided above, make available to the 2008 Certificate Insurer and, at the 2008 Certificate Insurer's direction, to any fiscal agent, the registration books of the Authority maintained by the Trustee and all records relating to the funds maintained under the documentation.

(c) The Trustee shall provide the 2008 Certificate Insurer and any fiscal agent with a list of registered owners of the 2008 Certificates entitled to receive principal or interest payments from the 2008 Certificate Insurer under the terms of the 2008 Certificate Insurance Policy, and shall make arrangements with the 2008 Certificate Insurer, the fiscal agent or another designee of the 2008 Certificate Insurer to (i) mail checks or drafts to the registered owners of the 2008 Certificates (including the Bank) entitled to receive full or partial interest payments from the 2008 Certificate Insurer and (ii) pay principal upon the 2008 Certificates surrendered to the 2008 Certificate Insurer, the fiscal agent or another designee of the 2008 Certificate Insurer by the registered owners of the 2008 Certificates (including the Bank) entitled to receive full or partial principal payments from the 2008 Certificate Insurer.

(d) The Trustee shall, at the time it provides notice to the 2008 Certificate Insurer of any deficiency pursuant to clause (a) above, notify registered owners of the 2008 Certificates (including the Bank) entitled to receive the payment of principal or interest thereon from the 2008 Certificate Insurer (i) as to such deficiency and its entitlement to receive principal or interest, as applicable, (ii) that the 2008 Certificate Insurer will remit to them all or a part of the interest payments due on the related payment date upon proof of its entitlement thereto and delivery to the 2008 Certificate Insurer or any fiscal agent, in form satisfactory to the 2008 Certificate Insurer, of an appropriate assignment of the registered owner's right to payment, (iii) that, if they are entitled to receive partial payment of principal from the 2008 Certificate Insurer,

they must surrender the related the 2008 Certificates for payment first to the Trustee, which will note on such the 2008 Certificates the portion of the principal paid by the Trustee and second to the 2008 Certificate Insurer or its designee, together with an appropriate assignment, in form satisfactory to the 2008 Certificate Insurer, to permit ownership of the 2008 Certificates to be registered in the name of the 2008 Certificate Insurer, which will then pay the unpaid portion of principal, and (iv) that, if they are entitled to receive full payment of principal from the 2008 Certificate Insurer, they must surrender the 2008 Certificates for payment to the 2008 Certificate Insurer or its designee, rather than the Trustee, together with the an appropriate assignment, in form satisfactory to the 2008 Certificate Insurer, to permit ownership of the 2008 Certificates to be registered in the name of the 2008 Certificate Insurer.

(e) In addition, if the Trustee has written notice that any Owner of a 2008 Certificate (including the Bank) has been required to disgorge payments of principal or interest with respect to the 2008 Certificates to the City or its trustee in bankruptcy or creditors or others pursuant to a final judgment by a court of competent jurisdiction that such payment constitutes a voidable preference to such Owner within the meaning of any applicable bankruptcy laws, then the Trustee shall notify the 2008 Certificate Insurer or its designee of such fact by telephone or telegraphic notice, confirmed in writing by registered or certified mail.

(f) The Trustee is hereby irrevocably designated, appointed, directed and authorized to act as attorney-in-fact for Owners of the 2008 Certificates (including the Bank) as follows:

(i) If and to the extent there is a deficiency in amounts required to fully pay interest on the 2008 Certificates, the Trustee shall (i) execute and deliver to the 2008 Certificate Insurer, in form satisfactory to the 2008 Certificate Insurer, an instrument appointing the 2008 Certificate Insurer as agent for such Owners in any legal proceeding related to the payment of such interest and an assignment to the 2008 Certificate Insurer of the claims for interest to which such deficiency relates and which are paid by the 2008 Certificate Insurer, (ii) receive as designee of the respective Owners (and not as Trustee) in accordance with the tenor of the 2008 Certificate Insurance Policy payment from the 2008 Certificate Insurer with respect to the claims for interest so assigned and (iii) disburse the same to such respective Owners; and

(ii) If and to the extent of a deficiency in amounts required to pay principal with respect to the 2008 Certificates, the Trustee shall (i) execute and deliver to the 2008 Certificate Insurer, in form satisfactory to the 2008 Certificate Insurer, an instrument appointing the 2008 Certificate Insurer as agent for such Owner in any legal proceeding relating to the payment of such principal and an assignment to the 2008 Certificate Insurer of any of the 2008 Certificates surrendered to the 2008 Certificate Insurer of so much of the principal thereof as has not previously been paid or for which moneys are not held by the Trustee and available for such payment (but such assignment shall be effective only if payment from the 2008 Certificate Insurer is received), (ii) receive as designee of the respective Owners (and not as Trustee) in accordance with the tenor of the 2008 Certificate Insurance Policy payment therefor from the 2008 Certificate Insurer and (iii) disburse the same to such Owners.

(g) In the event that the Trustee shall have made a claim under the 2008 Certificate Insurance Policy with respect to principal and/or interest due on any payment date with respect to the 2008 Certificates and the Bank shall have paid on such payment date a draw made by the Trustee on the Bank's Credit Enhancement for such principal and/or interest, then, notwithstanding anything to the contrary, the amount paid by the 2008 Certificate Insurer with respect to the 2008 Certificates (the "Held Amount") on such payment date pursuant to such claim under the 2008 Certificate Insurance Policy shall be held uninvested by the Trustee until the Trustee shall have received notice from the 2008 Certificate Insurer that: (A) the Bank has directed the 2008 Certificate Insurer to reimburse the Bank for such draw pursuant to the Reimbursement Agreement between the Bank and the City, in which case the Trustee shall immediately pay the Held Amount to the Bank; or (B) the Bank has failed to direct the 2008 Certificate Insurer to reimburse the Bank for such draw within the time period set forth in the Reimbursement Agreement between the Bank and the City, in which case the Trustee shall immediately return the Held Amount to the 2008 Certificate Insurer. If the Held Amount is returned to the 2008 Certificate Insurer, the Authority shall pay interest at the Reimbursement Rate on such Held Amount from the date paid by the 2008 Certificate Insurer until such return to the 2008 Certificate Insurer. Payments with respect to claims for interest and principal with respect to the 2008 Certificates disbursed by the Trustee from proceeds of the 2008 Certificate Insurance Policy shall not be considered to discharge the obligation of the Authority with respect to such 2008 Certificates, and the 2008 Certificate Insurer shall become the Owner of such unpaid 2008 Certificates and claims for the interest in accordance with the tenor of the assignment made to it under the provisions of this Section 10.01 or otherwise.

(h) Irrespective of whether any such assignment is executed and delivered, the Authority and the Trustee hereby for the benefit of the 2008 Certificate Insurer that:

(i) to the extent the 2008 Certificate Insurer makes payments, directly or indirectly (as by paying through the Trustee), on account of the principal or interest with respect to the 2008 Certificates, the 2008 Certificate Insurer will be subrogated to the rights of the Owners of the 2008 Certificates to receive the amount of such principal and interest, with interest thereon as provided and solely from the sources stated in this Trust Agreement and the 2008 Certificates, and

(ii) they will accordingly pay to the 2008 Certificate Insurer the amount of such principal and interest, with interest thereon as provided in this Trust Agreement and the 2008 Certificates, but only from the sources and in the manner provided herein for the payment of the principal and interest with respect to the 2008 Certificates to Owners, and will otherwise treat the 2008 Certificate Insurer as the Owner of such rights to the amount of such principal and interest.

(i) The Authority hereby agrees to pay or reimburse the 2008 Certificate Insurer, to the extent permitted by law, (A) all amounts paid by the 2008 Certificate Insurer under the terms of the 2008 Certificate Insurance Policy, and (B) any and all charges, fees, costs and expenses which the 2008 Certificate Insurer may reasonably pay or incur, including, but not limited to, fees and expenses of attorneys, accountants, consultants and auditors and reasonable costs of investigations, in connection with (i) any accounts established to facilitate payments under the 2008 Certificate Insurance Policy, (ii) the administration, enforcement, defense or preservation

of any rights in respect of this Trust Agreement or any other financing document, including defending, monitoring or participating in any litigation or proceeding (including any bankruptcy proceeding in respect of the Authority or any affiliate thereof) relating to this Trust Agreement or any other financing document, any party to this Trust Agreement or any other financing document or the transaction contemplated by this Trust Agreement or any other financing documents, (iii) the foreclosure against, sale or other disposition of any collateral securing any obligations under this Trust Agreement or any other financing document, or the pursuit of any remedies under this Trust Agreement or any other financing document, to the extent such costs and expenses are not recovered from such foreclosure, sale or other disposition, or (iv) any amendment, waiver or other action with respect to, or related to, this Trust Agreement or any other financing document whether or not executed or completed; costs and expenses shall include a reasonable allocation of compensation and overhead attributable to time of employees of the 2008 Certificate Insurer spent in connection with the actions described in clauses (ii) - (iv) above. In addition, the 2008 Certificate Insurer reserves the right to charge a reasonable fee as a condition to executing any amendment, waiver or consent proposed in respect of this Trust Agreement or any other financing document. The Authority will pay interest on the amounts owed in this paragraph from the date of any payment due or paid, at the per annum rate of interest publicly announced from time to time by JP Morgan Chase Bank, National Association at its principal office in New York, New York as its prime lending rate (any change in such prime rate of interest to be effective on the date such change is announced by JPMorgan Chase Bank, National Association) plus three percent (3%) per annum (the 'Reimbursement Rate'). The Reimbursement Rate shall be calculated on the basis of the actual number of days elapsed over a 360-day year. In the event JPMorgan Chase Bank ceases to announce its prime rate publicly, the prime rate shall be the publicly announced prime rate or base lending rate of such national bank, as the 2008 Certificate Insurer shall specify.

(j) In addition to any and all rights of reimbursement, subrogation and any other rights pursuant hereto or under law or in equity, the Authority agrees to pay or reimburse the 2008 Certificate Insurer, to the extent permitted by law, any and all charges, fees, costs, claims, losses, liabilities (including penalties), judgments, demands, damages, and expenses which the 2008 Certificate Insurer or its officers, directors, shareholders, employees, agents and each Person, if any, who controls the 2008 Certificate Insurer within the meaning of either Section 15 of the Securities Act of 1933, as amended, or Section 20 of the Securities Exchange Act of 1934, as amended, may reasonably pay or incur, including, but not limited to, fees and expenses of attorneys, accountants, consultants and auditors and reasonable costs of investigations, of any nature in connection with, in respect of or relating to the transactions contemplated by this Trust Agreement or any other financing document by reason of:

(a) any omission or action (other than of or by the 2008 Certificate Insurer) in connection with the offering, issuance, sale, remarketing or delivery of the 2008 Certificates;

(b) the negligence, bad faith, willful misconduct, misfeasance, malfeasance or theft committed by any director, officer, employee or agent of the Authority in connection with any transaction arising from or relating to this Trust Agreement or any other financing document;

(c) the violation by the Authority of any law, rule or regulation, or any judgment, order or decree applicable to it;

(d) the breach by the Authority of any representation, warranty or covenant under this Trust Agreement or any other financing document or the occurrence, in respect of the Authority under this Trust Agreement or any other financing document of any "event of default" or any event which, with the giving of notice or lapse of time or both, would constitute any "event of default"; or

(e) any untrue statement or alleged untrue statement of a material fact contained in any official statement relating to the 2008 Certificates, if any, or any omission or alleged omission to state therein a material fact required to be stated therein or necessary to make the statements therein not misleading, except insofar as such claims arise out of or are based upon any untrue statement or omission in information included in an official statement, if any, and furnished by the 2008 Certificate Insurer in writing expressly for use therein.

(k) The 2008 Certificate Insurer shall be entitled to pay principal of or interest on the 2008 Certificates that shall become Due for Payment but shall be unpaid by reason of Nonpayment (as such terms are defined in the 2008 Certificate Insurance Policy) and any amounts due on the 2008 Certificates as a result of acceleration of the maturity thereof in accordance with this Trust Agreement, whether or not the 2008 Certificate Insurer has received a Notice (as defined in the 2008 Certificate Insurance Policy) of Nonpayment or a claim upon the 2008 Certificate Insurance Policy.

(l) In addition, the 2008 Certificate Insurer shall, to the extent it makes any payment of principal or interest on the 2008 Certificates, become subrogated to the rights of the recipients of such payments in accordance with the terms of 2008 Certificate Insurance Policy, and to evidence such subrogation (i) in the case of claims for interest, the Trustee shall note the 2008 Certificate Insurer's rights as subrogee on the registration books of the Authority maintained by the Trustee, upon receipt of proof of payment of interest thereon to the registered holders of the 2008 Certificates, and (ii) in the case of claims for principal, the Trustee, if any, shall note the 2008 Certificate Insurer's rights as subrogee on the registration books of the Authority maintained by the Trustee, upon surrender of the 2008 Certificates together with receipt of proof of payment of principal thereof.

Section 10.02. Additional Provisions Related to the 2008 Certificate Insurance Policy.

(a) Subject to Section 10.03, the 2008 Certificate Insurer shall be deemed to be sole Owner of the 2008 Certificates it insures for the purpose of exercising any voting right or privilege or giving any consent or direction or taking any other action that the 2008 Certificate Owners are entitled to take pursuant to this Trust Agreement, including any consent to any modification, amendment or supplement to this Trust Agreement pursuant to Section 7.01 hereof.

(b) Copies of any amendments made to the documents executed in connection with the issuance of the 2008 Certificates which are consented to by the 2008 Certificate Insurer shall be sent to Standard & Poor's.

(c) The 2008 Certificate Insurer shall receive written notice of the resignation or removal of the Trustee and any Trustee for the 2008 Certificates and the appointment of a successor thereto.

(d) The 2008 Certificate Insurer shall receive written copies of all notices required to be delivered to Owners of 2008 Certificates.

(e) The 2008 Certificate Insurer shall have the right to receive such additional information as it may reasonably request.

(f) The Authority will permit the 2008 Certificate Insurer to discuss the affairs, finances and accounts of the Authority or any information the 2008 Certificate Insurer may reasonably request regarding the security for the 2008 Certificates with appropriate officers of the Authority, and will use best efforts to enable the 2008 Certificate Insurer to have access to the facilities, books and records of the Authority on any business day upon reasonable prior notice.

(g) The Trustee shall notify the 2008 Certificate Insurer of any failure of the Authority to provide notices, certificates and other information under the financing documents.

(h) If the Trustee receives any moneys from proceeds of the 2008 Certificate Insurance Policy, the Trustee shall hold such moneys separate and apart from all other moneys held by the Trustee under this Trust Agreement and shall apply such moneys only to the payment of the principal or prepayment price or interest with respect to the 2008 Certificates for which such payments were received.

(i) In the event that the principal and/or interest due on the 2008 Certificates shall be paid by the 2008 Certificate Insurer pursuant to 2008 Certificate Insurance Policy, the 2008 Certificates shall remain outstanding for all purposes, not be defeased or otherwise satisfied and not be considered paid by the Authority, and the assignment and pledge of the trust estate and all covenants, agreements and other obligations of the Authority to the registered owners shall continue to exist and shall run to the benefit of the 2008 Certificate Insurer, and the 2008 Certificate Insurer shall be subrogated to the rights of such registered owners, including, without limitation, any rights that such owners may have in respect of securities law violations arising from the offer and sale of the 2008 Certificates.

(j) The 2008 Certificate Insurer shall be deemed to be the Owners of all of the 2008 Certificates for purposes of (a) exercising all remedies and directing the Trustee to take actions or for any other purposes following an Event of Default (as defined herein), and (b) granting any consent, direction or approval or taking any action permitted or required by the Owners of the 2008 Certificates.

(k) Notwithstanding anything in this Trust Agreement to the contrary so long as the 2008 Certificate Insurance Policy shall be in full force and effect and the 2008 Certificate Insurer

shall not be in default of any of its obligations thereunder, upon the occurrence and continuance of an Event of Default, as defined herein, the Trustee may, with the consent of the 2008 Certificate Insurer, and shall at the direction of the 2008 Certificate Insurer or the Bondholders with the prior written consent of the 2008 Certificate Insurer, by written notice to the Authority and the 2008 Certificate Insurer, as applicable (i) declare the payments under the Contract representing the principal of the 2008 Certificates immediately due and payable, in accordance with the terms of the Contract or (ii) annul any declaration of acceleration.

(l) In the event of any reorganization or liquidation, the 2008 Certificate Insurer shall have the right to vote on behalf of all Owners of the 2008 Certificates guaranteed by the 2008 Certificate Insurer, absent a default by the 2008 Certificate Insurer under the 2008 Certificate Insurance Policy.

(m) The Authority, to the extent permitted by law, but solely from amounts payable under the Contract, to the extent such amounts are not required to pay the 2008 Certificates shall indemnify, defend and hold harmless the 2008 Certificate Insurer against any loss, damages, liability or expense incurred without negligence, default or willful misconduct on the part of the 2008 Certificate Insurer arising out of or in connection with (i) the exercise or performance of any of its powers or duties hereunder, or (ii) any untrue statement or alleged untrue statement of any material fact or omission or alleged omission to state a material fact necessary to make the statements made, in the light of the circumstances under which they were made, not misleading in any official statement or other offering circular utilized in connection with the sale of any of the 2008 Certificates, including costs and expenses (including attorneys' fees) of defending itself against any claim or liability in connection with the exercise or performance of any of its powers hereunder. The rights of the 2008 Certificate Insurer and the obligations of the Authority under this Section shall survive the discharge of the 2008 Certificates and this Trust Agreement. Notwithstanding the foregoing, the Authority will not be liable for any losses, costs or expenses resulting from the willful misconduct or negligence of the 2008 Certificate Insurer, or resulting from a misrepresentation or omission made by the 2008 Certificate Insurer in any offering document or other disclosure materials or filings (including any filings made with any insurance regulator, the Securities & Exchange Commission or any other government body) concerning the 2008 Certificate Insurer.

(n) The 2008 Certificate Insurer shall be provided with the following information:

(i) the financial statements of the City and other information furnished by the City to the Authority within fifteen Business Days after receipt thereof by the City pursuant to Section 4.09(b) of the Master Purchase Contract;

(ii) notice of any draw upon the Reserve Fund within two Business Days after knowledge thereof other than (A) withdrawals of amounts in excess of the Reserve Fund Requirement, and (B) withdrawals in connection with a refunding of 2008 Certificates;

(iii) notice of any default under this Trust Agreement known to the Trustee or the Authority within five Business Days after knowledge thereof;

(iv) notice of the advance refunding or redemption of any of the 2008 Certificates within five Business Days after the Trustee receives notice thereof from the City, including the principal amount, maturities and CUSIP numbers thereof;

(v) as soon as practicable, notice of the commencement of any proceeding by or against the Authority or the City commenced under the United States Bankruptcy Code or any other applicable bankruptcy, insolvency, receivership, rehabilitation or similar law (an "Insolvency Proceeding");

(vi) as soon as practicable, notice of the making of any claim in connection with any Insolvency Proceeding seeking the avoidance as a preferential transfer of any payment of principal of, or interest on, the 2008 Certificates; and

(vii) as soon as practicable, a full transcript of all proceedings relating to the execution of any amendment, supplement or waiver to this Trust Agreement, the Master Contract or any other related document.

Section 10.03. 2008 Certificate Insurer Default. In the event that the 2008 Certificate Insurer is in payment default under the 2008 Certificate Insurance Policy, an Insurer Indenture Event of Default has occurred and is continuing with respect to the 2008 Certificate Insurance Policy or the 2008 Certificate Insurance Policy is no longer in effect (and all amounts due to the 2008 Certificate Insurer are then paid in full), all references herein to the 2008 Certificate Insurer and all provisions herein for the benefit of the 2008 Certificate Insurer shall be of no effect; provided, however, that the rights of the 2008 Certificate Insurer derived through subrogation and assignment shall remain in full force and effect.

Section 10.04. Modification, Cancellation, Termination or Substitution of 2008 Certificate Insurance Policy. The Authority shall not consent to the surrender, cancellation, termination, amendment or modification in any material respect of the 2008 Certificate Insurance Policy by the 2008 Certificate Insurer, or to the substitution of a different Credit Enhancement for the 2008 Certificate Insurance Policy, unless the Authority and the Trustee shall have received the consent of the Bank, and the Authority and the Trustee shall consent to any such surrender, cancellation, termination, amendment or modification of the 2008 Certificate Insurance Policy by the 2008 Certificate Insurer if so directed by the Bank within seven days of receiving such direction. If, upon receipt of such consent or direction from the Bank, the 2008 Certificate Insurance Policy is so surrendered, cancelled, terminated, amended or modified in any material respect by the 2008 Certificate Insurer, or a different Credit Enhancement is so substituted for the 2008 Certificate Insurance Policy, the 2008 Certificates shall be subject to mandatory tender.

Section 10.05. Additional Provisions with respect to Rights of the Bank.

(a) To the extent the Bank pays the principal of or interest on the 2008 Certificates from one or more drawings under its Credit Enhancement and has not been reimbursed for such payment by the Authority or the Trustee, on behalf of the Authority, in accordance with the terms of the Reimbursement Agreement between the Bank and the City, (i) such amounts of principal of and interest on such 2008 Certificates shall be deemed not to have been paid for

purposes of this Trust Agreement and such 2008 Certificates shall remain Outstanding and shall continue to be due and owing until paid or otherwise satisfied; (ii) all rights of the Owners of such 2008 Certificates with respect to receiving payment of such principal from the Authority shall, without any further action on the part of such Owners or the Trustee, be assigned to the Bank and the Bank shall become subrogated to such rights; (iii) as to any such payment of principal of the 2008 Certificates from a drawing under the Bank's Credit Enhancement, the Bank shall become the Owner of such 2008 Certificate, which shall be evidenced as set forth in the next sentence; and (iv) as to any such payment of interest on such 2008 Certificates from a drawing under the Bank's Credit Enhancement, the Bank shall become the owner of all rights to such interest, constituting the Assigned Rights to Interest with respect thereto. The Trustee shall designate any portion of payment of principal on 2008 Certificates paid from one or more drawings under the Bank's Credit Enhancement, whether by virtue of mandatory sinking fund pro rata redemption, maturity or other advancement of maturity, on its books as a reduction in the principal amount of 2008 Certificates registered to the then current Owner, whether DTC or its nominee or otherwise, and shall issue, as a replacement 2008 Certificate, a Subrogated Certificate to the Bank, registered in the name of the Bank, in a principal amount equal to the amount of principal so paid (without regard to Authorized Denominations); provided that the Trustee's failure to so designate any payment or issue any Subrogated Certificate shall have no effect on the amount of principal or interest payable by the Authority on any 2008 Certificate, the subrogation rights of the Bank or the Bank's ownership of such 2008 Certificate to the extent principal thereof has been paid from a drawing under the Bank's Credit Enhancement.

(b) In addition, to the extent the Bank pays the principal of or interest on 2008 Certificates from one or more drawings under the Bank's Credit Enhancement and has not been reimbursed from such payment by the Authority or the Trustee, on behalf of the Authority, in accordance with the terms of the Reimbursement Agreement between the Bank and the City, the Bank shall be subrogated to the rights of the Owners of such 2008 Certificates with respect to the 2008 Certificate Insurance Policy in respect of any such payment of principal or interest that is insured under the 2008 Certificate Insurance Policy (a "Covered Payment"); provided, however, that the Bank's subrogation rights with respect to the 2008 Certificate Insurance Policy in respect of the foregoing payments of principal and interest are subject to the terms and conditions of the 2008 Certificate Insurance Policy.

(c) To exercise such rights of subrogation as to a Covered Payment, the Bank must notify the Trustee and the 2008 Certificate Insurer on or before 5:00 p.m. New York City time on the date that is 30 days after a Covered Payment has been made that the Bank is making a claim (a "Claim") under the 2008 Certificate Insurance Policy, which claim shall (i) specifically reference the policy number of the 2008 Certificate Insurance Policy and shall be presented to the 2008 Certificate Insurer at its address specified herein or pursuant hereto, (ii) state the date of the Covered Payment, (iii) state the amount of the Covered Payment, and (iv) in all cases comply with the requirements of this Trust Agreement and the 2008 Certificate Insurance Policy. Upon payment of a Claim, the provisions of this Section shall apply to the same extent as if the 2008 Certificate Insurer had made such payment directly on the related Series of 2008 Certificates. In the event the Bank does not make a claim on or before 5:00 p.m. New York City time on the date that is 30 days after a Covered Payment, the 2008 Certificate Insurer shall have no further obligation to the Bank with respect thereto and a principal amount of the related Series of

Certificates equal to the principal that has been paid by the Bank shall be deemed to be fully discharged in accordance herewith.

(d) At all times from and after the occurrence of a Control Event with respect to the 2008 Certificate Insurance Policy, the Bank shall be an expressly intended third party beneficiary hereof and shall be deemed to be the sole Owner of the 2008 Certificates for the purpose of exercising any voting right or privilege or giving any consent or direction or taking any other action that the Owners of the 2008 Certificates are entitled to exercise, give or take pursuant to this Trust Agreement with respect to (i) Events of Default and remedies hereunder and under the Contract, (ii) the duties and obligations of the Trustee, and (iii) granting or withholding any consent wherever Owner consent is required.

(e) Notwithstanding any contrary provision hereof or of the Contract, following any Control Event, any references herein and in the Contract to the payment of the reasonable fees and expenses of the 2008 Certificate Insurer shall be deemed to refer to the reasonable fees and expenses of the Bank incurred in connection therewith; provided that any such fees and expenses previously incurred by the 2008 Certificate Insurer shall continue to be payable to the 2008 Certificate Insurer.

## ARTICLE XI

### MISCELLANEOUS

Section 11.01. Benefits of this Trust Agreement Limited to Parties. Nothing contained herein, expressed or implied, is intended to give to any person other than the Authority, the Trustee, the 2008 Certificate Insurer, the Bank and the Owners any right, remedy or claim under or by reason hereof. Any agreement or covenant required herein to be performed by or on behalf of the Authority or any member, officer or employee thereof shall be for the sole and exclusive benefit of the Trustee, the 2008 Certificate Insurer, the Bank and the Owners. The 2008 Certificate Insurer and the Bank shall be third-party beneficiaries of this Trust Agreement.

Section 11.02. Successor is Deemed Included In All References To Predecessor. Whenever herein either the Authority or any member, officer or employee thereof is named or referred to, such reference shall be deemed to include the successor to the powers, duties and functions that are presently vested in the Authority or such member, officer or employee, and all agreements and covenants required hereby to be performed by or on behalf of the Authority or any member, officer or employee thereof shall bind and inure to the benefit of the respective successors thereof whether so expressed or not.

Section 11.03. Execution of Documents by Owners. Any declaration, request or other instrument which is permitted or required herein to be executed by Owners may be in one or more instruments of similar tenor and may be executed by Owners in person or by their attorneys appointed in writing. The fact and date of the execution by any Owner or his attorney of any declaration, request or other instrument or of any writing appointing such attorney may be proved by the certificate of any notary public or other officer authorized to make acknowledgments of deeds to be recorded in the state or territory in which he purports to act that the person signing such declaration, request or other instrument or writing acknowledged to him

the execution thereof, or by an affidavit of a witness of such execution duly-sworn to before such notary public or other officer. The ownership of any 2008 Certificates and the amount, Certificate Payment Date, number and date of holding the same may be proved by the registration books relating to the 2008 Certificates at the corporate trust office of the Trustee.

Any declaration, request or other instrument or writing of the Owner of any 2008 Certificate shall bind all future Owners of such Certificate with respect to anything done or suffered to be done by the Authority or the Trustee in good faith and in accordance therewith.

Section 11.04. Waiver of Personal Liability. No member, officer or employee of the Authority shall be individually or personally liable for the payment of the interest or principal or prepayment premiums, if any, evidenced and represented by the 2008 Certificates by reason of their issuance, but nothing herein contained shall relieve any such member, officer or employee from the performance of any official duty provided by applicable provisions of law or hereby.

Section 11.05. Content of Certificates of the Authority. Every Certificate of the Authority with respect to compliance with any agreement, condition, covenant or provision provided herein shall include (a) a statement that the person or persons making or giving such certificate have read such agreement, condition, covenant or provision and the definitions herein relating thereto; (b) a brief statement as to the nature and scope of the examination or investigation upon which the statements contained in such certificate are based; (c) a statement that, in the opinion of the signers, they have made or caused to be made such examination or investigation as is necessary to enable them to express an informed opinion as to whether or not such agreement, condition, covenant or provision has been complied with; and (d) a statement as to whether, in the opinion of the signers, such agreement, condition, covenant or provision has been complied with.

Any Certificate of the Authority may be based, insofar as it relates to legal matters, upon an Opinion of Counsel unless the person making or giving such certificate knows that the Opinion of Counsel with respect to the matters upon which his certificate may be based, as aforesaid, is erroneous, or in the exercise of reasonable care should have known that the same was erroneous. Any Opinion of Counsel may be based, insofar as it relates to factual matters or information with respect to which is in the possession of the Authority, upon a representation by an officer or officers of the Authority unless the counsel executing such Opinion of Counsel knows that the representation with respect to the matters upon which his opinion may be based, as aforesaid, is erroneous, or in the exercise of reasonable care should have known that the same was erroneous.

Section 11.06. Accounts and Funds; Business Days. The Trustee may establish such funds and accounts as it deems necessary and appropriate to perform its duties and obligations hereunder. Any account or fund required herein to be established and maintained by the Trustee may be established and maintained in the accounting records of the Trustee either as an account or a fund, and may, for the purposes of such accounting records, any audits thereof and any reports or statements with respect thereto, be treated either as an account or a fund; but all such records with respect to all such accounts and funds shall at all times be maintained in accordance with sound corporate trust industry practice and with due regard for the protection of the security of the 2008 Certificates and the rights of the Owners. Any action required to occur hereunder on

a day which is not a Business Day shall be required to occur on the next succeeding Business Day with the same effect as if made on such non-Business Day.

Section 11.07. Notices.

(a) All written notices to be given hereunder shall be given by facsimile transmission or other Electronic means or by first-class mail or hand delivery (unless such delivery method shall be otherwise specified herein) to the party entitled thereto at its address set forth below, or at such other address as such party may provide to the other parties in writing from time to time, namely:

If to the Authority:

Modesto Public Financing Authority  
c/o City of Modesto  
City Hall  
1010 Tenth Street, Suite 5200  
Modesto, CA 95353  
Attention: Auditor and Treasurer  
Telephone No.: (209) 577-5371  
Facsimile No.: (209) 571-5880

If to the City:

City of Modesto  
1010 Tenth Street, Suite 5200  
Modesto, CA 95353  
Attention: Finance Director  
Telephone No.: (209) 577-5371  
Facsimile No.: (209) 571-5880

If to the Trustee:

The Bank of New York Mellon Trust Company,  
N.A.  
100 Pine Street, Suite 3100  
San Francisco, CA 94111  
Attention: Corporate Trust  
Telephone No.: (415) 263-2432  
Facsimile No.: (415) 399-1647

If to S&P:

Attn: Muni Structured Finance  
55 Water Street, 38<sup>th</sup> Floor  
New York, New York 10041  
Telephone No.: (212) 438-2000  
Email: Pubfin\_structured@standardand poors.com

If to Moody's:

Moody's Investors Services  
7 World Financial Center  
New York, New York 10007  
Attention: Public Finance Department  
Facsimile: (212) 553-4090

If to the 2008 Certificate Insurer: Assured Guaranty Corp.  
1325 Avenue of the Americas  
New York, New York 10019  
Attention: General Counsel  
Facsimile: (212) 581-3268

Assured Guaranty  
1325 Avenue of the Americas  
New York, New York 10019  
Attention: Risk Management Department - Public  
Finance Surveillance  
Facsimile: (212) 581-3268

If to the Bank: JPMorgan Chase Bank, N.A.  
383 Madison Avenue, Floor 8  
New York, New York 10179  
Mail Code: NY1-M076  
Attention: James G. Millard  
Telephone: (212) 270-2198  
Telecopy: (917) 456-3538

Each such notice, statement, demand, consent, approval, authorization, offer, designation, request or other communication hereunder shall be deemed delivered to the party to whom it is addressed (i) if personally served or delivered, upon delivery, (ii) if given by Electronic communication, whether by telex, telegram or telecopier, upon the sender's receipt of an appropriate answer back or other written acknowledgement or confirmation of receipt of the entire notice, approval, demand, report or other communication, (iii) if given by first class or registered or certified mail, return receipt requested, deposited the United States mail postage prepaid, 72 hours after such notice is deposited with the United States mail, (iv) if given by overnight courier, with courier charges prepaid, 24 hours after delivery to said overnight courier, or (v) if given by any other means, upon delivery at the address specified in this Section 11.07.

(b) The Trustee shall give notice to the Rating Agencies of the occurrence of any of the following with respect to the 2008 Certificates:

(i) the removal, resignation or appointment of the Trustee or Remarketing Agent;

(ii) the execution of any amendment or supplement to the Trust Agreement, the Credit Enhancement, the Liquidity Facility or the Remarketing Agreement;

(iii) the expiration, termination, extension or substitution of the Liquidity Facility or Credit Enhancement;

(iv) the redemption in whole of the Outstanding 2008 Certificates;

(v) the acceleration of all Outstanding 2008 Certificates pursuant to Article VIII of the Trust Agreement;

- (vi) the defeasance of all Outstanding 2008 Certificates; and
- (vii) any change in Mode of the 2008 Certificates.

(c) The Trustee shall give notice to the Holders of the expiration, termination, extension or substitution of the Liquidity Facility or Credit Enhancement;

Section 11.08. CUSIP Numbers. Neither the Authority nor the Trustee shall be liable for any defect or inaccuracy in the CUSIP number that appears on any 2008 Certificate or in any prepayment notice relating thereto. The Trustee may, in its discretion, include in any prepayment notice relating to any of the 2008 Certificates a statement to the effect that the CUSIP numbers on the 2008 Certificates have been assigned by an independent service and are included in such notice solely for the convenience of the Owners and that neither the Authority nor the Trustee shall be liable for any defects or inaccuracies in such numbers.

Section 11.09. Article and Section Headings and References. The headings or titles of the several articles and sections hereof and the table of contents appended hereto shall be solely for convenience of reference and shall not affect the meaning, construction or effect hereof. All references herein to "articles," "sections" and other subdivisions or clauses are to the corresponding articles, sections, subdivisions or clauses hereof; and the words "hereby," "herein," "hereof," "hereto," "herewith," "hereunder" and other words of similar import refer to this Trust Agreement as a whole and not to any particular article, section, subdivision or clause hereof.

Section 11.10. Partial Invalidity. If any one or more of the agreements or covenants Trustee shall be contrary to law, then such agreement or agreements, such covenant or covenants or such portions thereof shall be null and void and shall be deemed separable from the remaining agreements and covenants or portions thereof and shall in no way affect the validity hereof or of the 2008 Certificates, and the Owners shall retain all the benefit, protection and security afforded to them under any applicable provisions of law. The Authority and the Trustee hereby declare that they would have executed and delivered this Trust Agreement and each and every other article, section, paragraph, subdivision, sentence, clause and phrase hereof and would have authorized the execution and delivery of the 2008 Certificates pursuant hereto irrespective of the fact that any one or more articles, sections, paragraphs, subdivisions, sentences, clauses or phrases hereof or the application thereof to any person or circumstance may be held to be unconstitutional, unenforceable or invalid.

Section 11.11. Execution in Several Counterparts. This Trust Agreement may be executed in any number of counterparts and each of such counterparts shall for all purposes be deemed to be an original; and all such counterparts, or as many of them as the Authority and the Trustee shall preserve undestroyed, shall together constitute but one and the same instrument.

Section 11.12. California Law. This Trust Agreement shall be construed and governed in accordance with the laws of the State of California.

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IN WITNESS WHEREOF, the Modesto Public Financing Authority has caused this Trust Agreement to be signed in its name by its Auditor and Treasurer and The Bank of New York Mellon Trust Company, N.A., in token of its acceptance of the trusts created hereunder, has caused this Trust Agreement to be signed by one of the officers thereunder duly authorized, all as of the day and year first above written.

MODESTO PUBLIC FINANCING  
AUTHORITY

By: *Monette Brink*  
Auditor and Treasurer

THE BANK OF NEW YORK MELLON  
TRUST COMPANY, N.A.,  
as Trustee

By: \_\_\_\_\_  
Authorized Officer

IN WITNESS WHEREOF, the Modesto Public Financing Authority has caused this Trust Agreement to be signed in its name by its Auditor and Treasurer and The Bank of New York Mellon Trust Company, N.A., in token of its acceptance of the trusts created hereunder, has caused this Trust Agreement to be signed by one of the officers thereunder duly authorized, all as of the day and year first above written.

MODESTO PUBLIC FINANCING  
AUTHORITY

By: \_\_\_\_\_  
Auditor and Treasurer

THE BANK OF NEW YORK MELLON  
TRUST COMPANY, N.A.,  
as Trustee

By:  \_\_\_\_\_  
Authorized Officer

**EXHIBIT A**

**[FORM OF CERTIFICATE OF PARTICIPATION]**

**WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A**

**Evidencing and Representing a Proportionate Interest of the Owner Hereof  
in 2008 Payments to be made by the  
City of Modesto  
to the  
Modesto Public Financing Authority**

Unless this certificate is presented by an authorized representative of The Depository Trust Company a New York corporation ("DTC"), to the Trustee or its agent for registration of transfer, exchange, or payment, and any certificate issued is registered in the name of Cede & Co. or in such other name as is requested by an authorized representative of DTC (and any payment is made to Cede & Co. or to such other entity as is requested by an authorized representative of DTC), ANY TRANSFER, PLEDGE, OR OTHER USE HEREOF FOR VALUE OR OTHERWISE BY OR TO ANY PERSON IS WRONGFUL inasmuch as the registered owner hereof, Cede & Co., has an interest herein.

No. R-1

\$47,625,000

<u>Interest Rate</u>	<u>Certificate Payment Date</u>	<u>Dated Date</u>	<u>CUSIP</u>	<u>Substitution Date</u>
Variable	October 1, 2036	May 30, 2008	607804 AC5	July 14, 2011

REGISTERED OWNER: CEDE & CO.

PRINCIPAL SUM: FORTY SEVEN MILLION SIX HUNDRED TWENTY FIVE  
THOUSAND DOLLARS

THIS IS TO CERTIFY that the registered owner set forth above of this Water Refunding Revenue Certificate of Participation, 2008 Series A (this "Certificate"), is the owner of a proportionate interest in the 2008 Payments (as that term is defined in the Trust Agreement hereinafter mentioned) made under and pursuant to that certain Master Installment Purchase Contract executed and entered into as of November 1, 1997, as heretofore supplemented and as supplemented by that certain 2008 Supplemental Installment Purchase Contract, dated as of May 1, 2008, each by and between the City of Modesto, a charter city and municipal corporation organized and existing under and by virtue of the Constitution and laws of the State of California (the "City") and the Modesto Public Financing Authority, a joint exercise of powers agency duly organized and existing under and by virtue of the laws of the State of California (the "Authority") (which Master Installment Purchase Contract as so supplemented is referred to herein as the "Contract"), all of which rights in the 2008 Payments have been assigned by the

Authority to The Bank of New York Mellon Trust Company, N.A., a national banking association duly organized and existing under and by virtue of the laws of the United States of America, or any other bank or trust company which may at any time be substituted in place of the original trustee as provided in the Trust Agreement hereinafter mentioned (the "Trustee"). Capitalized terms used in this Certificate but not otherwise defined shall have the meanings assigned to them in the Trust Agreement.

The registered owner of this Certificate is entitled to receive, subject to the terms of the Contract and any right of prepayment prior thereto hereinafter provided for, on the Certificate Payment Date set forth above, upon surrender of this Certificate on such Certificate Payment Date or on the date of prepayment prior thereto at the corporate trust office of the Trustee, the principal sum set forth above, representing the registered owner's proportionate share of the 2008 Payments constituting principal installments with respect to Certificates becoming due and payable on such Certificate Payment Date or on the date of prepayment prior thereto, and to receive an interest installment on such principal installment on each Interest Payment Date to the respective Certificate Payment Date or date of prepayment prior thereto. While this Certificate is in a Daily Mode or a Weekly Mode, the Interest Payment Date shall be the first Business Day of the month. Payment of interest evidenced by this Certificate shall be made to the person appearing on the registration books of the Trustee as the Owner thereof as of the close of business on the applicable Record Date, such interest to be payable on each Interest Payment Date by the Trustee (i) by check mailed on such Interest Payment Date to such Owner's address as it appears on the registration books of the Trustee at the close of business on the Record Date or (ii) by wire transfer to any Owner of at least \$1,000,000 aggregate principal amount of Certificates according to the written instructions provided by such Owner on or prior to the applicable Record Date to the Trustee, which written instructions shall remain in effect until revised by such Owner by an instrument in writing delivered to the Trustee. Interest evidenced by this Certificate shall accrue from and including the Interest Accrual Date immediately preceding the date of authentication hereof, or, if such date of authentication shall be an Interest Accrual Date, from such Interest Accrual Date or, if such date of authentication shall be prior to the second Interest Accrual Date, from the Delivery Date.

This Certificate is one of the duly authorized certificates of participation aggregating \$47,625,000, which have been executed by the Trustee under and pursuant to the provisions of a Trust Agreement, dated as of May 1, 2008, as amended and restated by an Amended and Restated Trust Agreement, dated July 14, 2011 (the "Trust Agreement"), between the Authority and the Trustee. Copies of the Trust Agreement are on file at the corporate trust office of the Trustee in San Francisco, California and reference is hereby made to the Trust Agreement and to any and all amendments thereof and supplements thereto for a description of the covenants and pledges securing the 2008 Payments and the Certificates, for the nature, extent and manner of enforcement of such covenants and pledges, for the rights and remedies of the registered owners of the Certificates with respect thereto and for the other conditions and terms upon which the Certificates are executed and delivered thereunder.

To the extent and in the manner permitted by the terms of the Trust Agreement, the provisions of the Trust Agreement may be amended by the parties thereto, but no such amendment shall (1) extend the Certificate Payment Date of this Certificate, or change the payment dates of, or reduce the rate of interest or principal or prepayment premium, if any,

evidenced and represented hereby, without the express written consent of the registered owner hereof, or (2) reduce the percentage of Certificates required for the written consent to any amendment, or (3) modify any rights or obligations of the Trustee without its prior written assent thereto.

The Certificates are delivered as fully registered Certificates in Authorized Denominations. This Certificate is being issued initially in a Weekly Mode and so long as this Certificate shall remain in a Weekly Mode, this Certificate shall bear interest at a Weekly Rate determined by the provisions of the Trust Agreement.

As provided in and subject to the terms and conditions of the Trust Agreement, the Certificates may, from time to time, be changed from a Weekly Mode to a Daily Mode, a Flexible Mode, a Term Rate Mode or a Fixed Rate Mode.

Except in the event of serialization of the Certificates in accordance with the provisions of the Trust Agreement, the Certificates are subject to mandatory prepayment from Sinking Fund Payments prior to their Maturity Date, in part by lot, on October 1 of each year on and after October 1, 2008, in accordance with the schedule set forth below upon notice as provided in the Trust Agreement, from and in the amount of the principal installment of the 2008 Payments due and payable on such dates, at a prepayment price equal to the sum of the principal amount evidenced and represented thereby plus accrued and unpaid interest evidenced and represented thereby to the Prepayment Date, without a prepayment premium.

Sinking Fund Payments

Mandatory Sinking Fund Payment Date (October 1)	Sinking Fund Payment	Mandatory Sinking Fund Payment Date (October 1)	Sinking Fund Payment
2008	\$290,000	2023	\$2,300,000
2009	285,000	2024	2,410,000
2010	285,000	2025	2,515,000
2011	285,000	2026	2,595,000
2012	310,000	2027	2,705,000
2013	310,000	2028	2,810,000
2014	340,000	2029	2,945,000
2015	340,000	2030	3,055,000
2016	365,000	2031	3,185,000
2017	365,000	2032	3,295,000
2018	395,000	2033	3,430,000
2019	395,000	2034	3,570,000
2020	395,000	2035	3,705,000
2021	425,000	2036	3,870,000
2022	450,000		

Additionally, if any portion of this Certificate has been optionally prepaid as described in the succeeding paragraph, the amounts of such Sinking Fund Payments shall be reduced as

directed by the Authority, or if not so directed, proportionately in increments of Authorized Denominations by the principal amount evidenced and represented by all such Certificates so optionally prepaid.

Each Certificate in a Daily Mode or a Weekly Mode shall be subject to prepayment at the option of the Authority, in whole or in part, in Authorized Denominations on any Business Day, at a prepayment price equal to 100% of the principal amount thereof, plus, accrued interest, if any, to the Prepayment Date, without premium.

Notice of prepayment of any Certificate selected for prepayment shall be given by first-class mail not less than 30 days nor more than 60 days before the prepayment date to the registered owner hereof, subject to and in accordance with provisions of the Trust Agreement with respect thereto. If notice of prepayment has been duly given and money for the payment of the prepayment price is held by the Trustee, then this Certificate shall, on the prepayment date designated in such notice, become due and payable, and from and after the date so designated interest evidenced and represented by this Certificate shall cease to accrue, and the registered owner of this Certificate shall have no rights with respect hereto except to receive payment of the prepayment price hereof.

This Certificate is transferable on the books to be kept for that purpose at the above-mentioned office of the Trustee by the registered owner hereof in person or by his duly authorized attorney upon payment of the charges provided in the Trust Agreement and upon surrender of this Certificate for cancellation accompanied by delivery of a duly executed written instrument of transfer in a form acceptable to the Trustee, and thereupon a new Certificate or Certificates of the same Certificate Payment Date evidencing and representing a like aggregate principal amount in Authorized Denominations will be delivered to the transferee. This Certificate may be exchanged at the above-mentioned office of the Trustee upon payment of the charges provided in the Trust Agreement for a like aggregate principal amount of Certificates of the same Certificate Payment Date of other Authorized Denominations. The Trustee may deem and treat the registered owner hereof as the absolute owner hereof for the purpose of receiving payment of the interest and principal evidenced and represented hereby and for all other purposes, whether this Certificate shall be overdue or not, and the Trustee shall not be affected by any notice or knowledge to the contrary; and payment of the interest and principal and prepayment premium, if any, evidenced and represented by this Certificate shall be made only to such registered owner, which payments shall be valid and effectual to satisfy and discharge liability on this Certificate to the extent of the sum or sums so paid.

The Certificates each evidence and represent a proportionate interest in the 2008 Payments in an amount equal to the aggregate principal amount of Certificates originally executed and delivered by the Trustee pursuant to the Trust Agreement and enjoy the benefits of a security interest in the moneys held in the funds established pursuant to the Trust Agreement, subject to the provisions of the Trust Agreement permitting the disbursement thereof for or to the purposes and on the conditions and terms set forth therein. The obligation of the City to make the 2008 Payments is a special obligation of the City payable solely from the Gross Revenues of the Water Utility System as provided in the Contract, and does not constitute a debt of the City or of the State of California or of any political subdivision thereof in contravention of any

constitutional or statutory debt limitation or restriction. The City may incur other obligations payable on parity with the 2008 Payments in accordance with the Contract.

The Trustee has no obligation or liability to the Certificate owners for the payment of the interest or principal or the prepayment premiums, if any, evidenced and represented by the Certificates; but rather the Trustee's sole obligations are to administer, for the benefit of the City and the Certificate owners, the various funds established under the Trust Agreement.

No member, officer or employee of the Authority shall be individually or personally liable for the payment of the interest or principal or prepayment premiums, if any, evidenced and represented by the Certificates by reason of their delivery, but nothing herein contained shall relieve any such member, officer or employee from the performance of any official duty provided by applicable provisions of law or hereby.

The Trust Agreement prescribes the manner in which it may be discharged and after which the Certificates shall no longer be secured by or entitled to the benefits of the Trust Agreement.

IN WITNESS WHEREOF, this Certificate has been executed by the manual signature of an authorized signatory of the Trustee as of the date set forth above.

THE BANK OF NEW YORK MELLON TRUST  
COMPANY, N.A.,  
as Trustee

By: \_\_\_\_\_  
Authorized Officer

ASSIGNMENT

For value received the undersigned hereby sells, assigns and transfers unto \_\_\_\_\_ (Taxpayer Identification Number: \_\_\_\_\_) the within Certificate and all rights thereunder, and hereby irrevocably constitutes and appoints \_\_\_\_\_ attorney to transfer the within Certificate on the books kept for registration thereof, with full power of substitution in the premises.

Dated: \_\_\_\_\_

Note: The signature to this Assignment must correspond with the name as written on the face of the Certificate in every particular, without alteration or enlargement or any change whatever.

Signature Guaranteed: \_\_\_\_\_

Notice: Signature must be guaranteed by an eligible guarantor institution.

## STATEMENT OF INSURANCE

Assured Guaranty Corp. ("Assured Guaranty"), a Maryland-domiciled insurance company, has delivered its financial guaranty insurance policy (the "Policy") with respect to the scheduled payments of principal of and interest on this Certificate to The Bank of New York Trust Company, N.A., as paying agent on behalf of the holders of the Certificates (the "Paying Agent"). Such Policy is on file and available for inspection at the principal office of the Paying Agent and a copy thereof may be obtained from Assured Guaranty or the Paying Agent. All payments required to be made under the Policy shall be made in accordance with the provisions thereof. The owner of this Certificate acknowledges and consents to the subrogation rights of Assured Guaranty as more fully set forth in the Policy.

\$47,625,000  
CITY OF MODESTO  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

CERTIFIED COPY OF REIMBURSEMENT AGREEMENT

The undersigned authorized representative of the City of Modesto, California (the "City"), in connection with the City of Modesto Water Revenue Certificates of Participation, 2008 Series A (the "Certificates") DOES HEREBY CERTIFY that attached hereto is a full, true and correct copy of the REIMBURSEMENT AGREEMENT, dated as of July 1, 2011, between the City and JPMorgan Chase Bank, National Association, and does hereby further certify that prior to June 5, 2014 such agreement has not been further amended, modified or rescinded since July 1, 2011, and is now in full force and effect.

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IN WITNESS WHEREOF, I have hereunto set my hand this 5<sup>th</sup> day of June, 2014.

CITY OF MODESTO

By:



A handwritten signature in cursive script, appearing to read 'Stephanie Lopez', is written over a horizontal line.

Stephanie Lopez  
City Clerk

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REIMBURSEMENT AGREEMENT

Between

JPMORGAN CHASE BANK, NATIONAL ASSOCIATION

and

CITY OF MODESTO

Dated as of July 1, 2011

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REIMBURSEMENT AGREEMENT, dated as of July 1, 2011, by and between the CITY OF MODESTO, a charter city and municipal corporation organized under the Constitution and laws of the State of California, and JPMORGAN CHASE BANK, NATIONAL ASSOCIATION, a national banking association.

WITNESSETH:

Whereas, the Applicant (such term and each other capitalized term used herein having the meaning set forth in Article One hereof) desires to secure a source of funds to be devoted exclusively to the payment by the Trustee, when and as due, of the principal of and interest with respect to, and to pay the purchase price of, the Certificates of Participation, and has applied to the Bank for issuance by the Bank of the Letter of Credit in an original stated amount of \$47,625,989.

The Bank has agreed to issue the Letter of Credit the following manner and subject to the following terms and conditions.

NOW, THEREFORE, in consideration of the mutual covenants herein contained, the Applicant and the Bank hereby agree as follows:

ARTICLE 1  
DEFINITIONS; CONSTRUCTION

Section 1.1 Definitions. As used herein:

“Agreement” means this Reimbursement Agreement, as amended and supplemented.

“Applicant” means the City of Modesto, a charter city and municipal corporation organized under the Constitution and laws of the State.

“Applicant Related Document” means each Related Document to which the Applicant is a party.

“Assigned Rights to Interest” means those rights to receive payment from the Issuer pursuant to the Trust Agreement of any interest with respect to Certificates of Participation with respect to which, pursuant to Section 10.05 of the Trust Agreement, the Bank, to the extent it has paid such interest from a drawing under the Letter of Credit, has become subrogated and an assignee and the owner.

“Available Amount” has the meaning set forth in the Letter of Credit.

“Bank” means JPMorgan Chase Bank, N.A. and its successors and assigns.

“Bank Agreement” means any credit agreement, reimbursement agreement, bond purchase agreement, liquidity agreement or other similar agreement (or any amendment, supplemental or modification thereto) pursuant to which the provider of credit or liquidity thereunder (the “Bank Agreement Provider”) undertakes to make loans, extend credit or liquidity in respect of obligations of the Applicant secured by Gross Revenues.

“Bank Agreement Provider” has the meaning set forth in the defined term “Bank Agreement”.

“Bank Certificate Endorsement” has the meaning set forth in Section 3.1(xv) hereof.

“Bank Certificates” means Certificates of Participation and/or beneficial interests therein purchased with the proceeds of a drawing under the Letter of Credit and registered in the name of the Bank or its nominee or assignee. Certificates of Participation and/or beneficial interests therein shall cease to be Bank Certificates upon the remarketing thereof in accordance with the Trust Agreement and the Remarketing Agreement or upon the sale thereof to the Applicant.

“Bank Documents” means this Agreement, the Custodian Agreement, the Fee Letter and the Letter of Credit.

“Bank Rate” means, with respect to any Bank Certificate or Liquidity Advance, (a) on any day prior to the date that is 90 days from and including the date such Bank Certificate was purchased or Liquidity Advance was made pursuant to Section 2.3, a fluctuating rate of interest equal to the greater of (i) the Base Rate and (ii) the Certificate of Participation Rate; (b) on any day on or after the date that is 91 days from and including the date such Bank Certificate was purchased or Liquidity Advance was made pursuant to Section 2.3 through and including the day that is the 180th day from and including the date such Bank Certificate was purchased or Liquidity Advance was made pursuant to Section 2.3, a fluctuating rate of interest equal to the greater of (i) the Base Rate plus one percent (1.00%) and (ii) the Certificate of Participation Rate; and (c) on and after the 181st day from and including the date such Bank Certificate was purchased or Liquidity Advance made pursuant to Section 2.3, a fluctuating rate of interest equal to the greater of (i) the Base Rate plus two percent (2.00%) and (ii) the Certificate of Participation Rate; *provided*, that during the continuance of an Insurer Default, the Bank Rate shall equal the Default Rate; *provided further*, however, that in the event that the Insurance Policy is no longer in effect, during the continuance of an Event of Default, the Bank Rate shall equal the Default Rate.

“Base Rate” means, for any day, a rate per annum equal to the greatest of (a) 7.50% per annum; (b) Federal Funds Rate for such day plus 2.00% per annum and (c) Prime Rate for such day plus 1.50% per annum.

“Business Day” has the meaning set forth in the Letter of Credit.

“Cancellation Agreement” means the Cancellation Agreement of even date herewith among the Applicant, the Trustee, the Insurer and the Bank.

“Capital Lease” means any lease of Property which in accordance with GAAP would be required to be capitalized on the balance sheet of the lessee.

“Capitalized Lease Obligation” means the amount of the liability shown on the balance sheet of any Person in respect of a Capital Lease as determined in accordance with GAAP.

“Certificates of Participation” means the Water Revenue Refunding Certificates of Participation 2008 Series A evidencing and representing proportionate interests of the owners thereof in 2008 Payments to be made by the Applicant to the Issuer.

“Certificates of Participation Documents” means the Trust Agreement, the Purchase Contract, the Remarketing Agreement, the Insurance Policy, the Reoffering Circular and the Certificates of Participation.

“Certificate of Participation Rate” means the rate of interest payable with respect to Certificates of Participation that are not Bank Certificates.

“Change of Law” means the occurrence, after the Closing Date, of any of the following: (a) the adoption or taking effect of any law, rule, regulation, statute, treaty, policy, guideline or directive of any court, central bank, self regulatory organization or Governmental Authority, (b) any change in any law, rule, regulation, statute, treaty, policy, guideline or directive or in the application, interpretation, promulgation, implementation, administration or enforcement thereof by any court, central bank, self regulatory organization or Governmental Authority or (c) the making or issuance of any request, rule, guideline or directive (whether or not having the force of law) by any court, central bank, self regulatory organization or Governmental Authority; provided that notwithstanding anything herein to the contrary, (x) the Dodd-Frank Act and all requests, rules, guidelines or directives thereunder or issued in connection therewith and (y) all requests, rules, guidelines or directives promulgated by the Bank for International Settlements, the Basel Committee on Banking Supervision (or any successor or similar authority) or the United States or foreign regulatory authorities, in each case pursuant to Basel III, shall in each case be deemed to be a “Change in Law”, regardless of the date enacted, adopted or issued.

“Closing Date” means the date on which the Letter of Credit is issued.

“Code” means the Internal Revenue Code of 1986, and any successor statute thereto.

“Costs” has the meaning set forth in Section 7.3 hereof.

“Custodian Agreement” means the Custodian Agreement of even date herewith among the Applicant, the Bank and The Bank of New York Mellon Trust Company, N.A., in its capacity as a custodian for the Bank, and any successor agreement among the Applicant, the Bank and any successor Trustee in its capacity as custodian for the Bank.

“Default Rate” means, on any date, the Base Rate in effect on such day plus 3.00%.

“Dodd-Frank Act” means the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, as enacted by the United States Congress, and signed into law on July 21, 2010, and all statutes, rules, guidelines or directives promulgated thereunder.

“ERISA” means the Employee Retirement Income Security Act of 1974, as amended, or any successor statute thereto.

“Event of Default” has the meaning set forth in Section 6.1 hereof.

“Existing Swap Agreement” means, collectively, the ISDA Master Agreement, the ISDA U.S. Municipal Counterparty Schedule to the Master Agreement, the ISDA Credit Support Annex and the Confirmation, each dated as of May 29, 2008, between the Applicant and Bank of America, N.A.

“Federal Funds Rate” means, on any day, the rate determined by the Bank to be the average (rounded upwards, if necessary, to the next higher 1/100 of 1%) of the rates per annum quoted to the Bank at approximately 10:00 a.m. (or as soon thereafter as is practicable) on such day (or, if such day is not a Business Day, on the immediately preceding Business Day) by two or more Federal funds brokers selected by the Bank for the sale to the Bank at face value of Federal funds in an amount equal or comparable to the principal amount owed to the Bank for which such rate is being determined.

“GAAP” means generally accepted accounting principles in the United States applicable to governmental entities as in effect from time to time applied by the Applicant on a basis consistent with the Applicant’s most recent financial statements furnished to the Bank pursuant to Section 5.5 hereof.

“Governmental Approval” means an authorization, consent, approval, license, or exemption of, registration or filing with, or report to any Governmental Authority.

“Governmental Authority” means any nation or government, any state, department, agency or other political subdivision thereof, and any entity exercising executive, legislative, judicial, regulatory or administrative functions of or pertaining to any government, and any corporation or other entity owned or controlled (through stock or capital ownership or otherwise) by any of the foregoing.

“Gross Revenues” has the meaning set forth in the Purchase Contract.

“Guarantees” means, for any Person, all guarantees, endorsements (other than for collection or deposit in the ordinary course of business) and other contingent obligations of such person to purchase, to provide funds for payment, to supply funds to invest in any other Person or otherwise to assure a creditor of another Person against loss.

“Indebtedness” means for any Person (without duplication) (a) all indebtedness created, assumed or incurred in any manner by such Person representing money borrowed (including by the issuance of debt securities), (b) all obligations for the deferred purchase price of property or services (other than trade accounts payable arising in the ordinary course of business), (c) all obligations secured by any Lien upon Property of such Person, whether or not such Person has assumed or become liable for the payment of such indebtedness, (d) all Capitalized Lease Obligations of such Person, (e) all obligations of such Person on or with respect to letters of credit, banker’s acceptances and other evidences of indebtedness representing extensions of credit whether or not representing obligations for borrowed money, and (f) all Guarantees made by such Person.

“Indemnified Person” has the meaning set forth in Section 7.3 hereof.

“Instruction” has the meaning set forth in Section 7.3 hereof.

“Insurance Policy” means the financial guaranty insurance policy issued by the Insurer at the time the Certificates of Participation were originally executed and delivered to the initial purchaser thereof, which policy insures the payment of the principal of and interest with respect to the Certificates of Participation, together with all endorsements thereto, including the Bank Certificate Endorsement.

“Insurance Policy Cancellation Date” means the date the Insurance Policy is cancelled in accordance with the terms of the Cancellation Agreement.

“Insured Rate” means on any day with respect to any Bank Certificate or Subrogated Certificate, (a) if such day occurs during the Commitment Period but prior to the forty-sixth day following the date on which the Bank purchases such Bank Certificate or becomes the Owner of such Subrogated Certificate, a rate per annum equal to the Base Rate; (b) if such day occurs during the Commitment Period and after the forty-fifth day, but prior to the ninety-first day, following the date on which the Bank purchases such Bank Certificate or becomes the Owner of such Subrogated Certificate, a rate per annum equal to the Base Rate plus 1.00%; and (c) if such day occurs during the Commitment Period and after the ninetieth day following the date on which the Bank purchases such Bank Certificate or becomes the Owner of such Subrogated Certificate or if such day occurs after the Commitment Period has terminated or expired, a rate per annum equal to the Base Rate plus 3.00%; *provided, however*, that immediately and automatically upon the occurrence of an Insurer Default (and without any notice given with respect thereto) and during the continuance of such Insurer Default, “Insured Rate” shall mean the Default Rate. For purposes of this definition, notwithstanding the definition of the term “Base Rate” contained in this Section 1.1, the term “Base Rate” means, for any day, the higher of (a) the Prime Rate and (b) the Federal Funds Rate plus two percent (2.0%) per annum. For purposes of this definition, the term “Commitment Period” means the period commencing on the Closing Date and terminating on the Termination Date.

“Insurer” means Assured Guaranty Corp.

“Insurer Default” has the meaning set forth in Section 6.2 hereof.

“Insurer Downgrade Event” shall occur if Moody’s or S&P shall (a) assign a financial strength rating or claims paying ability rating to the Insurer that is less than “A1”, in the case of Moody’s and less than “A+” in the case of S&P or (b) withdraw or suspend the financial strength rating or claims paying ability rating of the Insurer for credit related reasons; *provided, however*, that for purposes of this definition, a withdrawal or a suspension of a rating by either Rating Agency at the direction of the Insurer as a result of a reduction or potential reduction of the financial strength or claims-paying ability rating of the Insurer will be deemed to have occurred for credit related reasons.

“ISDA” means the International Swap Dealers Association, Inc.

“ISP” or “ISP98” means, International Standby Practices 1998 (International Chamber of Commerce Publication No. 590).

“Issuer” means the Modesto Public Financing Authority, a joint exercise of powers authority organized and existing under the laws of the State.

“Letter of Credit” means the irrevocable transferable direct pay letter of credit issued by the Bank for the account of the Applicant in favor of the Trustee, in the form of Exhibit A hereto with appropriate insertions.

“Lien” means any mortgage, lien, security interest, pledge, charge or encumbrance of any kind in respect of any Property, including the interests of a vendor or lessor under any conditional sale, Capital Lease or other title retention arrangement.

"Liquidity Advance" has the meaning set forth in Section 2.3(a) hereof.

"Liquidity Drawing" means a drawing under the Letter of Credit resulting from the presentation of a certificate in the form of Annex E to the Letter of Credit.

"Liquidity Drawing Date" has the meaning set forth in Section 2.3(a) hereof.

"Mandatory Tender Event" shall occur if (a) either S&P or Moody's shall have (i) assigned a Rating below "A", in the case of S&P, or "A3", in the case of Moody's, or (ii) withdrawn (for reasons other than defeasance or redemption of the applicable Parity Obligations) or suspended a Rating or (b) a Change of Law shall occur which could reasonably be expected to result in a material adverse effect on the ability of the Applicant to pay any Obligation when due.

"Master Installment Purchase Contract" means the Master Installment Purchase Contract dated as of November 1, 1997 between the Issuer and the Applicant.

"Material Adverse Effect" means a materially adverse effect upon (a) the business, assets, liabilities, financial condition, results of operations or business prospects of the Water Utility System, and (b) the binding nature, validity or enforceability of the Applicant's obligations under the Applicant Related Documents, or the Applicant's ability to perform its material obligations under the Applicant Related Documents.

"Moody's" means Moody's Investors Service.

"Obligations" means (a) the Reimbursement Obligations, (b) the obligation of the Applicant to pay to the Bank all fees and expenses under the Fee Letter and (c) the obligation of the Applicant to pay to the Bank any other amounts set forth in the Related Documents (other than those described in clauses (a) and (b) immediately above).

"Parity Obligations" has the meaning set forth in the Purchase Contract.

"Payment Agreement" has the meaning set forth in the Purchase Contract.

"Payments" has the meaning set forth in the Purchase Contract.

"Person" means an individual, a corporation, a partnership, an association, a trust or any other entity or organization, including a government or political subdivision or any agency or instrumentality thereof.

"Potential Default" means an event or condition which, but for the lapse of time or the giving of notice, or both, would constitute an Event of Default.

"Prime Rate" means the rate of interest announced by the Bank from time to time as its prime commercial rate for U.S. dollar loans, or equivalent, as in effect on such day, with any change in the Prime Rate resulting from a change in said prime commercial rate to be effective as of the date of the relevant change in said prime commercial rate.

"Property" means any interest in any kind of property or asset, whether real, personal or mixed, or tangible or intangible, whether now owned or hereafter acquired, which comprise the Water Utility System.

“Purchase Contract” means the Master Installment Purchase Contract as supplemented by the 2006 Supplemental Installment Purchase Contract and the 2008 Supplemental Installment Purchase Contract.

“Rating” means, with respect to a Rating Agency, the lowest rating assigned by such Rating Agency to any long-term unenhanced indebtedness (including certificates of participation) of the Applicant secured by Gross Revenues.

“Rating Agency” means Moody’s and/or S&P as the context may require.

“Reimbursement Obligations” means any and all obligations of the Applicant to reimburse the Bank for any drawings under the Letter of Credit and all obligations to repay the Bank for any Liquidity Advance.

“Related Documents” means the Bank Documents, the Cancellation Agreement, the Certificates of Participation Documents and any other agreement or instrument relating thereto.

“Remarketing Agent” means the Person appointed from time to time by the Applicant or the Issuer, as the case may be, to remarket the Certificates of Participation.

“Remarketing Agreement” means, as of any date, the Remarketing Agreement in effect on such date between the Applicant and the Remarketing Agent.

“Reoffering Circular” means the Reoffering Circular of the Issuer related to the reoffering of the Certificates of Participation supported by the Letter of Credit, together with all supplements and amendments thereto.

“S&P” means Standard & Poor’s, a division of The McGraw-Hill Companies, Inc.

“Standard Letter of Credit Practice” means, for the Bank, any domestic law or letter of credit practice applicable in the city in which the Bank issued the Letter of Credit. Such practices shall be (a) of banks that regularly issue letters of credit in the particular city and (b) required or permitted under the ISP.

“State” means the State of California.

“Stated Expiration Date” has the meaning set forth in the Letter of Credit.

“Subordinate Obligations” has the meaning set forth in the Purchase Contract.

“Subrogated Certificate” means any Certificate of Participation with respect to which, pursuant to Section 10.05 of the Trust Agreement, the Bank, to the extent it has paid the principal of such Certificate from a drawing under the Letter of Credit, has become subrogated to, and the assignee of, the rights to receive payment of such principal from the Issuer pursuant to the Trust Agreement and has become the owner of such Certificate.

“Swap” means any interest rate swap agreement, forward payment conversion agreement, futures or contracts providing for payment based on levels of, or changes in, interest rates or other indices, or contracts to exchange cash flows or a series of payments or contracts, including,

without limitation, interest rate floors or caps, options, puts or calls to hedge payment, rate, spread or similar exposure.

“Tax Event” means a determination (whether by entry of any decree or judgment by a court of competent jurisdiction, the taking of any official action by the Internal Revenue Service or the delivery to the Applicant, the Trustee and the Bank of an opinion of nationally recognized bond counsel acceptable to the District, the Paying Agent and the Bank) that interest with respect to any of the Certificates of Participation is includable in the gross income of the owners thereof for federal income tax purposes (including by reason of such Certificates of Participation being declared invalid, illegal or unenforceable by a court of competent jurisdiction, whether or not such declaration is appealable or deemed to be final under applicable procedural law, or by operation of law).

“Termination Date” has the meaning set forth in the Letter of Credit.

“Trust Agreement” means the Amended and Restated Trust Agreement dated as of May 1, 2008, as amended and restated as of July 14, 2011, in each case by and between the Issuer and the Trustee.

“Trustee” means The Bank of New York Mellon Trust Company, N.A. (formerly known as The Bank of New York Trust Company, N.A.) in its capacity as trustee for the owners of the Certificates of Participation, and any successor trustee for the owner of the Certificates of Participation.

“2008 Supplemental Installment Purchase Contract” means the 2008 Supplemental Installment Purchase Contract dated as of May 1, 2008 between the Issuer and the Applicant.

“2006 Supplemental Installment Purchase Contract” means the 2006 Supplemental Installment Purchase Contract dated as of November 1, 2006 between the Issuer and the Applicant.

“Water Utility System” has the meaning set forth in the Purchase Contract.

“Wire Instructions” means JPMorgan Chase Bank, N.A., New York, New York, ABA number: 021000021, Account No. 324331754, Reference: Letter of Credit No. CPCS-923992, City of Modesto, or such other bank, ABA number, account number or reference as the Bank may designate in writing to the Applicant.

Section 1.2 Incorporation By Reference. Any capitalized terms used herein which are not specifically defined herein shall have the same meanings herein as in the Trust Agreement.

Section 1.3 Construction. The definitions of terms herein shall apply equally to the singular and plural forms of the terms defined. Whenever the context may require, any pronoun shall include the corresponding masculine, feminine and neuter forms. The words “include”, “includes” and “including” shall be deemed to be followed by the phrase “without limitation”. The word “will” shall be construed to have the same meaning and effect as the word “shall”. Unless the context requires otherwise (a) any definition of or reference to any agreement, instrument or other document herein shall be construed as referring to such agreement, instrument or other document as from time to time amended, supplemented or otherwise modified (subject to any restrictions on such amendments, supplements or modifications set forth

herein), (b) any reference herein to any Person shall be construed to include such Person's successors and assigns, (c) the words "herein", "hereof" and "hereunder", and words of similar import, shall be construed to refer to this Agreement in its entirety and not to any particular provision hereof and (d) all references herein to Sections, Schedules and Exhibits shall be construed to refer to Sections of, and Schedules and Exhibits to, this Agreement.

Section 1.4 Time References. All references in this Agreement to times of day shall be references to New York time unless otherwise expressly provided herein.

Section 1.5 GAAP References. Unless otherwise inconsistent with the terms of this Agreement, all accounting terms shall be interpreted and all accounting determinations hereunder shall be made in accordance with GAAP.

## ARTICLE 2 LETTER OF CREDIT

Section 2.1 Letter of Credit. Upon the terms, subject to the conditions and relying upon the representations and warranties set forth in this Agreement or incorporated herein by reference, the Bank agrees to issue the Letter of Credit. The Letter of Credit shall be in the original stated amount of U.S. \$47,625,989, which is the sum of (i) the principal amount of Certificates of Participation outstanding on the Closing Date, plus (ii) interest thereon at 12% per annum for a period of 35 days.

Section 2.2 Letter of Credit Drawings. The Trustee is authorized to make drawings under the Letter of Credit in accordance with the terms thereof. The Applicant hereby directs the Bank to make payments under the Letter of Credit in the manner therein provided. The Applicant hereby irrevocably approves reductions and reinstatements of the Available Amount as provided in the Letter of Credit.

Section 2.3 Reimbursement of Certain Liquidity Drawings Under the Letter of Credit; Prepayment; Interest.

(a) The principal component of each Liquidity Drawing made under the Letter of Credit shall constitute an advance ("Liquidity Advance") to the Applicant; *provided, however*, if the Insurance Policy Cancellation Date has occurred a Liquidity Drawing shall not automatically become a Liquidity Advance unless the conditions precedent set forth in Section 3.2 hereof are satisfied at the time of payment by the Bank of such Liquidity Drawing (the date of such Liquidity Drawing, the "Liquidity Drawing Date"). The Applicant promises to repay each Liquidity Advance and prepay the corresponding Bank Certificate or Bank Certificates in ten equal installments of principal commencing with the date that is six months following the Liquidity Drawing Date and continuing on each date that is six months thereafter with the final installment to be repaid no later than the fifth anniversary of the applicable Liquidity Drawing Date. The Applicant also promises to prepay each Liquidity Advance on (i) the date on which any Certificates of Participation purchased with funds disbursed under the Letter of Credit in connection with the Liquidity Drawing which gave rise to such Liquidity Advance are prepaid or cancelled pursuant to the Trust Agreement, which prepayment shall be made in a principal amount equal to the principal amount of Certificates of Participation prepaid or cancelled, (ii) the date on which any Certificates of Participation purchased with funds disbursed under the Letter

of Credit in connection with the Liquidity Drawing which gave rise to such Liquidity Advance are remarketed pursuant to the Trust Agreement, which prepayment shall be made in a principal amount equal to the principal amount of Certificates of Participation remarketed, (iii) the date on which the Certificates of Participation are converted to bear interest at a rate other than a daily rate or weekly rate, which prepayment shall be made in a principal amount equal to the principal amount of Certificates of Participation so converted, (iv) the date on which the Letter of Credit is replaced by a substitute letter of credit pursuant to the terms of the Trust Agreement and the Purchase Agreement, which prepayment shall be made in full, (v) if the Insurance Policy Cancellation Date has occurred, the date on which an Event of Default of the type described in Section 6.1(g) or 6.1(h) occurs, which prepayment shall be made in full, and (vi) the date on which the Bank gives notice to the Applicant pursuant to Section 6.3, with the consent of the Insurer if required by Section 6.3, that all Obligations have been accelerated as a result of the occurrence of an Event of Default (other than Event of Default of the type described in Section 6.1(g) or 6.1(h)), which prepayment shall be made in full. Subject to Section 2.14 hereof, the Applicant also promises to pay to the Bank interest with respect to the unpaid principal amount of each Liquidity Advance from the date such Liquidity Advance is made until it is paid in full as provided herein, at a rate per annum equal to the Bank Rate from time to time in effect, payable in arrears on each date the Liquidity Advance is payable or prepayable as herein provided and on the first Business Day of each calendar month. Any Liquidity Advance not paid when due shall bear interest at the Default Rate. Notwithstanding anything set forth herein to the contrary, the Bank hereby acknowledges and agrees that the Insurance Policy will not insure interest on the interest portion of any Liquidity Advance.

(b) Any Liquidity Advance created pursuant to paragraph (a) above may be prepaid in whole or in part at any time on any Business Day without premium or penalty. Upon the Bank's receipt of any payment or prepayment of any Liquidity Advance, the amount of such Liquidity Advance shall be reduced by the amount of such payment or prepayment and each remaining installment shall be reduced proportionately as nearly as possible.

Section 2.4 Reimbursement of Drawings Other Than Liquidity Drawings Creating Liquidity Advances Under the Letter of Credit. The Applicant agrees to reimburse the Bank for the full amount of the interest component of each Liquidity Drawing on the date such Liquidity Drawing is honored by the Bank. If the Insurance Policy Cancellation Date has occurred, the Applicant agrees to reimburse the Bank for the full amount of (a) the principal component of each Liquidity Drawing (but only if the conditions precedent contained in Section 3.2 hereof are not satisfied on the date of payment by the Bank of such Liquidity Drawing) and (b) all other drawings made under the Letter of Credit, in each case, on the same date of each such drawing. If the Insurance Policy Cancellation Date has not occurred, the Applicant agrees to reimburse the Bank for the full amount of all drawings, other than Liquidity Drawings, made under the Letter of Credit on the same date of each such drawing. If the Applicant does not make such reimbursement on such date, such reimbursement obligation shall bear interest at the rate per annum specified in Section 2.9 hereof.

Section 2.5 Certain Fees and Expenses. The Applicant hereby agrees to pay, or cause to be paid, to the Bank the fees, expenses and other amounts set forth in the Fee Letter at the times and in the manner set forth in the Fee Letter, which Fee Letter, by this reference, is incorporated herein as if set forth herein in its entirety.

Section 2.6 Method of Payment; Etc. All payments to be made by the Applicant under this Agreement shall be made to the Bank in lawful money of the United States of America in freely transferable and immediately available funds in accordance with the Wire Instructions and shall be received by the Bank not later than 2:00 p.m. on the date when due.

Section 2.7 Computation of Interest and Fees. All computations of fees payable by the Applicant under this Agreement and/or the Fee Letter shall be made on the basis of a 360-day year and actual days elapsed. All computations of interest payable by the Applicant under this Agreement shall be made on the basis of a 365/366-day year and actual days elapsed. Interest shall accrue during each period during which interest is computed from and including the first day thereof to and including the last day thereof.

Section 2.8 Payment Due on Non-Business Day to Be Made on Next Business Day. If any sum becomes payable pursuant to this Agreement on a day which is not a Business Day, the date for payment thereof shall be extended, without penalty, to the next succeeding Business Day, and such extended time shall be included in the computation of interest and fees.

Section 2.9 Late Payments. If the principal amount of any Obligation is not paid when due (including by the Insurer in accordance with the Insurance Policy, if such Obligation is insured thereby), such Obligation shall bear interest until paid in full at a rate per annum equal to the Default Rate, payable on demand.

Section 2.10 Source of Funds. All payments made by the Bank pursuant to the Letter of Credit shall be made from funds of the Bank, and not from the funds of any other Person.

Section 2.11 Extension of Stated Expiration Date. At any time there shall remain no less than 90 days and no more than 120 days prior to the then current Stated Expiration Date, the Applicant may request the Bank to extend the then current Stated Expiration Date for an additional period. If the Bank, in its sole discretion, elects to extend the Stated Expiration Date then in effect, the Bank shall give written notice of such election to extend to the Applicant and the Trustee within 30 days of receipt of such extension request from the Applicant, it being understood and agreed that the failure of the Bank to notify the Applicant and the Trustee of any decision within such 30-day period shall be deemed to be a rejection of such request and the Bank shall not incur any liability or responsibility whatsoever by reason of the Bank's failure to notify such parties within such 30-day period. The Bank's consent to any such extension of the Stated Expiration Date shall be conditioned upon the preparation, execution and delivery of documentation in form and substance satisfactory to the Bank and its counsel. Any date to which the Stated Expiration Date has been extended in accordance with this Section 2.11 may be extended in like manner.

Section 2.12 Amendments Upon Extension. Upon any extension of the Stated Expiration Date pursuant to Section 2.11 of this Agreement, the Bank and the Applicant each reserves the right to renegotiate any provision hereof.

Section 2.13 Electronic Transmissions. The Bank is authorized to accept and process any amendments, transfers, assignments of proceeds, Instructions, consents, waivers and all documents relating to the Letter of Credit which are sent to Bank by electronic transmission, including SWIFT, electronic mail, telex, telecopy, courier, mail or other computer generated telecommunications and such electronic communication shall have the same legal effect as if

written and shall be binding upon and enforceable against the Applicant. The Bank may, but shall not be obligated to, require authentication of such electronic transmission or that the Bank receives original documents prior to acting on such electronic transmission.

Section 2.14 Recapture. Any interest payable pursuant to this Agreement, the Fee Letter or the other Related Documents shall not exceed the maximum amount permitted by law (the "Highest Lawful Rate"). In the event any interest required to be paid hereunder at any time exceeds the Highest Lawful Rate, the portion of such interest required to be paid on a current basis shall equal such Highest Lawful Rate; *provided, however*, that the differential between the amount of interest payable assuming no Highest Lawful Rate and the amount paid on a current basis after giving effect to the Highest Lawful Rate ("Excess Interest") shall be carried forward and shall be payable on any subsequent date of calculation so as to result in a recovery of interest previously unrealized (because of the limitation dictated by such Highest Lawful Rate) at a rate of interest, and as part of the interest payable, that, after giving effect to the recovery of such excess and all other interest paid and accrued hereunder to the date of calculation, does not exceed such Highest Lawful Rate. In consideration for the limitation of the rate of interest otherwise payable hereunder, the Fee Letter and the other Related Documents, to the extent permitted by law, the Applicant shall pay to the Bank a fee equal to the amount of all unpaid deferred Excess Interest upon the termination of this Agreement and the final payment hereunder.

Section 2.15 Security. The Obligations are special, limited obligations of the Applicant payable solely from and secured by the Gross Revenues.

### ARTICLE 3 CONDITIONS PRECEDENT

Section 3.1 Conditions Precedent to Issuance of Letter of Credit. As conditions precedent to the obligation of the Bank to issue the Letter of Credit, (a) the Applicant shall provide to the Bank on the Closing Date, in form and substance satisfactory to the Bank and its counsel, White & Case LLP (hereinafter, "Bank's counsel"):

- (i) a written opinion or opinions of counsel to the Applicant, dated the Closing Date and addressed to the Bank;
- (ii) a reliance letter from Sidley Austin LLP, Certificates of Participation counsel, dated the Closing Date and addressed to the Bank, permitting the Bank to rely on its opinion rendered at the time the Certificates of Participation were originally issued;
- (iii) the written opinion of counsel to the Issuer, dated the Closing Date and addressed to the Bank;
- (iv) the written opinion of counsel to the Insurer, dated the Closing Date and addressed to the Bank, (A) permitting the Bank to rely on the opinion of counsel to the Insurer rendered at the time the Insurance Policy was originally issued, (b) addressing the enforceability of the Bank Certificate Endorsement and (c) addressing the enforceability of the Cancellation Agreement;

(v) the written opinion of counsel to the Trustee, dated the Closing Date and addressed to the Bank, addressing the enforceability of the Cancellation Agreement;

(vi) a certificate signed by a duly authorized officer of the Applicant, dated the Closing Date and stating that:

(A) the representations and warranties of the Applicant contained in Article 4 that are not qualified by "material," "materiality," "Material Adverse Effect" or similar qualifier are true and correct in all material respects on and as of the Closing Date as though made on and as of such date, except to the extent any such representation or warranty relates specifically to an earlier date in which case such representation and warranty shall be true and correct in all material respects as of such earlier date;

(B) the representations and warranties of the Applicant contained in Article 4 that are qualified by "material," "materiality," "Material Adverse Effect" or similar qualifier are true and correct in all respects on and as of the Closing Date as though made on and as of such date, except to the extent any such representation or warranty relates specifically to an earlier date in which case such representation and warranty shall be true and correct in all respects as of such earlier date; and

(C) no Event of Default or Potential Default or Insurer Default has occurred and is continuing, or would result from the issuance of the Letter of Credit or the execution, delivery or performance of this Agreement or any Related Document to which the Applicant is a party; and

(D) the electronic copy of the Applicant's charter available at [www.ci.modesto.ca.us/](http://www.ci.modesto.ca.us/) is accurate and complete;

(vii) evidence of the due authorization, execution and delivery by the parties thereto of the Related Documents;

(viii) a copy of resolutions of the city council of the Applicant and all other necessary approvals, if any, certified as of the Closing Date by the city clerk of the Applicant, authorizing, among other things, the execution, delivery and performance by the Applicant of the Related Documents to which it is a party and the issuance of the Letter of Credit;

(ix) true and correct copies of all Governmental Approvals, if any, necessary for the Applicant to execute, deliver and perform the Related Documents to which it is a party and to authorize the Applicant to obtain the issuance of the Letter of Credit;

(x) evidence that the Applicant has received all consents and other approvals from creditors necessary for the Applicant to execute, deliver and perform the Related Documents to which it is a party and to authorize the Applicant to obtain the issuance of the Letter of Credit;

(xi) a certificate of the city clerk of the Applicant certifying the names and true signatures of the officers of the Applicant authorized to sign the Related Documents to which the Applicant is a party;

(xii) certified copies of documents evidencing all necessary action taken by the Issuer to authorize the execution and delivery of the Related Documents to which it is a party;

(xiii) evidence that Bank Certificates have been assigned a CUSIP number that is unique and distinct from the CUSIP number assigned to Certificates of Participation that are not Bank Certificates;

(xiv) evidence that either Moody's or S&P has assigned a long-term unenhanced rating to the Bank Certificates of "Baa3" or "BBB-", respectively, or better;

(xv) an executed original of an endorsement to the Insurance Policy (the "Bank Certificate Endorsement") so that the Insurance Policy as endorsed insures the payment when due of regularly scheduled principal of and interest with respect to the Certificates of Participation, including any Bank Certificates and Subrogated Certificates, but in the case of interest on Bank Certificates and Subrogated Certificates the amount thereof insured shall not exceed the amount that would accrue thereon if interest accrued at the Insured Rate, such endorsement to be in form and substance satisfactory to the Bank; and

(xvi) executed originals of each of the Related Documents (other than the Letter of Credit and the Certificates of Participation) and such other documents, certificates and opinions as the Bank or Bank's counsel may reasonably request;

(b) no law, regulation, ruling or other action of the United States or the States of California, Illinois or New York or any political subdivision or authority therein or thereof shall be in effect or shall have occurred, the effect of which would be to prevent the Bank from fulfilling its obligations under this Agreement or the Letter of Credit; and

(c) all legal requirements provided herein incident to the execution, delivery and performance of the Related Documents and the transactions contemplated thereby, shall be reasonably satisfactory to the Bank and Bank's counsel.

Section 3.2 Conditions Precedent to Liquidity Advances After the Insurance Policy Cancellation Date. Following any payment by the Bank under the Letter of Credit pursuant to a Liquidity Drawing made after the Insurance Policy Cancellation Date has occurred, a Liquidity Advance shall be made available to the Applicant only if on the date of payment of such Liquidity Drawing by the Bank the following statements shall be true:

(a) the representations and warranties of the Applicant contained in Article 4 and in the other Related Documents that are not qualified by "material," "materiality," "Material Adverse Effect" or similar qualifier shall be true and correct in all material respects on and as of the date of such payment as though made on and as of such date, except to the extent any such representation or warranty relates specifically to an earlier date in which case such representation and warranty shall be true and correct in all material respects as of such earlier date;

(b) the representations and warranties of the Applicant contained in Article 4 and in the other Related Documents that are qualified by “material,” “materiality,” “Material Adverse Effect” or similar qualifier shall be true and correct in all respects on and as of the date of such payment as though made on and as of such date, except to the extent any such representation or warranty relates specifically to an earlier date in which case such representation and warranty shall be true and correct in all respects as of such earlier date; and

(c) no event has occurred and is continuing, or would result from such payment, which constitutes a Potential Default or Event of Default.

Unless the Applicant shall have previously advised the Bank in writing that one or more of the above statements are no longer true, the Applicant shall be deemed to have represented and warranted on the date of such payment that all of the above statements are true and correct.

#### ARTICLE 4 REPRESENTATIONS AND WARRANTIES

In order to induce the Bank to enter into this Agreement, the Applicant represents and warrants to the Bank as follows:

Section 4.1 Organization and Powers. The Applicant is a municipality and chartered city of the State duly organized and validly existing under and pursuant to the Constitution and laws of the State, including its city charter. The Applicant has full right, power and authority to (a) enter into the Applicant Related Documents and to perform each and all of the matters and things therein provided for and (b) own and operate the Water Utility System.

Section 4.2 Authorization; No Contravention; Approvals. The execution, delivery and performance by the Applicant of the Applicant Related Documents are within the Applicant’s powers. The execution, delivery and performance by the Applicant of the Applicant Related Documents do not and will not violate (a) any provision of the Applicant’s charter; (b) any provision of any law, rule, regulation, order, writ, judgment, injunction, decree, determination or award to which the Applicant is subject, including Environmental Laws; (c) result in a breach of or constitute a default under the provisions of any resolution, indenture, trust agreement, loan or credit agreement, Payment Agreement or any other agreement, lease or instrument to which the Applicant is subject or by which it, or its Property, is bound; or (d) result in, or require, the creation or imposition of any mortgage, deed of trust, assignment, pledge, lien, security interest or other charge or encumbrance of any nature or with respect to any of the Property of the Applicant other than as provided therein. The Applicant is not in default under any such law, rule, regulation, order, writ, judgment, injunction, decree, determination or award or any such resolution, indenture, trust agreement, loan or credit agreement, Payment Agreement or any other agreement, lease or instrument. All Governmental Approvals and all consents and approvals of other Persons necessary for the Applicant to (i) execute, deliver and perform its obligations under the Applicant Related Documents and (ii) own and operate the Water Utility System have been obtained.

Section 4.3 Binding Effect. (a) Each Applicant Related Document constitutes the legal, valid and binding obligation of the Applicant, enforceable against the Applicant in accordance with its terms, except as such enforceability may be limited by the Applicant’s bankruptcy, insolvency, reorganization or other laws or equitable principles relating to or limiting creditors’

rights generally, and (b) each of the Certificates of Participation has been duly executed and delivered pursuant to the Trust Agreement and is entitled to the benefits thereof.

Section 4.4 Financial Information. All information supplied by the Applicant to the Bank relating to the Applicant and the Water Utility System is true and accurate in all material respects including, without limitation, the Applicant's audited proprietary funds statement of net assets as of June 30, 2010, statement of revenues, expenses and changes in fund net assets for the year ended June 30 2010 and statement of cash flows for the year ended June 30, 2010 and the unqualified opinion letter dated November 30, 2010, of Brown Armstrong Accountancy Corporation, independent certified public accountants, copies of which have been delivered to the Bank, is in all respects complete and correct and fairly present the financial condition of the Applicant as at such dates for the periods covered by such statements, all in conformity with GAAP. Since the date of the most recent financial statement delivered to the Bank, there has been no material adverse change in the condition (financial or otherwise) of the business or operations of the Applicant. The Applicant has no contingent liabilities that are material to it other than as indicated on the most recent financial statements delivered to the Bank.

Section 4.5 Litigation. There are no actions, suits, proceedings, inquiries or investigations, at law or in equity, before any court, Governmental Authority or arbitrator pending or, to the best knowledge of the Applicant, threatened, against or directly involving the Applicant, affecting the existence of the Applicant, the title of any officials of the Applicant to their respective offices, the Water Utility System or affecting or seeking to prohibit, restrain or enjoin the execution or delivery of any Applicant Related Document, or in any way contesting or affecting the validity or enforceability of the Certificates of Participation, any Applicant Related Document or contesting the tax exempt status of the Certificates of Participation, or contesting in any way the completeness or accuracy of the Reoffering Circular, or contesting the powers of the Applicant or any authority for the issuance of the Certificates of Participation, the execution and delivery of the Applicant Related Documents, nor, to the best, knowledge of the Applicant, is there any basis therefor, which, if determined adversely to the Applicant could reasonably be expected to (i) have a Material Adverse Effect or (ii) result in a Tax Event.

Section 4.6 Employee Benefit Plans, Etc. The Applicant is not subject to Title I reporting and disclosure requirements, Title II or Title IV of ERISA and has no obligation or liability under or in respect of any "employee benefit plan" within the meaning of Section 3(3) of ERISA or any other form of bonus, incentive compensation, deferred compensation or other similar plan or arrangement. The Applicant currently has a pension plan providing benefits for its employees. Such pension plan is in compliance in all material respects with the requirements of the applicable laws of the State, including without limitation the obligation of the Applicant to pay contributions on behalf of its employees in accordance therewith. No condition exists or event or transaction has occurred with respect to the Applicant's pension plan which could reasonably be expected to result in the incurrence by the Applicant of any material liability, fine or penalty that would be payable from Gross Revenues.

Section 4.7 Environmental Laws. The Applicant has not received notice to the effect that the operations of the Water Utility System are not in compliance with any of the requirements of applicable federal, state or local environmental, health and safety statutes and regulations or are the subject of any governmental investigation evaluating whether any remedial action is needed to respond to a release of any toxic or hazardous waste or substance into the

environment, which non-compliance or remedial action could reasonably be expected to result in a Material Adverse Effect.

Section 4.8 No Sovereign Immunity. The Applicant is subject to civil and commercial law in respect of its obligations under the Applicant Related Documents. The Applicant does not enjoy any right of immunity in respect of such obligations on the grounds of immunity (sovereign or otherwise) from jurisdiction in any court or from setoff or any legal process, whether through service or notice, attachment prior to judgment, attachment in aid of execution or otherwise, under the laws of the United States of America and the State.

Section 4.9 Disclosure. No representation, warranty or other written statement made by the Applicant in or pursuant to any Applicant Related Document, or any other document or financial statement provided by the Applicant to the Bank in connection with any Related Document, contains any untrue statement of a material fact or omits (as of the date made or furnished) any material fact necessary to make the statements therein not misleading in light of the circumstances under which they are made. There is no fact known to the Applicant which the Applicant has not disclosed to the Bank in writing which could reasonably be expected to result in a Material Adverse Effect. Except for information contained in the Reoffering Circular under the headings "THE JPMORGAN LETTER OF CREDIT AND THE REIMBURSEMENT AGREEMENT," "INFORMATION CONCERNING JPMORGAN" and "INFORMATION CONCERNING ASSURED GUARANTY CORP.," as to which no representation is made, the Reoffering Circular is, and any supplement or amendment to the Reoffering Circular shall be, accurate in all material respects for the purpose for which its use is, was or shall be, authorized; and except for information contained in the Reoffering Circular under the previously mentioned captions, as to which no representation is made, the Reoffering Circular does not, and any such supplement or amendment will not, contain any untrue statement of a material fact or omit to state any material fact necessary to make the statements made therein, in the light of the circumstances under which they are or were made, not misleading.

Section 4.10 Margin Stock. The Applicant is not engaged in the business of extending credit for the purpose of purchasing or carrying margin stock (within the meaning of Regulation U of the Board of Governors of the Federal Reserve System), and no part of the proceeds of any Liquidity Advance or of any drawing under the Letter of Credit will be used to purchase or carry any such margin stock or extend credit to others for the purpose of purchasing or carrying any such margin stock.

Section 4.11 Marketable Fee. The Applicant has good and marketable title to the Water Utility System. The Water Utility System is an essential asset of the Applicant necessary to serve the needs of the Applicant. The Applicant believes that at all times while any Payments or any obligation of the Applicant under the Applicant Related Documents remains unpaid, the Water Utility System will remain an essential asset of the Applicant.

Section 4.12 Casualty. The Water Utility System is not currently affected by any fire, explosion, accident, strike, lockout or other labor dispute, drought, storm, hail, earthquake, embargo, act of God or of the public enemy or other casualty (whether or not covered by insurance).

Section 4.13 No Defaults. No Potential Default or Event of Default has occurred and is continuing.

Section 4.14 Usury. The obligations of the Applicant under the Bank Documents are not subject to any law, rule or regulation of the State prescribing a maximum rate of interest.

Section 4.15 Solvency. The Applicant is able to pay its debts and satisfy its liabilities as they come due, is solvent and has not made any assignment for the benefit of creditors.

Section 4.16 Security. The Purchase Contract creates a valid perfected security interest in the Gross Revenues as security for the punctual payment of the interest and principal due with respect to the Bank Certificates and all Obligations. The Reimbursement Obligations constitute Parity Obligations. All Obligations other than Reimbursement Obligations are Subordinate Obligations. Except for early termination payments under the Existing Swap Agreement that are insured by the Insurer, the Applicant is not a party to any Swap that contains termination payments that are Parity Obligations. The Issuer has validly assigned all of its right to receive Payments to the Trustee under the Trust Agreement.

Section 4.17 Tax-Exempt Status. The Applicant has not taken any action or omitted to take any action, and knows of no action taken or omitted to be taken by any other Person, which action, if taken or omitted, would adversely affect the exclusion of interest on the Certificates of Participation from gross income for Federal income tax purposes or the exemption of such interest from State personal income taxes.

Section 4.18 Legal Matters. There is no amendment, or, to the best knowledge of the Applicant, proposed amendment certified for placement on a statewide ballot, to the Constitution of the State or any published administrative interpretation of the Constitution of the State or any State law, or any legislation which has passed either house of the State legislature or is under consideration by any conference or similar committee, or any published judicial or administrative decision interpreting any of the foregoing, and no action has been passed by the city council of the Applicant, the effect of which could reasonably be expected to have a Material Adverse Effect.

Section 4.19 Incorporation of Representations and Warranties by Reference. The Applicant hereby makes to the Bank the same representations and warranties as are set forth by it in each Applicant Related Document (other than this Agreement), which representations and warranties, as well as the related defined terms contained therein, are hereby incorporated herein by reference for the benefit of the Bank, *mutatis mutandis*, with the same effect as if each and every such representation and warranty and defined term were set forth herein in its entirety and were made as of the date hereof. No amendment to such representations and warranties or defined terms made pursuant to any Applicant Related Document shall be effective to amend such representations and warranties and defined terms as incorporated by reference herein without the prior written consent of the Bank.

## ARTICLE 5 COVENANTS

The Applicant will do, or will refrain from doing, as applicable, the following so long as any amounts may be drawn under the Letter of Credit or any Obligations remain outstanding under this Agreement, unless the Bank shall otherwise consent in writing:

Section 5.1 Existence. The Applicant will preserve and maintain its existence, rights and franchises as a city duly organized and existing under the laws of the State and will not merge, combine or consolidate with any other Person.

Section 5.2 Maintenance of Properties. The Applicant will maintain, preserve and keep the Water Utility System in good repair, working order and condition (ordinary wear and tear excepted).

Section 5.3 Taxes and Assessments. The Applicant will pay all taxes, assessments and governmental charges imposed upon it or the Water Utility System before the same become delinquent, unless and to the extent that the same are being contested in good faith and by appropriate proceedings and reserves are provided therefor that in the opinion of the Applicant are adequate.

Section 5.4 Insurance. The Applicant shall maintain insurance as required by Section 4.08 of the Purchase Contract. The Applicant shall cause the Bank to be named an additional insured on such policies and shall require that all providers of such insurance will provide the Bank with not less than 30 days prior written notice of any intended cancellation thereof or reduction of coverage provided thereby.

Section 5.5 Reports; Notices. The Applicant will maintain a standard system of accounting in accordance with GAAP and will furnish to the Bank such information respecting the business and financial condition of the Applicant as the Bank may reasonably request; and without any request, will furnish to the Bank:

(a) as soon as available and in any event within 180 days after the end of each fiscal year of the Applicant, an audited statement of net assets for the Water Utility System of the Applicant as of the end of such fiscal year, an audited statement of revenues, expenses and changes in fund net assets for the Water Utility System of the Applicant for such fiscal year and an audited statement of cash flows for the Water Utility System of the Applicant for such fiscal year, in each case prepared in accordance with GAAP and in reasonable detail showing in comparative form the figures for the previous fiscal year, accompanied by an opinion thereon of a firm of independent public accountants of recognized national standing, selected by the Applicant and reasonably acceptable to the Bank, to the effect that, in the opinion of such firm, (i) the audit was conducted in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States and (ii) the Water Utility System financial statements of the Applicant present fairly, in all material respects, the financial position of the Water Utility System of the Applicant, as of the end of the applicable fiscal year, and the changes in financial position and cash flows thereof for the applicable fiscal year then ended in conformity with GAAP, which opinion shall contain no qualifications other than qualifications relating to the implementation of rules issued by the Government Accounting Standards Board (the failure to comply with which would not, in the opinion of the Bank in its sole discretion, individually or in the aggregate, have a material impact on any fund financial statement line item);

(b) as soon as available and in any event within 45 days after the end of each fiscal quarter of the Applicant, an unaudited statement of net assets for the Water Utility System of the

Applicant as of the end of such fiscal quarter, an unaudited statement of revenues, expenses and changes in fund net assets for the Water Utility System of the Applicant for such fiscal quarter and an unaudited statement of cash flows for the Water Utility System of the Applicant for such fiscal quarter, in each case prepared in accordance with GAAP and in reasonable detail showing in comparative form the figures for the corresponding fiscal quarter of the prior fiscal year;

(c) simultaneously with the delivery of each set of financial statements referred to in clauses (a) and (b) above, a certificate of the Applicant stating that, to the best knowledge of the chief financial officer (or his/her designee) of the Applicant, there exists on the date of such certificate no Event of Default or Potential Default or, if any Event of Default or Potential Default then exists, setting forth the details thereof and the action which the Applicant is taking or proposes to take with respect thereto;

(d) promptly (and, in any event, no later than 5 Business Days) after knowledge thereof by the Applicant, written notice of the occurrence of any Potential Default, Event of Default or Insurer Default together with a statement of the Applicant setting forth the details thereof and the action which the Applicant is taking or proposes to take with respect thereto;

(e) promptly after process has been served on the Applicant, notice of any action, suit or proceeding before any court or Governmental Authority in which there is a reasonable probability of an adverse decision which could reasonably be expected to result in a Material Adverse Effect;

(f) promptly upon the availability thereof, a copy of any official statement, offering memorandum or other disclosure documents relating to the offering, reoffering or remarketing of any Parity Obligations;

(g) promptly after obtaining knowledge thereof, written notice of any change in the long term ratings assigned by a Rating Agency to any unenhanced Parity Obligations;

(h) as soon as available to the Applicant, copies of all enacted legislation which, to the best knowledge of the Applicant, relates to, in any material way, or adversely impacts in any material manner upon the Related Documents or the ability of the Applicant to perform its obligations under the Applicant Related Documents;

(i) promptly upon the adoption thereof, a copy of the Water Utility System's 5-year financial plan and the Applicant's budget, together with each amendment or supplement thereto that may be adopted from time to time during each fiscal year; and

(j) notice of any event or circumstance known to the Applicant which might result in a Material Adverse Effect;

(k) notice of the failure by the Remarketing Agent or the Trustee to perform any of their respective obligations under any Related Document to which any such entity is a party;

(l) notice of any inquiry, investigation or audit or threatened inquiry, investigation or audit of the Applicant or its securities by the Securities and Exchange Commission, the Department of Justice or the Internal Revenue Service;

(m) notice and a copy of any amendment to the Applicant's investment policy guidelines; and

(n) notice of any proposed amendment or supplement to any Certificates of Participation Document and copies of all such amendments and supplements promptly following the execution thereof.

Section 5.6 Inspection and Field Audit. Upon prior notice from the Bank, the Applicant will permit the Bank and its duly authorized representatives and agents to visit and inspect any of the Properties, corporate books and financial records of the Applicant and the Water Utility System, to examine and make copies of the books of accounts and other financial records of the Applicant and the Water Utility System, and to discuss the affairs, finances and accounts of the Applicant and the Water Utility System with, and to be advised as to the same by, its officers and independent public accountants (and by this provision the Applicant authorizes such accountants to discuss with the Bank the finances and affairs of the Applicant and the Water Utility System) at such reasonable times and reasonable intervals as the Bank may designate.

Section 5.7 No Change in Fiscal Year. The Applicant will not change its fiscal year from its present basis without the prior written consent of the Bank.

Section 5.8 Compliance with Laws; Compliance with Agreements. The Applicant covenants that it will comply with the requirements of (a) all applicable law of any Governmental Authority having jurisdiction over the Applicant including, without limitation, all Environmental Laws applicable to the Applicant and the Water Utility System, the non compliance with which would have a Material Adverse Effect unless the same is being contested in good faith and by appropriate proceedings and such contest shall operate to stay the Material Adverse Effect of any such non compliance and (b) all investment policy guidelines of the Applicant. The Applicant will observe and perform all of its obligations under the Related Documents and any other document, agreement or instrument to which the Applicant is a party and which obligations are secured by pledge of the Gross Revenues.

Section 5.9 Certificates of Participation Documents. The Applicant will not amend or consent to any amendment of any Certificates of Participation Document, without the prior written consent of the Bank, which consent shall not be unreasonably withheld if such amendment would not have a material adverse effect on the Bank or its rights and remedies.

Section 5.10 Certificates of Participation Proceeds; Application of Drawings. The Applicant shall not permit the proceeds of the Certificates of Participation to be used for any purpose other than as set forth in the Trust Agreement. The Applicant will not take or omit to take any action, nor direct the Trustee to take any action or omit to take action, which action or omission will in any way result in the proceeds of drawings under the Letter of Credit being applied for any purpose other than to pay principal of, the purchase price of and interest with respect to the Certificates of Participation as and when the same become due and payable.

Section 5.11 Liens; Indebtedness; Swaps; Consolidation and Merger.

(a) The Applicant will not create or suffer to exist any Lien over the Gross Revenues except for the Lien created pursuant to the Purchase Contract, the Lien created pursuant to the Amended and Restated Treatment and Delivery Agreement between Modesto Irrigation District

and the City approved by the parties thereto on October 11, 2005, the Lien created in favor of the Clean Water State Revolving Fund and the Lien created pursuant to the Existing Swap Agreement. Except as provide in Section 5.11(b), the Applicant will not create or suffer to exist any Lien over the Property of the Water Utility System which could reasonably be expected to have a Material Adverse Effect. Without limiting the foregoing, in the event a non-permitted Lien attaches (i) to the Gross Revenues or (ii) to Property of the Water Utility System, in either case the Applicant shall take all action necessary to remove such Lien as soon as practicable.

(b) The Applicant will not issue or incur any additional Parity Obligations unless such issuance or incurrence complies with the Constitution and other laws of the State and with Sections 3.01 and 3.02 of the Purchase Contract. The Applicant will not issue any obligation secured by Gross Revenues that is senior in right of payment to the Reimbursement Obligations. The Applicant shall not take any action that would result in the Reimbursement Obligations not ranking at least *pari passu* in right of payment with all Parity Obligations.

(c) The Applicant shall not enter into any Swap with termination payments that are Parity Obligations.

(d) The Applicant will not consolidate the Water Utility System or merge the Water Utility System with or into any Person or sell, lease or otherwise transfer all or substantially all of the assets of the Water Utility System to any Person.

#### Section 5.12 Trustee and Remarketing Agent.

(a) The Applicant shall not remove (or cause to be removed) the Trustee or appoint (or cause to be appointed) any successor thereto without the prior written consent of the Bank, which consent shall not be unreasonably withheld. If the Trustee is removed or resigns, the Applicant shall use its best efforts to appoint (or caused to be appointed) a successor thereto that is reasonably acceptable to the Bank as soon as practicable and, in the case of resignation, no later than the resignation effective date. The Applicant shall cause any successor Trustee to enter into a Custodian Agreement with the Applicant and the Bank.

(b) The Applicant will not permit the Remarketing Agent to remarket any Certificates of Participation at a price less than the principal amount thereof plus accrued interest, if any, with respect thereto to the respective dates of remarketing. The Applicant shall not remove (or cause to be removed) the Remarketing Agent or appoint (or caused to be appointed) any successor thereto without the prior written consent of the Bank. If the Remarketing Agent fails to make efforts as required under the Remarketing Agreement to perform its duties under, and in accordance with the terms of, the Remarketing Agreement or if the Remarketing Agent fails to remarket Bank Certificates for thirty (30) consecutive calendar days, the Applicant shall, at the written direction of the Bank, remove (or cause to be removed) the Remarketing Agent. If the Remarketing Agent is removed or resigns, the Applicant shall (or shall cause) appoint a successor thereto in accordance with the terms of the Trust Agreement and with the prior written consent of the Bank. Such appointment shall be made as soon as practicable and, in the case of resignation, no later than the resignation effective date. The Applicant shall not enter into, or suffer to exist, any Remarketing Agreement unless such Remarketing Agreement contains the following: (i) an agreement on the part of the Remarketing Agent to use its best efforts to remarket Certificates of Participation, including Bank Certificates, at rates up to an including the

“Maximum Rate” (as defined in the Trust Agreement); and (ii) a provision that requires that the Remarketing Agent’s resignation shall not become effective until sixty (60) day’s following the Remarketing Agent’s delivery of written notice to the Applicant and the Bank. Without limiting the preceding sentence, the Applicant will not enter into any successor Remarketing Agreement without the prior written consent of the Bank, which consent shall not be unreasonably withheld, unless such successor Remarketing Agreement contains provisions that are substantially the same as those contained in, and affords protection to the rights and interests of the Bank that is substantially the same as that afforded by, the predecessor Remarketing Agreement.

Section 5.13 Purchase of Certificates of Participation. The Applicant will not purchase any Certificates of Participation (or any beneficial interest therein) unless such Certificate of Participation are promptly delivered to the Trustee for cancellation. In the event the Applicant purchases any Certificates of Participation, it agrees not to tender them for optional purchase.

Section 5.14 Fixed Rate Conversions. The Applicant will not convert or permit the conversion of the interest rate on less than all of the Certificates of Participation to a fixed rate to maturity.

Section 5.15 Prepayments. The Applicant shall cause Bank Certificates to be prepaid in whole prior to any other prepayment of Certificates of Participation.

Section 5.16 Alternate Credit Facility.

(a) The Applicant agrees to use its best efforts to (i) obtain an Alternate Credit Facility to replace the Letter of Credit; (ii) defease the Certificates of Participation; or (iii) convert the interest on the Certificates of Participation to a fixed interest rate to maturity in the event (A) the Bank shall determine not to extend the Stated Expiration Date or shall fail to respond to a request to extend the Stated Expiration Date, (B) the Applicant shall fail to seek an extension of the Stated Expiration Date by the date that is 60 days prior to the Stated Expiration Date or (C) the unenhanced long-term rating for any Parity Obligations shall fall below “A3” by Moody’s or below “A+” by S&P.

(b) The Applicant agrees that any Alternate Credit Facility will require, as a condition to the effectiveness of the Alternate Credit Facility, that the issuer of the Alternate Credit Facility will provide funds, on the substitution date, for the purchase of all Bank Certificates at par plus accrued interest (at the Bank Rate) through and including the day immediately preceding the substitution date to the extent not paid by the Applicant or any other Person. On such substitution date, any and all amounts due to the Bank under any Related Document shall be payable in full to the Bank.

(c) The Applicant shall not permit an Alternate Credit Facility to become effective with respect to less than all of the Certificates of Participation without the prior written consent of the Bank.

Section 5.17 Return of Letter of Credit. The Applicant shall, upon the occurrence of the Termination Date, cause the Trustee to surrender forthwith the Letter of Credit to the Bank for cancellation.

Section 5.18 Insurance Policy. The Applicant shall take no action with respect to the Insurer or the Insurance Policy that contradicts or violates the terms of the Cancellation Agreement.

Section 5.19 Maintenance of Tax Exempt Status of the Certificates of Participation. The Applicant shall not take any action or omit to take any action which, if taken or omitted, would adversely affect the exclusion of interest on the Certificates of Participation from gross income for purposes of federal income taxation or the exemption of such interest from State income taxes.

Section 5.20 Reoffering Circular. The Applicant shall not include, or permit to be included, in an offering, reoffering, remarketing or resale document for the Certificates of Participation any information concerning the Bank that is not supplied in writing, or otherwise consented to, by the Bank expressly for inclusion therein. The Applicant shall not make any changes in reference to the Bank, the Letter of Credit or this Agreement in any revision of or supplement to the Reoffering Circular without the Bank's prior written consent thereto.

Section 5.21 Waiver of Immunity. To the fullest extent permitted by law, the Applicant agrees not to assert the defense of sovereign immunity, if available, in any proceeding to enforce any of the obligations of the Applicant under any Related Document in any federal or state court of competent jurisdiction.

Section 5.22 Additional Terms. In the event the Applicant shall enter into any Bank Agreement which Bank Agreement provides the Bank Agreement Provider with (a) covenants not included in this Agreement, (b) covenants which are included in this Agreement but which are significantly more favorable to the Bank Agreement Provider, (c) events of default not included in this Agreement (other than additional events of default the remedy for which is in an immediate termination or suspension of the obligations of the Bank Agreement Provider), (d) events of default which are included in this Agreement but which are more favorable to the Bank Agreement Provider (e.g., shorter cure periods) and/or (e) collateral in addition to a pledge of Gross Revenues (collectively, the "Additional Rights") than are provided to the Bank in this Agreement, then such Additional Rights shall automatically be incorporated into this Agreement and the Bank shall have the benefit of such Additional Rights as soon as such Bank Agreement becomes effective. Promptly following the Applicant's execution and delivery of a Bank Agreement containing Additional Rights, the Applicant shall give the Bank written notice thereof and the Applicant shall enter into an amendment to this Agreement to include such Additional Rights, *provided* that the Bank shall maintain the benefit of such Additional Rights even if the Applicant fails to provide such amendment. If the Applicant shall amend the Bank Agreement such that it no longer provides for such Additional Rights or if the Bank Agreement terminates, then, without the consent of the Bank, this Agreement shall automatically no longer contain the Additional Rights and the Bank shall no longer have the benefits of any of the Additional Rights. In the event that the Applicant shall enter into any Bank Agreement after the Insurance Policy Cancellation Date which provides that the Applicant shall repay the obligations thereunder that are secured by Gross Revenues over a period of time that is shorter (such shorter amortization period, the "Shorter Amortization Period") than the three-year Liquidity Advance amortization period provided in Section 2.3(a) (the "Existing Amortization Period"), this Agreement shall automatically be deemed amended so that the Existing Amortization Period shall become the Shorter Amortization Period. Promptly following the Applicant's execution and delivery of a Bank Agreement containing a Shorter Amortization Period, the Applicant shall

give the Bank written notice thereof and the Applicant shall enter into an amendment to this Agreement to include such Shorter Amortization Period, *provided* that the Bank shall maintain the benefit of such Shorter Amortization Period even if the Applicant fails to provide such amendment. If the Applicant shall amend the Bank Agreement such that it no longer provides for such Shorter Amortization Period or if the Bank Agreement terminates, then, without the consent of the Bank, this Agreement shall automatically be amended so that the Shorter Amortization Period reverts to the Existing Amortization Period in effect immediately prior to the entry into such Bank Agreement. Notwithstanding the foregoing, prior to the Insurance Policy Cancellation Date, this Section 5.22 shall not apply to any provision of any Bank Agreement under which, directly or indirectly, any Person or Persons undertakes to make loans or extend credit or liquidity to the Applicant payable from Gross Revenues relating to (A) facility fee rates, (B) interest rates with respect to advances, loans or drawings under any Bank Agreement or (C) any other fees and charges payable by the Applicant under any Bank Agreement.

Section 5.23 Further Assurances. The Applicant shall execute, acknowledge where appropriate, and deliver, and cause to be executed, acknowledged where appropriate, and delivered, from time to time promptly at the request of the Bank, all such instruments and documents as in the opinion of the Bank are necessary or advisable to carry out the intent and purpose of this Agreement and the other Bank Documents.

Section 5.24 Incorporation of Covenants by Reference. The Applicant hereby makes to the Bank the same covenants as are set forth by it in each Applicant Related Document (other than this Agreement), which covenants, as well as the related defined terms contained therein, are hereby incorporated herein by reference for the benefit of the Bank, *mutatis mutandis*, with the same effect as if each and every such covenant and defined term were set forth herein in its entirety and were made as of the date hereof. No amendment to such covenants or defined terms made pursuant to any Applicant Related Document shall be effective to amend such representations and warranties and defined terms as incorporated by reference herein without the prior written consent of the Bank.

## ARTICLE 6 EVENTS OF DEFAULT; INSURER DEFAULTS; REMEDIES

Section 6.1 Events of Default and Remedies. If any of the following events shall occur, each such event shall be an "Event of Default":

(a) (i) any representation or warranty made by the Applicant in this Agreement (or incorporated herein by reference) or in any of the other Related Documents or in any certificate, document, instrument, opinion or financial or other statement contemplated by or made or delivered pursuant to or in connection with this Agreement or with any of the other Related Documents that is not qualified by "material," "materiality," "Material Adverse Effect" or similar qualifier, shall prove to have been incorrect, incomplete or misleading in any material respect; or (ii) any representation or warranty made by the Applicant in this Agreement (or incorporated herein by reference) or in any of the other Related Documents or in any certificate, document, instrument, opinion or financial or other statement contemplated by or made or delivered pursuant to or in connection with this Agreement or with any of the other Related Documents that is qualified by "material," "materiality," "Material Adverse Effect" or similar qualifier, shall prove to have been incorrect, incomplete or misleading in any respect; or

(b) any "event of default" shall have occurred under any of the Related Documents (as defined respectively therein) other than this Agreement; or

(c) failure to pay to the Bank any Obligations when and as due hereunder; or

(d) default in the due observance or performance by the Applicant of any covenant set forth in Section 5.1, 5.5(d), 5.7, 5.9, 5.10, 5.11, 5.12(b), 5.13, 5.14, 5.15, 5.16(b) or 5.16(c) hereof; or

(e) default in the due observance or performance by the Applicant of any other covenant set forth in this Agreement and the continuance of such default for 30 days after the occurrence thereof; or

(f) any material provision of this Agreement or any of the other Related Documents shall cease to be valid and binding, or the Applicant or a senior officer of the the Applicant shall contest any such provision, or the Applicant or a senior officer of the the Applicant or any agent or trustee on behalf of the Applicant shall deny that it has any or further liability under this Agreement or any of the other Related Documents; or

(g) the Applicant shall (i) have entered involuntarily against it an order for relief under the United States Bankruptcy Code, as amended, (ii) not pay, or admit in writing its inability to pay, its debts generally as they become due, (iii) make an assignment for the benefit of creditors, (iv) apply for, seek, consent to, or acquiesce in, the appointment of a receiver, custodian, trustee, examiner, liquidator or similar official for it or any substantial part of its Property, (v) institute any proceeding seeking to have entered against it an order for relief under the United States Bankruptcy Code, as amended, to adjudicate it insolvent, or seeking dissolution, winding up, liquidation, reorganization, arrangement, marshalling of assets, adjustment or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors or fail to file an answer or other pleading denying the material allegations of any such proceeding filed against it, (vi) take any action in furtherance of any matter described in parts (i) through (v) above, or (vii) fail to contest in good faith any appointment or proceeding described in Section 6.1(h) hereof; or

(h) a custodian, receiver, trustee, examiner, liquidator or similar official shall be appointed for the Applicant or any substantial part of its Property, or a proceeding described in Section 6.1(g) (v) shall be instituted against the Applicant and such appointment continues undischarged or any such proceeding continues undismissed or unstayed for a period of 60 or more days; or

(i) dissolution or termination of the existence of the Applicant; or

(j) a default shall occur under any evidence of Indebtedness issued, assumed, or guaranteed by the Applicant or under any indenture, agreement or other instrument under which the same may be issued, and such default shall continue for a period of time sufficient to permit the acceleration of the maturity of any such Indebtedness (whether or not such maturity is in fact accelerated) or any such Indebtedness shall not be paid when and as due (whether by lapse of time, acceleration or otherwise); or

(k) any judgment or judgments, writ or writs or warrant or warrants of attachment, or any similar process or processes in an aggregate amount in excess of \$5,000,000 shall be entered or filed against the Applicant or against any of its Property that is payable from Gross Revenues and remain undismissed, unvacated, unbonded or unstayed for a period of 30 days; or

(l) there shall be appointed or designated with respect to the Applicant an entity such as an organization, board, commission, authority, agency or body to monitor or declare a financial emergency or similar state of financial distress with respect to the Applicant, or there shall be declared by the Applicant or by any legislative or regulatory body with competent jurisdiction over the Applicant, the existence of a state of financial emergency or similar state of financial distress in respect of the Applicant; or

(m) the Trustee shall cease to have an effective security interest to the extent and priority created or purported to be created by the Trust Agreement; or

(n) a Tax Event shall have occurred.

Section 6.2 Insurer Defaults. If any of the following events shall occur, each such event shall be an "Insurer Default":

(a) any principal of or interest with respect to any Certificate of Participation (including Bank Certificates) is not paid by the Applicant when due and such principal or interest is not paid by the Insurer when, as and in the amounts required to be paid pursuant to the terms of the Insurance Policy; or

(b) the Insurer shall fail to make any payment related to principal and interest when due under any insurance policy (other than the Insurance Policy) or surety bond issued by it insuring or supporting the payment of municipal obligations rated by any Rating Agency, and such failure shall continue for a period of thirty (30) days (it being understood by the Bank that default for purposes of this clause (b) shall not mean a situation whereby the Insurer contests in good faith its liability under any such policy or policies in light of the claims made thereunder); or

(c) a proceeding is instituted in a court having jurisdiction in the premises seeking an order for relief, rehabilitation, reorganization, conservation, liquidation or dissolution in respect of the Insurer or for any substantial part of its property under any applicable bankruptcy, insolvency or other similar law now or hereafter in effect, or for the appointment of a receiver, liquidator, assignee, custodian, trustee or sequestrator (or other similar official) and such proceeding shall not have been dismissed within 60 days or such court enters an order granting the relief sought in such proceeding; or the New York Department of Insurance shall declare a moratorium on the payment of the Insurer's debts, or the Insurer shall commence a voluntary case under any applicable bankruptcy, insolvency or other similar law now or hereafter in effect, shall consent to the entry of an order for relief in an involuntary case under any such law or shall consent to the appointment of or taking possession by a receiver, liquidator, assignee, trustee, custodian or sequestrator (or other similar official) of the Insurer or for any substantial part of its property, or shall make a general assignment for the benefit of creditors, or shall fail generally to pay its debts (provided for purposes of this definition, "debts" shall not include any obligation of

the Insurer under any insurance policy or surety bond) as they become due, or an order for rehabilitation, liquidation or dissolution of the Insurer shall be issued; or

(d) (i) any material provision of the Insurance Policy relating to the obligation of the Insurer to make payments of principal and interest thereunder at any time for any reason ceases to be valid and binding on the Insurer in accordance with the terms of the Insurance Policy or the New York Department of Insurance, or a court or other Governmental Authority of appropriate jurisdiction shall find or rule or shall enter an order, judgment or decree that the Insurance Policy is not valid and binding on the Insurer or (ii) the Insurer shall (A) claim in writing that the Insurance Policy is not valid and binding on the Insurer, (B) repudiate the Insurer's obligations under the Insurance Policy or (C) initiate legal proceedings seeking an adjudication that the Insurance Policy, or any material provision thereof regarding the payment of principal or interest on Certificates of Participation (including Bank Certificates) is not valid and binding on the Insurer.

Section 6.3 Remedies Prior to the Insurance Policy Cancellation Date. If an Event of Default or a Mandatory Tender Event shall have occurred and be continuing prior to the Insurance Policy Cancellation Date, the Bank may exercise any one or more of the following rights and remedies in addition to any other remedies herein or by law provided:

(a) give written notice of the occurrence of such Event of Default or a Mandatory Tender Event, as the case may be, to the Trustee and direct the Trustee to cause a mandatory tender of the Certificates of Participation pursuant to Section 3.02 of the Trust Agreement and clause (vi) of the definition of "Mandatory Purchase Date" contained therein, thereby causing the Letter of Credit to terminate ten (10) days thereafter in accordance with its terms, in which case the Bank shall, in accordance with the provisions of Section 10.04 of the Trust Agreement, direct that the Insurance Policy be terminated and the Issuer, the Applicant, the Trustee and the Bank shall take such action as shall be necessary to effect such termination in accordance with the terms of the Cancellation Agreement; *provided, however*, that if an Insurer Default shall have occurred and be continuing, the Bank may give notice of an Event of Default or a Mandatory Tender Event to the Trustee and direct the Trustee to cause a mandatory tender of the Certificates of Participation without directing the Issuer, the Applicant and the Trustee to take such action as shall be necessary to effect a termination of the Insurance Policy in accordance with the terms of the Cancellation Agreement;

(b) pursue any rights and remedies it may have under the Related Documents subject to the terms thereof, including, instituting suit, actions or proceedings to enforce its rights under the Trust Agreement; or

(c) pursue any other action available at law or in equity either for specific performance of any covenant or agreement contained herein or in aid of execution of any power herein granted or for the enforcement of any proper legal remedy;

*provided, however*, that in the case of the foregoing clauses (b) and (c), the Bank shall not exercise any such rights and remedies or pursue such other actions, including directions or remedies under the Trust Agreement, without the consent of the Insurer unless the following conditions precedent are met: (i) the Insurance Policy is no longer in effect and (ii) to the extent that no Insurer Default shall have occurred and is then continuing, the Insurer has been paid all

amounts due and payable to it (it being understood that (x) in all events, including where an Insurer Event of Default shall have occurred and be continuing, the Insurer's rights derived through subrogation or assignment shall continue in full force and effect and (y) in the event that an Insurer Default has occurred and is then continuing, payment of all amounts due and payable to the Insurer shall not be a condition precedent to the exercise by the Bank, without the consent of the Insurer, of any such rights and remedies and pursuit of such other actions, including direction of remedies under the Related Documents); *provided further, however*, notwithstanding the condition set forth in clause (i) of the foregoing proviso, if a Control Event (as defined in the Trust Agreement) shall have occurred and be continuing, the Bank may, while the Insurance Policy is in effect, exercise any such rights and remedies and pursue such other actions, including directions or remedies under the Trust Agreement, without the consent of the Insurer, if the Bank has directed the Trustee to cause a mandatory tender of all of the Certificates of Participation pursuant to Section 6.3(a) or 6.4(a) hereof (a "Tender Direction"), in which case the Bank shall, and hereby covenants with the Insurer that it will, and will use its best efforts to cause the appropriate parties to, satisfy at the earliest time practicable all applicable conditions to the effectiveness of cancellation of the Insurance Policy pursuant to the Cancellation Agreement and the Trust Agreement and, during the period between the date of delivery of such Tender Direction and the effective date of cancellation of the Insurance Policy, the Bank will direct the Trustee not to draw on the Insurance Policy. Notwithstanding anything to the contrary herein, the Insurer's right to enforce the Bank's covenants set forth in this Section shall survive any termination of other rights of the Insurer.

#### Section 6.4 Other Rights to Direct Mandatory Tender.

(a) If an Insurer Default or an Insurer Downgrade Event shall have occurred, the Bank may give written notice to the Trustee of the occurrence of such Insurer Default or Insurer Downgrade Event, as applicable, and direct, in accordance with Section 10.04 of the Trust Agreement, that the Insurance Policy be terminated within fifteen (15) days of such direction, whereupon, in accordance with Section 3.02 of the Trust Agreement and clause (viii) of the definition of "Mandatory Purchase Date" contained therein, the Certificates of Participation shall be subject to mandatory tender. Upon any such direction, the Issuer, the Applicant, the Trustee and the Bank shall take such action as shall be necessary to effect such termination pursuant to the terms of the Cancellation Agreement.

(b) If (i) the Applicant fails to pay any Facility Fee (as defined in the Fee Letter) or (ii) an Insurer Default or an Insurer Downgrade Event shall have occurred and be continuing, in each case, during the occurrence and continuation of an Event of Default, the Bank may give written notice to the Trustee of the occurrence of (x) such failure to pay such Facility Fee or (y) such Insurer Default or Insurer Downgrade Event, as applicable, together with such Event of Default, and direct the Trustee to cause a mandatory tender of the Certificates of Participation in accordance with Section 3.02 of the Trust Agreement and clause (vi) of the definition of "Mandatory Purchase Date" contained therein, thereby causing the Letter of Credit to terminate fifteen (15) days thereafter.

Section 6.5 Remedies On and After the Insurance Policy Cancellation Date. If the Insurance Policy Cancellation Date has occurred, upon the occurrence and continuance of an Event of Default or a Mandatory Tender Event, the Bank may exercise any one or more of the following rights and remedies:

(a) by notice to the Applicant, declare all Obligations to be, and such amounts shall thereupon become, immediately due and payable without presentment, demand, protest or other notice of any kind, all of which are hereby waived by the Applicant, provided that upon the occurrence of an Event of Default under Section 6.1(g) or (h) hereof such acceleration shall automatically occur (unless such automatic acceleration is waived by the Bank in writing);

(b) give notice of the occurrence of an Event of Default to the Trustee, directing the Trustee to cause a mandatory purchase the Certificates of Participation, thereby causing the Letter of Credit to expire ten (10) days thereafter;

(c) pursue any rights and remedies it may have under the Related Documents;  
or

(d) pursue any other action available at law or in equity.

## ARTICLE 7 MISCELLANEOUS

### Section 7.1 No Deductions; Increased Costs.

(a) All payments made by the Applicant to the Bank under the Bank Documents shall be made without setoff, counter-claim or other defense and will be made free and clear of, and without deduction or withholding for, any present or future taxes, levies, imposts, duties, fees, assessments or other charges of whatever nature now or hereafter imposed by any jurisdiction or by any political subdivision or taxing authority thereof or therein (but excluding, except as provided below, any tax imposed on or measured by the overall net income of the Bank pursuant to the laws of the jurisdiction (or any political subdivision or taxing authority thereof or therein) under which the Bank is organized) and all interest, penalties or similar liabilities with respect thereto (collectively, "Taxes"). If the Applicant shall be required by any law, rule or regulation to deduct any Taxes from or in respect of any sum payable under any Bank Document to the Bank, (i) the sum payable shall be increased as necessary so that after making all required deductions (including deductions applicable to additional sums payable under this Section), the Bank receives an amount equal to the sum it would have received had no such deductions been made, (ii) the Applicant shall make such deductions, (iii) the Applicant shall pay the full amount deducted to the relevant taxation authority or other authority in accordance with applicable laws, rules and regulations and (iv) within 45 days after the date of such payment, the Applicant shall furnish to the Bank the original or a certified copy of a receipt evidencing payment thereof. In addition, the Applicant agrees to pay any present or future stamp, recording or documentary taxes and any other excise or property taxes, charges or similar levies that arise from the execution or delivery or otherwise with respect to the Bank Documents (hereinafter referred to as "Other Taxes"). The Bank shall provide to the Applicant within a reasonable time a copy of any written notification it receives with respect to Other Taxes owing by the Applicant to the Bank hereunder *provided* that the Bank's failure to send such notice shall not relieve the Applicant of its obligation to pay such amounts hereunder. The Applicant will to the maximum extent permitted by applicable law indemnify and hold harmless the Bank, and reimburse the Bank upon its written request, for the amount of any Taxes or Other Taxes so levied or imposed and paid by the Bank.

(b) If a Change of Law shall:

(i) limit the deductibility of interest with respect to funds obtained by the Bank to pay any of its liabilities or subject the Bank to any tax, duty, charge, deduction or withholding on or with respect to payments relating to the Certificates of Participation, the Bank Documents, or any amount paid or to be paid by the Bank as the issuer of the Letter of Credit (other than any tax measured by or based upon the overall net income of the Bank imposed by any jurisdiction having control over the Bank);

(ii) impose, modify, require, make or deem applicable to the Bank any reserve requirement, capital requirement, special deposit requirement, insurance assessment or similar requirement against any assets held by, deposits with or for the account of, or loans, letters of credit or commitments by, an office of the Bank;

(iii) change the basis of taxation of payments due the Bank under the Bank Documents or the Certificates of Participation (other than by a change in taxation of the overall net income of the Bank);

(iv) cause or deem letters of credit to be assets held by the Bank and/or as deposits on its books; or

(v) impose upon the Bank any other condition with respect to any amount paid or payable to or by the Bank or with respect to any Related Documents;

and the result of any of the foregoing is to increase the cost to the Bank of making any payment or maintaining the Letter of Credit or making any Liquidity Advance, or to reduce the amount of any payment (whether of principal, interest or otherwise) receivable by the Bank, or to reduce the rate of return on the capital of the Bank or to require the Bank to make any payment on or calculated by reference to the gross amount of any sum received by it, in each case by an amount which the Bank in its reasonable judgment deems material, then:

(1) the Bank shall promptly notify the Applicant in writing of such event;

(2) the Bank shall promptly deliver to the Applicant a certificate stating the change which has occurred or the reserve requirements or other costs or conditions which have been imposed on the Bank or the request, direction or requirement with which it has complied, together with the date thereof, the amount of such increased cost, reduction or payment and a reasonably detailed description of the way in which such amount has been calculated, and the Bank's determination of such amounts, absent fraud or manifest error, shall be conclusive; and

(3) the Applicant shall pay to the Bank, from time to time as specified by the Bank, within two Business Days of any demand, such an amount or amounts as will compensate the Bank for such additional cost, reduction or payment.

The protection of this Section 7.1(b) shall be available to the Bank regardless of any possible contention of invalidity or inapplicability of the law, regulation or condition which has been imposed; *provided, however*, that if it shall be later determined by the Bank that any amount so

paid by the Applicant pursuant to this Section 7.1(b) is in excess of the amount payable under the provisions hereof, the Bank shall refund such excess amount to the Applicant.

**Section 7.2 Right of Setoff; Other Collateral.**

(a) Upon the occurrence and during the continuance of an Event of Default, the Bank is hereby authorized at any time and from time to time without notice to the Applicant (any such notice being expressly waived by the Applicant) but subject to the consent right, if any, of the Insurer set forth in Section 6.3(a), and to the fullest extent permitted by law, to setoff, to exercise any banker's lien or any right of attachment and apply any and all balances, credits, deposits (general or special, time or demand, provisional or final), accounts or monies at any time held and other indebtedness at any time owing by the Bank to or for the account of the Applicant (irrespective of the currency in which such accounts, monies or indebtedness may be denominated and the Bank is authorized to convert such accounts, monies and indebtedness into United States dollars) against any and all of the Obligations of the Applicant, whether or not the Bank shall have made any demand for any amount owing to the Bank by the Applicant.

(b) The rights of the Bank under this Section 7.2 are in addition to, in augmentation of, and, except as specifically provided in this Section 7.2, do not derogate from or impair, other rights and remedies (including, without limitation, other rights of setoff) which the Bank may have. The Bank agrees to use commercially reasonable efforts to notify the Applicant in writing after any such setoff and application referred to in subsection (a) above, provided that failure to give such notice shall not affect the validity of such setoff and application or subject the Bank to any liability to the Applicant.

**Section 7.3 Indemnity.** To the maximum extent permitted by law, the Applicant shall indemnify and hold harmless the Bank, its parent and each of their respective directors, officers, employees and agents (each, including the Bank, an "Indemnified Person") from and against any and all claims, suits, judgments, costs, losses, fines, penalties, damages, liabilities, and expenses, including expert witness fees and legal fees, charges and disbursements of any counsel (including in-house counsel fees and allocated costs) for any Indemnified Person ("Costs"), arising out of, in connection with, or as a result of: (i) the Letter of Credit or any pre-advice of its issuance; (ii) any transfer, sale, delivery, surrender, or endorsement of the Letter of Credit at any time(s) held by any Indemnified Person in connection with the Letter of Credit; (iii) any action or proceeding arising out of or in connection with any Related Document (whether administrative, judicial or in connection with arbitration), including any action or proceeding to compel or restrain any presentation or payment under the Letter of Credit, or for the wrongful dishonor of or honoring a presentation under the Letter of Credit; (iv) any independent undertakings issued by the beneficiary of the Letter of Credit; (v) any unauthorized communication or instruction (whether oral, telephonic, written, telegraphic, facsimile or electronic) (each an "Instruction") regarding the Letter of Credit or error in computer transmission; (vi) an adviser, confirmer or other nominated person seeking to be reimbursed, indemnified or compensated; (vii) any third party seeking to enforce the rights of an applicant, beneficiary, nominated person, transferee, assignee of proceeds of the Letter of Credit; (viii) the fraud, forgery or illegal action of parties other than the Indemnified Person; (ix) the enforcement of any Bank Document or any rights or remedies under or in connection with any Related Document; (x) the acts or omissions, whether rightful or wrongful, of any present or future de jure or de facto governmental or regulatory authority or cause or event beyond the control of such Indemnified Person; in each case, including that resulting from Bank's own negligence,

*provided, however*, that such indemnity shall not be available to any Person claiming indemnification under (i) through (x) above to the extent that such Costs are found in a final, non-appealable judgment by a court of competent jurisdiction to have resulted directly from the gross negligence or willful misconduct of the Indemnified Person claiming indemnity. If and to the extent that the obligations of Applicant under this paragraph are unenforceable for any reason, Applicant shall make the maximum contribution to the Costs permissible under applicable law.

Section 7.4 Obligations Absolute. The obligations of the Applicant under this Agreement shall be absolute, unconditional and irrevocable, and shall be paid strictly in accordance with the terms of this Agreement under all circumstances whatsoever, including, without limitation: (i) any lack of validity, enforceability or legal effect of this Agreement or any Related Document, or any term or provision herein or therein; (ii) payment against presentation of any draft, demand or claim for payment under the Letter of Credit that does not comply in whole or in part with the terms of the Letter of Credit or which proves to be fraudulent, forged or invalid in any respect or any statement therein being untrue or inaccurate in any respect, or which is signed, issued or presented by a Person (or a transferee of such Person) purporting to be a successor or transferee of the beneficiary of the Letter of Credit; (iii) the Bank or any of its branches or affiliates being the beneficiary of the Letter of Credit; (iv) the Bank honoring a drawing against any draft, demand or claim for payment up to the amount available under the Letter of Credit even if such any draft, demand or claim for payment is in an amount in excess of the amount available under the Letter of Credit; (v) the existence of any claim, set-off, defense or other right that the Applicant or any other Person may have at any time against any beneficiary, any assignee of proceeds, the Bank or any other Person; (vi) the Bank having previously paid against fraudulently signed or presented draft, demand or claim for payment (whether or not the Applicant shall have reimbursed the Bank for such drawing); and (vii) any other event, circumstance or conduct whatsoever, whether or not similar to any of the foregoing, that might, but for this paragraph, constitute a legal or equitable defense to or discharge of, or provide a right of set-off against, the Applicant's obligations hereunder (whether against the Bank, the beneficiary or any other Person); *provided, however*, that subject to Section 7.5 hereof, the foregoing shall not exculpate the Bank from such liability to the Applicant as may, be finally, judicially determined in an independent action or proceeding brought by the Applicant against the Bank following payment of the Applicant's obligations under this Agreement.

Section 7.5 Liability of the Bank.

(a) The liability of the Bank (or any other Indemnified Person) under, in connection with and/or arising out of any Related Document, regardless of the form or legal grounds of the action or proceeding, shall be limited to any direct compensatory damages, as opposed to consequential damages, suffered by the Applicant that are caused directly by Bank's gross negligence or willful misconduct in (i) honoring a presentation under the Letter of Credit that does not at least substantially comply with the Letter of Credit, or (ii) failing to honor a presentation under the Letter of Credit that strictly complies with the Letter of Credit. In no event shall the Bank be deemed to have failed to act with due diligence or reasonable care if the Bank's conduct is in accordance with Standard Letter of Credit Practice or in accordance with this Agreement. The Applicant's aggregate remedies against the Bank and any Indemnified Person for wrongfully honoring or wrongfully failing to honor a presentation under the Letter of Credit shall in no event exceed the aggregate amount facility fees (set forth in the Fee Letter) received by the Bank. Notwithstanding anything to the contrary herein, the Bank and the other

Indemnified Persons shall not, under any circumstances whatsoever, be liable for any punitive, consequential, indirect or special damages or losses regardless of whether the Bank or any Indemnified Person shall have been advised of the possibility thereof or of the form of action in which such damages or losses may be claimed. The Applicant shall take action to avoid and mitigate the amount of any damages claimed against the Bank or any Indemnified Person. Any claim by the Applicant for damages under or in connection with this Agreement or the Letter of Credit shall be reduced by an amount equal to the sum of (i) the amount saved by the Applicant as a result of the breach or alleged wrongful conduct and (ii) the amount of the loss that would have been avoided had the Applicant mitigated damages.

(b) The Bank shall not be liable for any Costs resulting from any act or omission by the Bank in accord with the ISP.

(c) Without limiting any other provision of this Agreement, the Bank and each other Indemnified Person (if applicable), shall not be responsible to the Applicant for, and the Bank's rights and remedies against the Applicant and the Applicant's obligation to reimburse the Bank shall not be impaired by: (i) honor of a presentation under the Letter of Credit which on its face substantially complies with the terms of the Letter of Credit; (ii) honor of a presentation of any any draft, demand or claim for payment which appears on its face to have been signed, presented or issued (A) by any purported successor or transferee of any beneficiary or other party required to sign, present or issue any draft, demand or claim for payment under the Letter of Credit or (B) under a new name of the beneficiary; (iii) acceptance as a draft of any written or electronic demand or request for payment under the Letter of Credit, even if nonnegotiable or not in the form of a draft, and may disregard any requirement that such draft, demand or request bear any or adequate reference to the Letter of Credit; (iv) the identity or authority of any presenter or signer of any any draft, demand or claim for payment or the form, accuracy, genuineness, or legal effect of any presentation under the Letter of Credit (v) disregard of any non-documentary conditions stated in the Letter of Credit; (vi) acting upon any Instruction which it, in Good Faith, believes to have been given by a Person or entity authorized to give such Instruction; (vii) any errors, omissions, interruptions or delays in transmission or delivery of any message, advice or document (regardless of how sent or transmitted) or for errors in interpretation of technical terms or in translation; (viii) any delay in giving or failing to give any notice; (ix) any acts, omissions or fraud by, or the solvency of, any beneficiary, any nominated Person or any other Person; (x) any breach of contract between the beneficiary and the Applicant or any of the parties to the underlying transaction; (xi) assertion or waiver of any provision of the ISP which primarily benefits an issuer of a letter of credit, including, any requirement that any any draft, demand or claim for payment be presented to it at a particular hour or place; and (xii) acting or failing to act as required or permitted under Standard Letter of Credit Practice. For purposes of this Section 7.5(c), "Good Faith" means honesty in fact in the conduct of the transaction concerned.

Section 7.6 Participants. The Bank shall have the right to grant participations in the Bank Documents to one or more other Persons, and such participants shall be entitled to the benefits of this Agreement, including, without limitation, Sections 7.1, 7.3 and 7.14 hereof, to the same extent as if they were a direct party hereto; *provided, however*, that no such participation by any such participant shall in any way affect the obligation of the Bank under the Letter of Credit; and provided further that no such participant shall be entitled to receive payment hereunder of any amount greater than the amount which would have been payable had the Bank not granted a participation to such participant. The Applicant agrees that the Bank may disclose any

information received by the Bank in connection herewith including, without limitation, the financial information described in Section 5.5 hereof, to any participant.

Section 7.7 Survival of this Agreement. All covenants, agreements, representations and warranties made in this Agreement shall survive the issuance by the Bank of the Letter of Credit and shall continue in full force and effect so long as the Letter of Credit shall be unexpired or any Obligations shall be outstanding and unpaid. The obligation of the Applicant to reimburse the Bank pursuant to Sections 7.1, 7.3 and 7.14 hereof shall survive the payment of the Certificates of Participation and termination of this Agreement.

Section 7.8 Modification of this Agreement. No amendment, modification or waiver of any provision of this Agreement or the Fee Letter shall be effective unless the same shall be in writing and signed by the Bank and the Applicant and no amendment, modification or waiver of any provision of the Letter of Credit, and no consent to any departure by the Applicant therefrom, shall in any event be effective unless the same shall be in writing and signed by the Bank. Any such waiver or consent shall be effective only in the specific instance and for the purpose for which given. No notice to or demand on the Applicant in any case shall entitle the Applicant to any other or further notice or demand in the same, similar or other circumstances. Notwithstanding anything to the contrary contained in this Section 7.8, as long as the Insurance Policy remains in effect, no amendment, modification or waiver of any provision of this Agreement shall be effective unless consented to in writing by the Insurer; *provided, however*, that if an Insurer Event of Default shall have occurred and be continuing, then the Bank and the Applicant may amend or modify this Agreement or waive any provision hereof without the consent of the Insurer unless such amendment, modification or waiver would be adverse to the Insurer or would change its obligations in connection with any Bank Certificates; *provided, further*, that no consent of the Insurer shall ever be required in connection with the extension of the Stated Expiration Date or any amendment to the Fee Letter. As long as the Insurance Policy remains in effect, the Bank shall provide the Insurer with a copy of all amendments and modifications to this Agreement.

Section 7.9 Waiver of Rights by the Bank. No course of dealing or failure or delay on the part of the Bank in exercising any right, power or privilege hereunder or under the Letter of Credit or this Agreement shall operate as a waiver thereof, nor shall a single or partial exercise thereof preclude any other or further exercise or the exercise of any other right or privilege. The rights of the Bank under the Letter of Credit and the rights of the Bank under this Agreement are cumulative and not exclusive of any rights or remedies that the Bank would otherwise have.

Section 7.10 Severability. In case any one or more of the provisions contained in this Agreement should be invalid, illegal or unenforceable in any respect, the validity, legality and enforceability of the remaining provisions contained herein shall not in any way be affected or impaired thereby. The parties shall endeavor in good faith negotiations to replace the invalid, illegal or unenforceable provisions with valid provisions the economic effect of which comes as close as possible to that of the invalid, illegal or unenforceable provisions.

Section 7.11 Governing Law. PURSUANT TO SECTION 5-1401 OF THE NEW YORK GENERAL OBLIGATIONS LAW (OR ANY SUCCESSOR STATUTE THERETO), THIS AGREEMENT AND THE FEE LETTER SHALL BE DEEMED TO BE A CONTRACT UNDER, AND SHALL BE GOVERNED BY, AND CONSTRUED AND INTERPRETED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF NEW YORK WITHOUT REGARD

TO CHOICE OF LAW RULES; PROVIDED, HOWEVER, THAT THE LAWS OF THE STATE OF CALIFORNIA SHALL GOVERN THE INTERPRETATION OF THIS AGREEMENT AND THE FEE LETTER AS IT RELATES TO THE CAPACITY, POWER AND AUTHORITY OF THE APPLICANT TO ENTER INTO AND PERFORM ITS OBLIGATIONS UNDER THIS AGREEMENT.

Section 7.12 Notices. All notices hereunder shall be given by United States certified or registered mail or by telecommunication device capable of creating written record of such notice and its receipt. Notices hereunder shall be effective when received and shall be addressed:

If to the Bank, to: JPMorgan Chase Bank, N.A.  
Public Finance - Credit Origination  
383 Madison Avenue  
Mail Code: NY1-M076  
New York, NY, 10179  
Telephone No.: (212) 270-2198  
Telecopy No.: (917) 456-3538  
Attention: James G. Millard

With a copy to the Bank,  
Standby Letter of Credit Unit:

JPMorgan Chase Bank, N.A.  
131 South Dearborn, 5th Floor  
Mail Code IL1-0236  
Chicago, IL 60603-5506  
Facsimile No.: (312) 954-6163  
Telephone No.: (800) 634-1969, Option 1  
Attention: Standby Service Unit

If to the Applicant, to: City of Modesto  
1010 Tenth Street, Suite 5200  
Modesto, CA 95353  
Facsimile No.: (209) 571-5880  
Telephone No.: (209) 577-5371  
Attention: Finance Director

If to the Trustee, to: The Bank of New York Mellon Trust Company, N.A.  
100 Pine Street, Suite 3100  
San Francisco, CA 94111  
Facsimile No.: (415) 399-1647  
Telephone No.: (415) 263-2432  
Attention: Corporate Trust

Section 7.13 Successors and Assigns. Whenever in this Agreement the Bank is referred to, such reference shall be deemed to include the successors and assigns of the Bank and all covenants, promises and agreements by or on behalf of the Applicant which are contained in this Agreement shall inure to the benefit of such successors and assigns. The rights and duties of the Applicant hereunder, however, may not be assigned or transferred, except as specifically

provided in this Agreement or with the prior written consent of the Bank, and all obligations of the Applicant hereunder shall continue in full force and effect notwithstanding any assignment by the Applicant of any of its rights or obligations under any of the Related Documents or any entering into, or consent by the Applicant to, any supplement or amendment to any of the Related Documents.

Section 7.14 Expenses. The Applicant shall pay (a) all reasonable out-of-pocket expenses of the Bank, including reasonable fees and expenses of counsel retained by the Bank in connection with any amendment, waiver or consent under any Related Document and (b) if any Event of Default, Insurer Default or Insurer Downgrade Event occurs, all reasonable out-of-pocket expenses incurred by the Bank, including reasonable fees and disbursements of counsel and experts retained by the Bank in connection with such Event of Default, Insurer Default or Insurer Downgrade Event and collection and other enforcement proceedings resulting therefrom.

Section 7.15 Headings. The captions in this Agreement are for convenience of reference only and shall not define or limit the provisions hereof.

Section 7.16 Counterparts. This Agreement may be executed in counterparts, each of which shall constitute an original but all taken together to constitute one instrument.

Section 7.17 Entire Agreement. The Bank Documents constitute the entire understanding of the parties with respect to the subject matter thereof and any prior agreements, whether written or oral, with respect thereto are superseded hereby.

Section 7.18 Government Regulations. Applicant shall ensure that the Certificates of Participation proceeds, the proceeds of any drawing made under the Letter of Credit and the proceeds of any Liquidity Advance shall not be used to violate any of the foreign asset control regulations of Office of Foreign Assets Control or any enabling statute or Executive Order relating thereto. Further, Applicant shall comply with all applicable Bank Secrecy Act laws and regulations, as amended. Applicant agrees to provide documentary and other evidence of Applicant's identity as may be requested by Bank at any time to enable Bank to verify Applicant's identity or to comply with any applicable law or regulation, including, without limitation, Section 326 of the USA Patriot Act of 2001, 31 U.S.C. Section 5318.

Section 7.19 Waiver of Jury Trial. TO THE EXTENT MAXIMUM EXTENT PERMITTED BY LAW, EACH OF THE PARTIES HERETO HEREBY IRREVOCABLY WAIVES ANY AND ALL RIGHT TO TRIAL BY JURY IN ANY LEGAL ACTION OR PROCEEDING ARISING OUT OF OR RELATING TO THE BANK DOCUMENTS OR THE TRANSACTIONS CONTEMPLATED THEREBY AND AGREES THAT ANY SUCH ACTION OR PROCEEDING SHALL BE TRIED BEFORE A COURT AND NOT BEFORE A JURY. EACH OF THE PARTIES HERETO ACKNOWLEDGES THAT THIS WAIVER IS A MATERIAL INDUCEMENT TO ENTER INTO A BUSINESS RELATIONSHIP, THAT EACH HAS RELIED ON THE WAIVER IN ENTERING INTO THIS AGREEMENT AND THE OTHER RELATED DOCUMENTS TO WHICH IT IS A PARTY, AND THAT EACH WILL CONTINUE TO RELY ON THIS WAIVER IN THEIR RELATED FUTURE DEALINGS. EACH OF THE PARTIES HERETO WARRANTS AND REPRESENTS THAT EACH HAS HAD THE OPPORTUNITY OF REVIEWING THIS JURY WAIVER WITH LEGAL COUNSEL, AND THAT EACH KNOWINGLY AND VOLUNTARILY WAIVES ITS JURY TRIAL RIGHTS.

Section 7.20 Assignment to Federal Reserve Bank. The Bank may assign and pledge all or any portion of the Obligations to any Federal Reserve Bank or the United States Treasury as collateral security pursuant to Regulation A of the Board of Governors of the Federal Reserve System and any Operating Circular issued by such Federal Reserve Bank, *provided* that any payment in respect of such assigned Obligations made by the Applicant to the Bank in accordance with the terms of the applicable Bank Document shall satisfy the Applicant's obligations thereunder in respect of such assigned Obligation to the extent of such payment. No such assignment shall release the Bank from its obligations hereunder.

Section 7.21 Insurance Policy Claims. Following payment by the Bank of any drawing under the Letter of Credit, the Bank shall have thirty (30) calendar days from the date of such payment to direct the Insurer to reimburse the Bank for the amount of such drawing that was not reimbursed by the Applicant or by the Trustee from amounts in the funds and accounts under the Trust Agreement. In the event the Bank fails to direct the Insurer to reimburse it within the thirty (30) calendar day period, the Bank shall be deemed to have elected not to receive reimbursement from the Insurer with respect to such payment under the Letter of Credit and waived its right to present such a claim to the Insurer for failure of the Applicant to make such reimbursement. In no event shall the Bank be deemed to have waived its right to direct a mandatory tender of the Certificates of Participation with respect to any such reimbursement default as a result of the Bank waiving its right to present a claim of reimbursement from the Insurer.

Section 7.22 Insurer's Rights.

(a) Anything contained in this Agreement to the contrary notwithstanding, the parties hereto acknowledge and agree that the Insurer shall maintain all rights given to it under the Trust Agreement and hereunder with respect to the giving of consents, approvals and notices and direction of proceedings except as set forth in Section 10.03 of the Trust Agreement with respect to its rights under the Trust Agreement and in Section 6.3 hereof with respect to its rights hereunder.

(b) The Bank, the Trustee, the Issuer and the Applicant acknowledge that the Insurer shall be an express third party beneficiary of the provisions of this Agreement, with the power to enforce the same unless (i) the Insurance Policy is no longer in effect and (ii) the Insurer has been paid all amounts due and payable to it or (ii) an Insurer Default has occurred and is continuing.

(c) No provision of this Section 7.22 shall in any way limit or affect the rights of the Insurer as subrogee of the Bank or any other owner of a Certificate of Participation or as assignee of such Bank or any other owner of a Certificate of Participation or to otherwise be reimbursed and indemnified for its costs and expenses and other payment on or in connection with the Insurance Policy either by operation of law or at equity or by contract.

*[Remainder of page intentionally left blank.]*

IN WITNESS WHEREOF, each party hereto has caused this Agreement to be duly executed and delivered by its respective officer thereunto duly authorized as of the date first written above.

CITY OF MODESTO

By:   
Name: Gloriette G. Beck  
Title: Finance Director/Treasurer

JPMORGAN CHASE BANK, NATIONAL  
ASSOCIATION

By: James G. Millard  
Name: James G. Millard  
Title: Executive Director

EXHIBIT A  
FORM OF LETTER OF CREDIT

Irrevocable Transferable Letter of Credit

July 14, 2011

U.S. \$47,625,989

No. CPCS-923992

The Bank of New York Mellon Company, N.A.,  
as trustee (the "*Trustee*") and Agent under the  
Amended and Restated Trust Agreement,  
Trust Agreement dated as of July 14, 2011  
(the "*Trust Agreement*") between the Modesto  
Public Financing Authority (the "*Authority*")  
and the Trustee

555 Kearny Street, Suite 600  
San Francisco, CA 94108

Attention: Corporate Trust Department

Ladies and Gentlemen:

We hereby establish in your favor as Trustee for the benefit of the holders of the Authority's Water Revenue Refunding Certificates of Participation 2008 Series A (the "*Certificates*"), our irrevocable transferable Letter of Credit No. CPCS-923992 for the account of the City of Modesto (the "*Applicant*"), whereby we hereby irrevocably authorize you to draw on us from time to time, from and after the date hereof to and including the earliest to occur of our close of business on: (i) July 14, 2014 (as extended from time to time, the "*Stated Expiration Date*"), (ii) the earlier of (A) the date which is five (5) days following the Conversion Date (as defined in the Trust Agreement) of all of the Certificates as such date is specified in a certificate in the form of Annex A hereto (the "*Conversion Date*") to a rate of interest other than a Daily Rate (as defined in the Trust Agreement) or the Weekly Rate (as defined in the Trust Agreement) or (B) the date on which the Bank honors a drawing under the Letter of Credit on or after the Conversion Date, (iii) the date which is five (5) days following receipt from you of a certificate in the form set forth as Annex B hereto, and (iv) the date which is ten (10) days following receipt by you of a written notice from us stating that such notice is delivered pursuant to Section 6.3(a) or Section 6.5(b), as the case may be, of the Reimbursement Agreement, dated as of July 1, 2011, between the Applicant and us (such agreement, the "*Reimbursement Agreement*"; such notice, a "*Default Notice*") and specifying the occurrence of an Event of Default or a Rating Event under the Reimbursement Agreement and directing you to cause a mandatory purchase of the Certificates (the "*Termination Date*"), a maximum aggregate amount not exceeding Forty Seven Million Six Hundred Twenty Five Thousand Nine Hundred Eighty Nine United States Dollars (U.S. \$47,625,989) (the "*Original Stated Amount*") to pay principal of and accrued interest with respect to, or the purchase price of, the Certificates in accordance with the terms hereof (said U.S. \$47,625,989 having been calculated to be equal to Forty Six Million Seven Hundred Sixty Five Thousand United States Dollars (U.S. \$46,765,000), the outstanding principal amount of the Certificates, plus Eight Hundred Sixty Thousand Nine Hundred Eighty Nine United States

Dollars (U.S. \$860,989) (the "*Interest Component*"), which is 56 days' accrued interest with respect to said principal amount of the Certificates at the rate of twelve percent (12%) per annum calculated on a 365 days basis (the "*Cap Interest Rate*").

This credit is available to you against presentation of the following documents (the "*Payment Documents*") presented to JPMorgan Chase Bank, N.A. (the "*Bank*") as described below:

A certificate (with all blanks appropriately completed) (i) in the form attached as Annex C hereto to pay accrued interest with respect to the Certificates (an "*Interest Drawing*"), (ii) in the form attached as Annex D hereto to pay the principal amount of and accrued interest with respect to the Certificates in respect of any payment of the principal of the Certificates (including payments of principal at maturity and upon redemption) (a "*Principal Drawing*"), provided that in the event the date of payment coincides with an Interest Payment Date (as defined in the Trust Agreement), the Principal Drawing shall not include any accrued interest with respect to the Certificates (which interest is payable pursuant to an Interest Drawing), or (iii) in the form attached as Annex E hereto to pay the purchase price of Certificates which have not been remarketed or which are not required to be remarketed (a "*Liquidity Drawing*"), provided that in the event the purchase date coincides with an Interest Payment Date, the Liquidity Drawing shall not include any accrued interest with respect to the Certificates (which interest is payable pursuant to an Interest Drawing), each certificate to state therein that it is given by your duly authorized representative and dated the date such certificate is presented hereunder. No drawings shall be made under this Letter of Credit for Liquidity Provider Certificates (as defined in the Trust Agreement) or Certificates registered in the name of the Applicant.

All drawings shall be made by presentation of each Payment Document by facsimile (at facsimile number (312) 954-6163 or alternately to (312) 954-3140), Attention: Standby Service Unit, without further need of documentation, including the original of this Letter of Credit, it being understood that each Payment Document so submitted is to be the sole operative instrument of drawing.

We agree to honor and pay the amount of any Interest Drawing, Principal Drawing or Liquidity Drawing if presented in compliance with all of the terms of this Letter of Credit. If such drawing, other than a Liquidity Drawing, is presented at or prior to 5:00 P.M., Eastern time, on a Business Day, payment shall be made to the account number or address designated by you of the amount specified, in immediately available funds, by 1:00 P.M., Eastern time, on the following Business Day. If any such drawing, other than a Liquidity Drawing, is presented after 5:00 P.M., Eastern time, on a Business Day, payment shall be made to the account number or address designated by you of the amount specified, in immediately available funds, by 1:00 P.M., Eastern time, on the second following Business Day. If a Liquidity Drawing is presented at or prior to 12:30 P.M., Eastern Time, on a Business Day, payment shall be made to the account number or address designated by you of the amount specified, in immediately available funds, by 2:30 P.M., Eastern time, on the same Business Day. If a Liquidity Drawing is presented after 12:30 P.M., Eastern time, payment shall be made to the account number and at such bank designated by you of the amount specified, in immediately available funds, by 2:30 P.M., Eastern time, on the following Business Day. Payments made hereunder shall be made by wire transfer to you or by deposit into your account with us in accordance with the instructions

specified by you in the drawing certificate relating to a particular drawing hereunder. "*Business Day*" means any day other than (i) a Saturday or Sunday, (ii) a day on which banking institutions in the city or cities in which the principal corporate trust office of the Trustee (as defined in the Trust Agreement) or the Trustee is located or banking institutions in New York, New York are authorized or required by law to close, (iii) in the case of the Bank, a day on which banking institutions in the city in which the office of the Bank at which drawings under the Letter of Credit are to be presented is located are authorized or required by law to close or (iv) any day on which the New York Stock Exchange is closed.

The Available Amount (as hereinafter defined) will be reduced automatically by the amount of any drawing hereunder; *provided, however*, that the amount of any Interest Drawing hereunder that is not accompanied by a Principal Drawing or Liquidity Drawing shall be automatically reinstated immediately on the fifth day after demand for payment is honored by us unless you receive a Default Notice (which may include delivery by telecopier, telex, prepaid telegram or other telecommunication) on or before the close of business on such date. After payment by us of a Liquidity Drawing, the obligation of the Bank to honor drawings under this Letter of Credit will be automatically reduced by an amount equal to the Original Purchase Price (as defined below) of any Certificates (or portions thereof) purchased pursuant to said drawing. In addition, prior to the Conversion Date, in the event of the remarketing of the Certificates (or portions thereof) previously purchased with the proceeds of a Liquidity Drawing, our obligation to honor drawings hereunder shall be automatically reinstated concurrently upon receipt by the Bank, or the Trustee on the Bank's behalf, of an amount equal to the Original Purchase Price of such Certificates (or portion thereof) plus accrued interest thereon as required under the Reimbursement Agreement as specified in a certificate in the form of Annex I hereto; the amount of such reinstatement shall be equal to the Original Purchase Price of such Certificates (or portions thereof). "*Original Purchase Price*" shall mean the principal amount of any Certificate purchased with the proceeds of a Liquidity Drawing plus the amount of accrued interest with respect to such Certificate paid with the proceeds of a Liquidity Drawing (and not pursuant to an Interest Drawing) upon such purchase.

Upon receipt by us of a certificate of the Trustee in the form of Annex F hereto, the Available Amount to be drawn hereunder will automatically and permanently be reduced by the amount specified in such certificate. Such reduction shall be effective as of the next Business Day following the date of delivery of such certificate. Upon any permanent reduction of the Available Amount to be drawn under this Letter of Credit, as provided herein, we will deliver to you an amendment to this Letter of Credit substantially in the form of Annex J hereto to reflect any such reduction. The "*Available Amount*" shall mean the Original Stated Amount (i) less the amount of all prior reductions pursuant to Interest Drawings, Principal Drawings or Liquidity Drawings, (ii) less the amount of any reduction thereof pursuant to a certificate in the form of Annex F hereto, (iii) plus the amount of all reinstatements as above provided.

Prior to the Termination Date, we may extend the Stated Expiration Date from time to time at the request of the Applicant by delivering to you an amendment to this Letter of Credit in the form of Annex H hereto designating the date to which the Stated Expiration Date is being extended. Each such extension of the Stated Expiration Date shall become effective on the Business Day following delivery of such notice to you and thereafter all references in this Letter of Credit to

the Stated Expiration Date shall be deemed to be references to the date designated as such in such notice. Any date to which the Stated Expiration Date has been extended as herein provided may be extended in a like manner.

Upon the Termination Date this Letter of Credit shall automatically terminate and be delivered to the Bank for cancellation. Failure to deliver said Letter of Credit will have no effect on the Termination Date, and the Letter of Credit will still be considered terminated.

This Letter of Credit is transferable to any transferee who has succeeded you as Trustee under the Trust Agreement, and may be successively transferred. Any transfer request must be affected by presenting to us the attached form of Annex G signed by the transferor and the transferee together with the original Letter of Credit. Upon our endorsement of such transfer, the transferee instead of the transferor shall, without necessity of further action, be entitled to all the benefits of and rights under this Letter of Credit in the transferor's place; *provided* that, in such case, any certificates of the Trustee to be provided hereunder shall be signed by one who states therein that he is a duly authorized officer or agent of the transferee.

Communications with respect to this Letter of Credit shall be addressed to us at JPMorgan Chase Bank, N.A., 131 South Dearborn, 5<sup>th</sup> Floor, Mail Code IL1-0236, Chicago, IL 60603-5506, Attention: Standby Letter of Credit Unit, specifically referring to the number of this Letter of Credit. For telephone assistance, please contact the Standby Client Service Unit at 1-800-634-1969, select Option 1, and have this Letter of Credit number available.

Except as expressly stated herein, this Letter of Credit is governed by, and construed in accordance with the International Standby Practices, ICC Publication No. 590 (the "ISP98"). As to matters not governed by the ISP98, this Letter of Credit shall be governed by and construed in accordance with the laws of the State of New York, including without limitation the Uniform Commercial Code as in effect in the State of New York, without regard to principals of conflict of laws.

All payments made by us hereunder shall be made from our funds and not with the funds of any other Person.

*(Signature Page Follows)*

This Letter of Credit sets forth in full the terms of our undertaking, and such undertaking shall not in any way be modified or amended by reference to any other document whatsoever except the attached annexes.

Very truly yours,

JPMORGAN CHASE BANK, N.A.

By: \_\_\_\_\_  
Name:  
Title:

ANNEX A  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992

NOTICE OF CONVERSION DATE

[Date]

JPMorgan Chase Bank, N.A.  
131 South Dearborn  
5th Floor, Mail Code IL1-0236  
Chicago, IL 60603-5506

Attn: Standby Letter of Credit Unit

Ladies and Gentlemen:

Reference is hereby made to that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "*Letter of Credit*"), which has been established by you for the account of the City of Modesto, in favor of the Trustee.

The undersigned hereby certifies and confirms that the Conversion Date of all of the Certificates to an interest rate other than a Daily Rate (as defined in the Trust Agreement) or a Weekly Rate (as defined in the Trust Agreement) has occurred on [insert date], and, accordingly, said Letter of Credit shall terminate 5 days after such Conversion Date in accordance with its terms.

All defined terms used herein which are not otherwise defined herein shall have the same meaning as in the Letter of Credit.

The Bank of New York Mellon Company,  
N.A., as Trustee

By: \_\_\_\_\_  
[Title of Authorized  
Representative]

ANNEX B  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992

NOTICE OF TERMINATION

[Date]

JPMorgan Chase Bank, N.A.  
131 South Dearborn  
5th Floor, Mail Code IL1-0236  
Chicago, IL 60603-5506

Attn: Standby Letter of Credit Unit

Ladies and Gentlemen:

Reference is hereby made to that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "*Letter of Credit*"), which has been established by you for the account of the City of Modesto, in favor of the Trustee.

The undersigned hereby certifies and confirms that (i) no Certificates (as defined in the Letter of Credit) remain outstanding within the meaning of the Trust Agreement, (ii) all drawings required to be made under the Trust Agreement and available under the Letter of Credit have been made and honored, or (iii) a substitute letter of credit has been issued to replace the Letter of Credit pursuant to the Trust Agreement, and, accordingly, the Letter of Credit shall be terminated in accordance with its terms.

All defined terms used herein which are not otherwise defined shall have the same meaning as in the Letter of Credit.

The Bank of New York Mellon Company,  
N.A., as Trustee

By \_\_\_\_\_  
[Title of Authorized  
Representative]

INTEREST DRAWING CERTIFICATE

JPMorgan Chase Bank, N.A.  
(facsimile number (312) 954-6163  
alternately to (312) 954-3140)

Attn: Standby Letter of Credit Unit

The undersigned individual, a duly authorized representative of The Bank of New York Mellon Company, N.A., as Trustee (the "*Beneficiary*"), hereby CERTIFIES on behalf of the Beneficiary as follows with respect to (i) that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "*Letter of Credit*"), issued by JPMORGAN CHASE BANK, N.A. (the "*Bank*") in favor of the Beneficiary; (ii) those certain Certificates (as defined in the Letter of Credit); and (iii) that certain Trust Agreement (as defined in the Letter of Credit):

1. The Beneficiary is the Trustee (as defined in the Letter of Credit) under the Trust Agreement.

2. The Beneficiary is entitled to make this drawing in the amount of U.S. \$ \_\_\_\_\_ under the Letter of Credit pursuant to the Trust Agreement with respect to the payment of interest due with respect to all Certificates outstanding on the Interest Payment Date (as defined in the Trust Agreement) occurring on [insert applicable date], other than Liquidity Provider Certificates (as defined in the Trust Agreement) and Certificates registered in the name of the Applicant (as defined in the Letter of Credit).

3. The amount of the drawing is equal to the amount required to be drawn by the Trustee pursuant to the Trust Agreement.

4. The amount of the drawing made by this Certificate was computed in compliance with the terms of the Trust Agreement and, when added to the amount of any other drawing under the Letter of Credit made simultaneously herewith, does not exceed the Available Amount (as defined in the Letter of Credit).

5. Payment by the Bank pursuant to this drawing shall be made to \_\_\_\_\_, ABA Number \_\_\_\_\_, Account Number \_\_\_\_\_, Attention: \_\_\_\_\_, Re: \_\_\_\_\_.

(Signature Page Follows)

**ANNEX C  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992  
(CONTINUED)**

IN WITNESS WHEREOF, this Certificate has been executed this \_\_\_\_ day of \_\_\_\_\_, 201\_.

The Bank of New York Mellon Company,  
N.A., as Trustee

By \_\_\_\_\_  
[Title of Authorized  
Representative]

PRINCIPAL DRAWING CERTIFICATE

JPMorgan Chase Bank, N.A.  
(facsimile number (312) 954-6163  
alternately to (312) 954-3140)

Attn: Standby Letter of Credit Unit

The undersigned individual, a duly authorized representative of The Bank of New York Mellon Company, N.A., as Trustee (the "*Beneficiary*"), hereby CERTIFIES on behalf of the Beneficiary as follows with respect to (i) that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "*Letter of Credit*"), issued by JPMORGAN CHASE BANK, N.A. (the "*Bank*") in favor of the Beneficiary; (ii) those certain Certificates (as defined in the Letter of Credit); and (iii) that certain Trust Agreement (as defined in the Letter of Credit):

1. The Beneficiary is the Trustee (as defined in the Letter of Credit) under the Trust Agreement.

2. The Beneficiary is entitled to make this drawing in the amount of U.S. \$ \_\_\_\_\_ under the Letter of Credit pursuant to the Trust Agreement.

3. (a) The amount of this drawing is equal to (i) the principal amount of Certificates to be paid (whether at maturity or by redemption) pursuant to the Trust Agreement on [insert applicable date] (the "*Principal Date*"), other than Liquidity Provider Certificates (as defined in the Trust Agreement) and Certificates registered in the name of the Applicant (as defined in the Letter of Credit), plus (ii) interest with respect to such Certificates accrued from the immediately preceding Interest Payment Date (as defined in the Trust Agreement) to the Principal Date, provided that in the event the Principal Date coincides with an Interest Payment Date this drawing does not include any accrued interest with respect to such Certificates.

(b) Of the amount stated in paragraph 2 above:

(i) U.S. \$ \_\_\_\_\_ is demanded in respect of the principal amount of the Certificates referred to in subparagraph (a) above; and

(ii) U.S. \$ \_\_\_\_\_ is demanded in respect of accrued interest with respect to such Certificates.

4. Payment by the Bank pursuant to this drawing shall be made to \_\_\_\_\_, ABA Number \_\_\_\_\_, Account Number \_\_\_\_\_, Attention: \_\_\_\_\_, Re: \_\_\_\_\_.

ANNEX D  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992  
(CONTINUED)

5. The amount of the drawing made by this Certificate was computed in compliance with the terms and conditions of the Trust Agreement and, when added to the amount of any other drawing under the Letter of Credit made simultaneously herewith, does not exceed the Available Amount (as defined in the Letter of Credit).

6. Upon payment of the amount drawn hereunder, the Bank is hereby directed to permanently reduce the Available Amount by U.S. \$[insert amount of reduction] and the Available Amount shall thereupon equal U.S. \$[insert new Available Amount]. The Available Amount has been reduced by an amount equal to the principal of Certificates paid with this drawing and an amount equal to 56 days' interest thereon at the Cap Interest Rate (as defined in the Letter of Credit).

7. Of the amount of the reduction stated in paragraph 6 above:

(i) U.S. \$ \_\_\_\_\_ is attributable to the principal amount of Certificates redeemed or paid at maturity; and

(ii) U.S. \$ \_\_\_\_\_ is attributable to interest with respect to such Certificates (*i.e.*, 56 days' interest thereon at the Cap Interest Rate).

8. The amount of the reduction in the Available Amount has been computed in accordance with the provisions of the Letter of Credit.

9. Following the reduction, the Available Amount shall be at least equal to the aggregate principal amount of the Certificates outstanding (to the extent such Certificates are not Liquidity Provider Certificates (as defined in the Trust Agreement) or Certificates registered in the name of the Applicant (as defined in the Letter of Credit) plus 56 days' interest thereon at the Cap Interest Rate.

\*10. Upon application of the proceeds drawn hereunder, no Certificates will remain Outstanding (as defined in the Trust Agreement).

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\* To be included in certificate only if no Certificates will remain Outstanding after application of the proceeds of the Principal Drawing.

**ANNEX D  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992  
(CONTINUED)**

IN WITNESS WHEREOF, this Certificate has been executed this \_\_\_\_\_ day of

\_\_\_\_\_.

The Bank of New York Mellon Company,  
N.A., as Trustee

By \_\_\_\_\_  
[Title of Authorized  
Representative]

ANNEX E  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992

LIQUIDITY DRAWING CERTIFICATE

JPMorgan Chase Bank, N.A.  
(facsimile number (312) 954-6163  
alternately to (312) 954-3140)

Attn: Standby Letter of Credit Unit

The undersigned individual, a duly authorized representative of The Bank of New York Mellon Company, N.A., as Trustee (the "*Beneficiary*"), hereby CERTIFIES on behalf of the Beneficiary as follows with respect to (i) that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "*Letter of Credit*"), issued by JPMORGAN CHASE BANK, N.A. (the "*Bank*") in favor of the Beneficiary; (ii) those certain Certificates (as defined in the Letter of Credit); and (iii) that certain Trust Agreement (as defined in the Letter of Credit):

1. The Beneficiary is the Trustee under the Trust Agreement.
2. The Beneficiary is entitled to make this drawing under the Letter of Credit in the amount of U.S. \$ \_\_\_\_\_ with respect to the payment of the purchase price of Certificates tendered for purchase in accordance with the Trust Agreement and to be purchased on [insert applicable date] (the "*Purchase Date*") which Certificates have not been remarketed as provided in the Trust Agreement or the purchase price of which has not been received by the Trustee (as defined in the Letter of Credit) on said Purchase Date.
3. (a) The amount of the drawing is equal to (i) the principal amount of Certificates to be purchased pursuant to the Trust Agreement on the Purchase Date, other than Liquidity Provider Certificates (as defined in the Trust Agreement) and Certificates registered in the name of the Applicant (as defined in the Letter of Credit), plus (ii) interest with respect to such Certificates accrued from the immediately preceding Interest Payment Date (as defined in the Trust Agreement) (or if none, the date of issuance of the Certificates) to the Purchase Date, provided that in the event the Purchase Date coincides with an Interest Payment Date this drawing does not include any accrued interest with respect to such Certificates.  
  
(b) Of the amount stated in paragraph (2) above:
  - (i) U.S. \$ \_\_\_\_\_ is demanded in respect of the principal portion of the purchase price of the Certificates referred to in subparagraph (2) above; and
  - (ii) U.S. \$ \_\_\_\_\_ is demanded in respect of payment of the interest portion of the purchase price of such Certificates.

ANNEX E  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992  
(CONTINUED)

4. The amount of the drawing made by this Certificate was computed in compliance with the terms and conditions of the Trust Agreement and, when added to the amount of any other drawing under the Letter of Credit made simultaneously herewith, does not exceed the Available Amount (as defined in the Letter of Credit).

5. The Beneficiary will register or cause to be registered in the name of the Bank, upon payment of the amount drawn hereunder, Certificates (or beneficial interests therein) in the principal amount of the Certificates being purchased with the amounts drawn hereunder in accordance with the requirements of the Custodian Agreement dated as of July 1, 2011, among The Bank of New York Mellon Company, N.A. (as custodian), the Applicant (as defined in the Letter of Credit) and the Bank.

6. Payment by the Bank pursuant to this drawing shall be made to \_\_\_\_\_, ABA Number \_\_\_\_\_, Account Number \_\_\_\_\_, Attention: \_\_\_\_\_, Re: \_\_\_\_\_.

IN WITNESS WHEREOF, this Certificate has been executed this \_\_\_\_\_ day of \_\_\_\_\_, \_\_\_\_\_.

The Bank of New York Mellon Company,  
N.A., as Trustee

By \_\_\_\_\_  
[Title of Authorized  
Representative]

REDUCTION CERTIFICATE

JPMorgan Chase Bank, N.A.  
131 South Dearborn  
5th Floor, Mail Code IL1-0236  
Chicago, IL 60603-5506

Attn: Standby Letter of Credit Unit

The undersigned individual, a duly authorized representative of The Bank of New York Mellon Company, N.A., as Trustee (the "*Beneficiary*"), hereby CERTIFIES on behalf of the Beneficiary as follows with respect to (i) that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "*Letter of Credit*"), issued by JPMORGAN CHASE BANK, N.A. (the "*Bank*") in favor of the Beneficiary; (ii) those certain Certificates (as defined in the Letter of Credit); and (iii) that certain Trust Agreement (as defined in the Letter of Credit):

1. The Beneficiary is the Trustee under the Trust Agreement.
2. Upon receipt by the Bank of this Certificate, the Available Amount (as defined in the Letter of Credit) shall be permanently reduced by U.S.\$ \_\_\_\_\_ and the Available Amount shall thereupon equal U.S. \$ \_\_\_\_\_. U.S. \$ \_\_\_\_\_ of the new Available Amount is attributable to interest.
3. The amount of the reduction in the Available Amount has been computed in accordance with the provisions of the Letter of Credit.
4. Following the reduction, the Available Amount shall be at least equal to the aggregate principal amount of the Certificates outstanding, other than Liquidity Provider Certificates (as defined in the Trust Agreement) and Certificates registered in the name of the Applicant (as defined in the Letter of Credit) plus 56 days' interest thereon at the Cap Interest Rate (as defined in the Letter of Credit).

IN WITNESS WHEREOF, this Certificate has been executed this \_\_\_\_\_ day of \_\_\_\_\_, \_\_\_\_\_.

The Bank of New York Mellon Company,  
N.A., as Trustee

By \_\_\_\_\_  
[Title of Authorized  
Representative]

ANNEX G  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992

REQUEST FOR TRANSFER

JPMorgan Chase Bank, N.A.  
131 South Dearborn  
5th Floor, Mail Code IL1-0236  
Chicago, IL 60603-5506

Date: \_\_\_\_\_

Attn: Standby Letter of Credit Unit

Re: JPMorgan Chase Bank, N.A. Irrevocable Standby Letter of Credit No. CPCS-923992

We, the undersigned "Transferor", hereby irrevocably transfer all of our rights to draw under the above referenced Letter of Credit ("Credit") in its entirety to:

NAME OF TRANSFEREE

\_\_\_\_\_  
(Print Name and complete address of the Transferee) "Transferee"

ADDRESS OF TRANSFEREE

\_\_\_\_\_  
CITY, STATE/COUNTRY ZIP  
\_\_\_\_\_

In accordance with ISP98, Rule 6, regarding transfer of drawing rights, all rights of the undersigned Transferor in the Credit are transferred to the Transferee, who shall have the sole rights as beneficiary thereof, including sole rights relating to any amendments whether increases or extensions or other amendments and whether now existing or hereafter made. All amendments are to be advised directly to the Transferee without necessity of any consent of or notice to the undersigned Transferor.

The original Credit, including amendments to this date, is attached and the undersigned Transferor requests that you endorse an acknowledgment of this transfer on the reverse thereof. The undersigned Transferor requests that you notify the Transferee of this Credit in such form and manner as you deem appropriate, and the terms and conditions of the Credit as transferred. The undersigned Transferor acknowledges that you incur no obligation hereunder and that the transfer shall not be effective until you have expressly consented to the transfer by notice to the Transferee.

If you agree to these instructions, please advise the Transferee of the terms and conditions of this transferred Credit and these instructions.

**ANNEX G**  
**TO**  
**JPMORGAN CHASE BANK, N.A.**  
**LETTER OF CREDIT**  
**NO. CPCS-923992**  
**(CONTINUED)**

Payment of transfer fee of U.S \$3,000 is for the account of the Applicant who agrees to pay you on demand any expense or cost you may incur in connection with the transfer. Receipt of such shall not constitute consent by you to the transfer.

Transferor represents and warrants that (a) the Transferee is the Transferor's successor trustee under the Trust Agreement, (b) the enclosed Credit is original and complete, and (c) there is no outstanding demand or request for payment or transfer under the Credit affecting the rights to be transferred.

The Effective Date shall be the date hereafter on which Transferring Bank effects the requested transfer by acknowledging this request and giving notice thereof to Transferee.

**WE WAIVE ANY RIGHT TO TRIAL BY JURY THAT WE MAY HAVE IN ANY ACTION OR PROCEEDING RELATING TO OR ARISING OUT OF THIS TRANSFER.**

This Request is made subject to ISP98 and is subject to and shall be governed by the laws of the State of New York, without regard to principles of conflict of laws.

*(Signature Page Follows)*

**ANNEX G**  
**TO**  
**JPMORGAN CHASE BANK, N.A.**  
**LETTER OF CREDIT**  
**No. CPCS-923992**  
**(CONTINUED)**

Sincerely yours,

\_\_\_\_\_  
(Print Name of Transferor)

\_\_\_\_\_  
(Transferor's Authorized Signature)

\_\_\_\_\_  
(Print Authorized Signers Name and Title)

\_\_\_\_\_  
(Telephone Number/Fax Number)

SIGNATURE GUARANTEED  
Signature(s) with title(s) conform(s) with that/those on file with us for this individual, entity or company and signer(s) is/are authorized to execute this agreement.

\_\_\_\_\_  
(Print Name of Bank)

\_\_\_\_\_  
(Address of Bank)

\_\_\_\_\_  
(City, State, Zip Code)

\_\_\_\_\_  
(Print Name and Title of Authorized Signer)

\_\_\_\_\_  
(Authorized Signature)

\_\_\_\_\_  
(Telephone Number)

\_\_\_\_\_  
(Date)

Acknowledged:

\_\_\_\_\_  
(Print Name of Transferee)

\_\_\_\_\_  
(Transferee's Authorized Signature)

\_\_\_\_\_  
(Print Authorized Signers Name and Title)

\_\_\_\_\_  
(Telephone Number/Fax Number)

SIGNATURE GUARANTEED  
Signature(s) with title(s) conform(s) with that/those on file with us for this individual, entity or company and signer(s) is/are authorized to execute this agreement.

\_\_\_\_\_  
(Print Name of Bank)

\_\_\_\_\_  
(Address of Bank)

\_\_\_\_\_  
(City, State, Zip Code)

\_\_\_\_\_  
(Print Name and Title of Authorized Signer)

\_\_\_\_\_  
(Authorized Signature)

\_\_\_\_\_  
(Telephone Number)

\_\_\_\_\_  
(Date)

**ANNEX G  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992  
(CONTINUED)**

Acknowledged as of \_\_\_\_\_, 201\_:

JPMorgan Chase Bank, N.A.

By: \_\_\_\_\_

Name:

Title:

**ANNEX H  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992**

**NOTICE OF EXTENSION AMENDMENT**

\_\_\_\_\_

The Bank of New York Mellon Company, N.A.  
555 Kearney Street, Suite 600  
San Francisco, California 94108

Attention: Corporate Trust Department

Ladies and Gentlemen:

Reference is hereby made to that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "*Letter of Credit*"), established by us in your favor as Beneficiary. We hereby notify you that, in accordance with the terms of the Letter of Credit and that certain Reimbursement Agreement dated as of July 1, 2011, between the City of Modesto and us, the Stated Expiration Date (as defined in the Letter of Credit) has been extended to \_\_\_\_\_.

This letter shall be attached to the Letter of Credit and made a part thereof.

JPMorgan Chase Bank, N.A.

By: \_\_\_\_\_  
Name:  
Title:

REINSTATEMENT CERTIFICATE

JPMorgan Chase Bank, N.A.  
(facsimile number (312) 954-6163  
alternately to (312) 954-3140)

Attn: Standby Letter of Credit Unit

The undersigned hereby certifies to JPMorgan Chase Bank, N.A. (the "Bank"), with reference to Irrevocable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "Letter of Credit") issued by the Bank in favor of the Trustee, that:

1. The undersigned is the Trustee under the Trust Agreement.
2. The Trustee has previously made a Liquidity Draw under the Letter of Credit on \_\_\_\_\_ in the amount of U.S. \$ \_\_\_\_\_ (representing U.S. \$ \_\_\_\_\_ of principal and U.S. \$ \_\_\_\_\_ of interest) with respect to the purchase price of Certificates which are Liquidity Provider Certificates (as defined in the Trust Agreement).
3. The Bank of New York Mellon Company, N.A., as Trustee and custodian under the Custodian Agreement, dated as of July 1, 2011, among The Bank of New York Mellon Company, N.A., the Applicant (as defined in the Letter of Credit) and the Bank has received proceeds from the sale of remarketed Liquidity Provider Certificates originally purchased with the proceeds of the above described Liquidity Drawing and as of the date hereof holds U.S. \$ \_\_\_\_\_ (representing U.S. \$ \_\_\_\_\_ of principal and U.S. \$ \_\_\_\_\_ of interest) with respect to the sale of such Liquidity Provider Certificates.
4. In accordance with the terms of the Letter of Credit, the Available Amount (as defined in the Letter of Credit) is hereby automatically reinstated to the extent of the lesser of (i) the proceeds of such remarketed Liquidity Provider Certificates (as described in paragraph 3 above), or (ii) the amount of the Liquidity Drawing described above, all in accordance with the terms of the Letter of Credit and this notice.

IN WITNESS WHEREOF, the undersigned has executed and delivered this Certificate this \_\_\_\_ day of \_\_\_\_\_, \_\_\_\_\_.

The Bank of New York Mellon Company,  
N.A., as Trustee

By \_\_\_\_\_  
[Title of Authorized  
Representative]

ANNEX J  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992

NOTICE OF REDUCTION AMENDMENT

[Date]

The Bank of New York Mellon Company, N.A.  
555 Kearney Street, Suite 600  
San Francisco, California 94108

Attention: Corporate Trust Department

Ladies and Gentlemen:

Reference is hereby made to that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "Letter of Credit"), established by us in your favor as Beneficiary. We hereby notify you that, in accordance with the terms of the Letter of Credit, the Available Amount (as defined in the Letter of Credit) has been reduced to U.S.

\$ \_\_\_\_\_, of which U.S. \$ \_\_\_\_\_ is attributable to principal and U.S.  
\$ \_\_\_\_\_ is attributable to interest.

This letter shall be attached to the Letter of Credit and made a part thereof.

JPMorgan Chase Bank, N.A.

By: \_\_\_\_\_  
Name:  
Title:

CLOSING MEMORANDUM

\$47,625,000  
CITY OF MODESTO  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

EXTENSION OF LETTER OF CREDIT

This memorandum will summarize the procedures to be followed in satisfying the conditions precedent to the extension of a letter of credit for the City of Modesto, California (the “City”) of its Water Refunding Revenue Certificates of Participation, 2008 Series A (the “Certificates”).

CLOSING SCHEDULE

Wednesday, June 4, 2014	Via Sidley Austin’s Firmex Virtual Closing Site	Pre-Closing
Thursday, June 5, 2014	Via Sidley Austin’s Firmex Virtual Closing Site	Closing

\$47,625,000  
CITY OF MODESTO  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

MEMORANDUM OF LEGAL PAPERS

to be included in transcripts  
relating to the above-mentioned Certificates

\*\*\*\*\*

Closing: Thursday, June 5, 2014

Complete transcripts are to be prepared for distribution to the following parties:

Modesto Public Financing Authority (the “Authority”)

\*City of Modesto (the “City”)

The Bank of New York Mellon Trust Company, N.A. (the “Trustee”)

\*Sidley Austin LLP (“Bond Counsel” or “BC”)

\*JPMorgan Chase Bank, National Association (the “Bank”)

McGuireWoods LLP (“Bank Counsel”)

Public Financial Management, Inc. (“PFM”)

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\* We will be preparing transcripts on CD-ROM for all parties. In addition to CD-ROM copies, parties indicated above with an asterisk (\*) will be receiving one paper copy of the transcript with original signatures of the primary documents.

**Pre-Closing**

The Pre-Closing will be held on Wednesday, June 4, 2014, via Sidley's Virtual Closing Site.

The parties indicated below will deliver five (5) originals of each of the respective documents so indicated below. The documents will be executed in advance of the Closing by the respective parties thereto and delivered no later than the Pre-Closing. Unless otherwise indicated, the documents will be dated as of the date of Closing. All such deliveries will be deemed to have been made in escrow until final delivery at the Closing has been made.

Responsibility for preparing or assembling the documents is indicated in parentheses.

**Closing**

In connection with the extension of the letter of credit for the Bonds, a closing email will be distributed to the financing team by Sidley indicating the transaction is closed.

\$47,625,000  
CITY OF MODESTO  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

DOCUMENTS AND INSTRUMENTS

The following documents and instruments are to be delivered to the appropriate party or parties at the Pre-Closing.

	<u>Index Number</u>
I. <u>BASIC DOCUMENTS</u>	
1. Certified copy of the AMENDED AND RESTATED TRUST AGREEMENT, dated as of May 1, 2008 and amended and restated July 14, 2011, by and between Trustee and the Authority. (BC)	1
2. Certified copy of the REIMBURSEMENT AGREEMENT, dated as of July 1, 2011, between the City and the Bank. (BC)	2
3. Executed copy of the FIRST AMENDMENT TO THE REIMBURSEMENT AGREEMENT, dated as of June 5, 2014, between the City and the Bank. (Bank Counsel)	3
4. Executed copy of the FEE LETTER, dated June 5, 2014, between the City and the Bank. (Bank Counsel)	4
5. SPECIMEN COPY OF NOTICE OF EXTENSION OF LETTER OF CREDIT. (Bank Counsel)	5
6. OFFICIAL STATEMENT SUPPLEMENT NO. 2, dated June 5, 2014, to Official Statement dated May 29, 2008 as supplemented by the Official Statement Supplement No. 1, dated July 5, 2011, and as amended by Amendment to Official Statement Supplement No. 1, dated July 5, 201. (BC)	6

II. AUTHORIZATION OF THE FINANCING

A. By the City

1. Certified copy of Resolution No. 2014-213 of the City Council of the City, adopted June 3, 2014, entitled “A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF MODESTO RELATING TO WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION, 2008 SERIES A; APPROVING THE FORMS OF AND AUTHORIZING THE EXECUTION AND DELIVERY OF A FIRST AMENDMENT TO REIMBURSEMENT AGREEMENT AND FEE LETTER AND APPROVING THE FORM OF AND AUTHORIZING THE DISTRIBUTION OF A SUPPLEMENT TO AN OFFICIAL STATEMENT IN CONNECTION THEREWITH; AND AUTHORIZING CERTAIN OTHER RELATED ACTIONS.” (BC) 7

B. By the Authority

1. Certified copy of Resolution No. \_\_\_-2014 of the Commission of the Authority, adopted June 3, 2014, entitled “A RESOLUTION OF THE MODESTO PUBLIC FINANCING AUTHORITY RELATING TO WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION, 2008 SERIES A; APPROVING THE FORM OF AND AUTHORIZING THE DISTRIBUTION OF A SUPPLEMENT TO AN OFFICIAL STATEMENT IN CONNECTION THEREWITH; AND AUTHORIZING CERTAIN OTHER RELATED ACTIONS.” (BC) 8

III. CLOSING DOCUMENTS

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IV. NOTICE

1. NOTICE of Extension of Letter of Credit to Notice Parties, dated June 5, 2014, pursuant to Sections 3.11(f), 11.07(b)(iii) and 11.07(c) of the Amended and Restated Trust Agreement. (Trustee) 11

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V. MISCELLANEOUS

1. DISTRIBUTION LIST. (BC)

12

\$47,625,000  
CITY OF MODESTO  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

CERTIFIED COPY OF AMENDED AND RESTATED TRUST AGREEMENT

The undersigned authorized representative of the Modesto Public Financing Authority (the "Authority"), in connection with the City of Modesto Water Revenue Certificates of Participation, 2008 Series A (the "Certificates") DOES HEREBY CERTIFY that attached hereto is a full, true and correct copy of the AMENDED AND RESTATED TRUST AGREEMENT, dated as of May 1, 2008, as amended and restated as of July 14, 2011, between the Authority and The Bank of New York Mellon Trust Company, N.A., and does hereby further certify that such agreement has not been further amended, modified or rescinded since July 14, 2011, and is now in full force and effect.

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IN WITNESS WHEREOF, I have hereunto set my hand this 5<sup>th</sup> day of June, 2014.

MODESTO PUBLIC FINANACING  
AUTHORITY

By:



A handwritten signature in cursive script, appearing to read 'Stephanie Lopez', is written over a horizontal line.

Stephanie Lopez  
Secretary

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AMENDED AND RESTATED TRUST AGREEMENT

between the

MODESTO PUBLIC FINANCING AUTHORITY

and

THE BANK OF NEW YORK MELLON TRUST COMPANY, N.A.,  
as Trustee

Dated as of May 1, 2008

and

Amended and Restated July 14, 2011

Relating to

\$47,625,000

WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

EVIDENCING AND REPRESENTING PROPORTIONATE INTERESTS  
OF THE OWNERS THEREOF IN 2008 PAYMENTS TO BE MADE BY THE  
CITY OF MODESTO  
TO THE  
MODESTO PUBLIC FINANCING AUTHORITY

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## TRUST AGREEMENT

THIS AMENDED AND RESTATED TRUST AGREEMENT, dated July 14, 2011 (the "Trust Agreement"), amending and restating the Trust Agreement dated as of May 1, 2008 (the "Original Trust Agreement"), is by and between the MODESTO PUBLIC FINANCING AUTHORITY, a joint exercise of powers authority duly organized and existing under and by virtue of the laws of the State of California (the "Authority"), and THE BANK OF NEW YORK MELLON TRUST COMPANY, N.A., a national banking association duly organized and existing under and by virtue of the laws of the United States of America (the "Trustee");

### WITNESSETH:

WHEREAS, the Authority is a joint exercise of powers authority duly organized and existing under and pursuant to the Joint Exercise of Powers Act (being Sections 6500 et seq. of the Government Code of the State of California) (the "Act") and a Joint Exercise of Powers Agreement (the "JPA Agreement"), dated as of December 1, 1989, by and between the City of Modesto (the "City") and the Industrial Development Authority of the City of Modesto; and

WHEREAS, the Act and the JPA Agreement authorize and empower the Authority to assist the City in acquiring and financing and refinancing certain additions, betterments, extensions and improvements to the water utility system of the City; and

WHEREAS, the Authority and the City have heretofore entered into a Master Installment Purchase Contract, dated as of November 1, 1997 (the "Master Contract"), as supplemented by the 1997 Supplemental Installment Purchase Contract, dated as of November 1, 1997 (the "1997 Supplemental Contract"), under and pursuant to which the Authority agreed to assist the City by refinancing certain additions, betterments, extensions and improvements to the water utility system of the City (the "1997 Project" as defined therein); and

WHEREAS, the City is obligated to make certain payments to the Authority under the 1997 Supplemental Contract (the "1997 Payments"), and all rights to receive such payments have been assigned by the Authority to State Street Bank and Trust Company of California, N.A., as succeeded by The Bank of New York Mellon Trust Company, N.A. (formerly known as The Bank of New York Trust Company N. A.), as successor trustee for the owners of the Refunding Revenue Certificates of Participation (1997 Water Utility Refinancing Project); and

WHEREAS, the Authority and the City have heretofore entered into the 2006 Supplemental Installment Purchase Contract, dated as of November 1, 2006 (the "2006 Supplemental Contract"), under and pursuant to which the Authority agreed to assist the City by financing certain additions, betterments, extensions and improvements to the water utility system of the City (the "2006 Project" as defined therein); and

WHEREAS, the City is obligated to make certain payments to the Authority under the 2006 Supplemental Contract (the "2006 Payments"), and all rights to receive such payments have been assigned by the Authority to the Trustee, as trustee in relation to the Water Revenue Certificates of Participation 2006 Series A; and

WHEREAS, the Authority and the City have heretofore entered into the 2008 Supplemental Installment Purchase Contract dated as of May 1, 2008 (the "2008 Supplemental Contract" and together with the Master Contract, the 1997 Supplemental Contract, and the 2006 Supplemental Contract, the "Contract"), under and pursuant to which the Authority agreed to assist the City in refinancing the 2006 Project as described in the 2008 Supplemental Contract (the "2008 Project" as defined therein); and

WHEREAS, the City is obligated to make certain payments to the Authority under the 2008 Supplemental Contract (the "2008 Payments"), and all rights to receive such payments are being assigned by the Authority to the Trustee in relation to the Water Refunding Revenue Certificates of Participation, 2008 Series A (the "2008 Certificates"); and

WHEREAS, in consideration of such assignment of the 2008 Payments and the execution and entering into of the Trust Agreement, the Trustee has agreed to execute and deliver the 2008 Certificates in an aggregate principal amount equal to the aggregate principal amount of such 2008 Payments, each representing a proportionate interest in such 2008 Payments; and

WHEREAS, the Authority has determined that all acts, conditions and things required by law to exist, to have happened and to have been performed precedent to and in connection with the execution and delivery of this Trust Agreement do exist, have happened and have been performed in regular and due time, form and manner as required by law, and the execution and delivery of this Trust Agreement have been in all respects duly authorized; and

WHEREAS, in order to support the payment of the principal and Purchase Price of, and interest on, the 2008 Certificates, the Authority, the City and Bank of America, N.A. (the "Initial Liquidity Facility Provider") entered into Standby Certificate Purchase Agreement, dated as of May 1, 2008 (the "Initial Liquidity Facility"); and

WHEREAS, as a result of the expiration of the Initial Liquidity Facility, the Authority and the City have elected to replace the Initial Credit Facility with an Alternate Liquidity Facility in the form of a direct-pay letter of credit (the "Replacement Liquidity Facility") from JPMorgan Chase Bank, N.A. (the "Bank"), effective on the Substitution Date (as defined herein), thereby triggering a mandatory tender of the 2008 Certificates in whole on the Substitution Date for the Initial Liquidity Facility; and

WHEREAS, the Replacement Liquidity Facility constitutes an Alternate Liquidity Facility for purposes of the Contract and this Trust Agreement; and

WHEREAS, the Original Trust Agreement is being amended and restated as of the Substitution Date pursuant to this Trust Agreement, in order to add provisions relating to the Replacement Liquidity Facility; and

WHEREAS, Section 7.01 of the Original Trust Agreement permits any amendments of the Original Trust Agreement, with the prior written consent of the 2008 Certificate Insurer, but without the consent of the Owners, if effective upon the remarketing of the 2008 Certificates following mandatory tender of the 2008 Certificates; and

WHEREAS, this Trust Agreement shall be effective on the Substitution Date;

NOW, THEREFORE, in consideration of the premises and the mutual agreements and covenants herein, and for other valuable consideration, the parties hereto do hereby covenant and agree, as follows:

## ARTICLE I

### DEFINITIONS; EQUAL SECURITY

Section 1.01. Definitions. Unless the context otherwise requires, the terms defined in this Section shall for all purposes hereof and of any Supplemental Trust Agreement and of any certificate, opinion, request or other document herein or therein mentioned have the meanings herein specified unless the context or use clearly indicates another or different meaning or intent:

“Alternate Liquidity Facility” means a letter of credit (including, without limitation, the Replacement Liquidity Facility), line of credit, surety bond, standby purchase agreement or other security or liquidity instrument, as the case may be, approved by the 2008 Certificate Insurer and issued in accordance with the terms hereof with respect to the 2008 Certificates as a replacement or substitute for any Liquidity Facility then in effect.

“Alternate Rate” means, on any Rate Determination Date, for the 2008 Certificates in a Daily Mode, a Weekly Mode, a Flexible Rate Mode or a Term Rate Mode, a rate per annum equal to (a) the SIFMA Municipal Swap Index (the “SIFMA Rate”) most recently available as of the date of determination, or (b) if such index is no longer available, or if the SIFMA Rate is no longer published, the S&P Weekly High Grade Index (formerly the J.J. Kenny Index), or (c) if neither the SIFMA Rate nor the S&P Weekly High Grade Index is published, the index determined to equal the prevailing rate determined by the Remarketing Agent for tax-exempt state and local government bonds meeting criteria determined in good faith by the Remarketing Agent to be comparable under the circumstances to the criteria used by the Securities Industry and Financial Markets Association (“SIFMA”) to determine the SIFMA Rate just prior to when the SIFMA stopped publishing the SIFMA Rate. If there is no Remarketing Agent for the 2008 Certificates, if the Remarketing Agent fails to make any such determination or if the Remarketing Agent has suspended its remarketing efforts in accordance with the Remarketing Agreement, then a financial advisor, investment banker or other qualified party shall make such determination at the expense of the Authority.

“Assigned Rights to Interest” means those rights to receive payment from the Authority pursuant to the Trust Agreement of any interest on 2008 Certificates with respect to which, pursuant to Section 10.05 hereof, the Bank or other Credit enhancement Provider, to the extent it has paid such interest from a drawing under the Replacement Liquidity Facility or other Credit Enhancement, has become subrogated and an assignee and the owner.

“Authority” means the Modesto Public Financing Authority, a joint exercise of powers authority duly organized and existing under and by virtue of the laws of the State.

“Authority Account” means the account by that name established within the 2008 Purchase Fund pursuant to Section 3.09(c) hereof.

“Authorized Denominations” means: (i) with respect to 2008 Certificates in a Daily Mode or Weekly Mode, \$100,000 and any integral multiple of \$5,000 in excess thereof; (ii) with respect to 2008 Certificates in a Flexible Mode, \$100,000 and any integral multiple of \$1,000 in excess thereof; and (iii) with respect to 2008 Certificates in a Term Rate Mode or Fixed Rate Mode, \$5,000 and any integral multiple thereof.

“Automatic Termination Event” means an event of default set forth in a Reimbursement Agreement between the Authority and a Liquidity Facility Provider which would result in the immediate termination of the Liquidity Facility provided pursuant to such Reimbursement Agreement prior to its stated expiration date without prior notice from the Liquidity Facility Provider to the Trustee.

“Available Amount” means the amount available under a Credit Enhancement or Liquidity Facility, as applicable, to pay the principal and interest with respect to the 2008 Certificates or the Purchase Price with respect to the 2008 Certificates, as applicable.

“Bank” means JPMorgan Chase Bank, N.A., and its successors or assigns.

“Basic Certificate Rate” shall mean the rate of interest applicable to 2008 Certificates that are not Liquidity Provider Certificates.

“Beneficial Owner” means, so long as the 2008 Certificates are held in the Book-Entry System, any Person who acquires a beneficial ownership interest in a 2008 Certificate held by the Securities Depository, and during any period the 2008 Certificates are not held in the Book-Entry System, Beneficial Owner shall mean the registered owner for purposes of this Trust Agreement.

“Book-Entry System” means a system under which physical certificates in fully registered form are registered only in the name of a Securities Depository or its nominee.

“Business Day” means any day other than (i) a Saturday or Sunday or (ii) a day on which the Trustee or applicable Remarketing Agent are required or authorized to be closed or (iii) a day on which the office of the applicable Credit Enhancement Provider or applicable Liquidity Facility Provider at which draws or advances will be paid is required or authorized to be closed or (iv) a day on which The New York Stock Exchange is closed.

“Cancellation Date” means the date on which the 2008 Certificate Insurance Policy is cancelled, which date shall be the seventh Business Day following receipt by the Trustee of written notice from (i) the Bank specifying that the 2008 Certificate Insurance Policy is to be cancelled in accordance with the terms of the Reimbursement Agreement between the Bank and the City or (ii) the Authority with the consent of the Bank specifying that the 2008 Certificate Insurance Policy is to be replaced with a substitute Credit Enhancement.

“Certificate of the Authority” means an instrument in writing signed by the Auditor and Treasurer of the Authority or by any other officer of the Authority duly authorized by the Authority for that purpose.

“Certificate Payment Date” means, with respect to any 2008 Certificate, subject to Section 2.03(a) hereof, the Certificate Payment Date designated therein, which is the October 1 on which or, in the case of 2008 Certificates subject to mandatory sinking fund prepayment, by which, the principal component of the final 2008 Payment evidenced and represented thereby shall become due and payable.

“City” means the City of Modesto, a charter city and municipal corporation, duly organized and existing under and by virtue of the Constitution and laws of the State.

“Code” means the Internal Revenue Code of 1986, and the regulations issued thereunder, as the same may be amended from time to time, and any successor provisions of law. Reference to a particular section of the Code shall be deemed to be a reference to any successor to any such section.

“Contract” means that certain Master Contract, as supplemented by the 1997 Supplemental Contract, the 2006 Supplemental Contract, and the 2008 Supplemental Contract, and as otherwise amended or supplemented from time to time.

“Control Event” means that one or more of the circumstances referred to in Section 10.03 hereof has occurred as a result of which all references herein to the 2008 Certificate Insurer and all provisions herein for the benefit of the 2008 Certificate Insurer are of no effect (other than rights of the 2008 Certificate Insurer derived through subrogation and assignment).

“Corporate Trust Office” means the corporate trust office of the Trustee in San Francisco, California, or such other office as may be specified by written notice from the Trustee to the Authority.

“Costs of Issuance” means all items of expense directly or indirectly payable by or reimbursable to the City or the Authority and related to the authorization, execution and delivery of the Contract and the Trust Agreement and the execution, sale and delivery of the 2008 Certificates, including, but not limited to, costs of preparation and reproduction of documents, costs of rating agencies and costs to provide information required by rating agencies, filing and recording fees, initial fees and charges of the Trustee and its counsel, legal fees and charges, fees and disbursements of consultants and professionals, fees and expenses of the underwriter, fees and charges for preparation, execution and safekeeping of the 2008 Certificates, fees and expenses of the Liquidity Facility Provider, fees of the Authority and any other cost, charge or fee in connection with the original execution and delivery of the 2008 Certificates.

“Costs of Issuance Fund” means the fund by that name established pursuant to Section 4.05 hereof.

“Credit Enhancement” means the 2008 Certificate Insurance Policy issued by the 2008 Certificate Insurer. In case a letter of credit is provided as a Liquidity Facility, such letter of credit will also be considered a Credit Enhancement and its issuer, a Credit Enhancement Provider, if such letter of credit is a direct-pay letter of credit that provides for the payment of the principal of, and interest with respect to, the 2008 Certificates as they become due.

“Credit Enhancement Provider” means, with respect to a Credit Enhancement, the issuer or provider thereof.

“Credit Enhancement Provider Failure” means: (i) a failure of a Credit Enhancement Provider to pay any amount due under its Credit Enhancement; (ii) the filing or commencement of any bankruptcy or insolvency proceedings by or against a Credit Enhancement Provider, provided such proceeding has not been dismissed within 60 consecutive days; (iii) the declaration by a Credit Enhancement Provider of a moratorium on the payment of its unsecured debt obligations; or (iv) the written repudiation by a Credit Enhancement Provider of its Credit Enhancement.

“Current Mode” shall have the meaning specified in Section 2.18(a)(i) hereof.

“Daily Mode” means the Mode during which the 2008 Certificates evidence interest at the Daily Rate.

“Daily Rate” means the per annum interest rate with respect to the 2008 Certificates in the Daily Mode determined pursuant to Section 2.15(a) hereof.

“Daily Rate Period” means the period during which the 2008 Certificates in the Daily Mode shall evidence interest at a Daily Rate, which shall be from the Business Day upon which a Daily Rate is set to but not including the next succeeding Business Day.

“Defaulted Interest” means interest evidenced by any 2008 Certificate that is payable but not duly paid on the date due.

“Delayed Remarketing Period” shall have the meaning specified in Section 3.10(b) hereof.

“Delivery Date” means May 30, 2008.

“DTC” means The Depository Trust Company, New York, New York, and its successors and assigns.

“Electronic” means telecopy, facsimile transmission, e-mail transmission or other similar electronic means of communication providing evidence of transmission, including a telephonic communication confirmed by any other method set forth in this definition.

“Eligible Account” means an account that is either (i) maintained with a federal or state-chartered depository institution or trust company that has a Standard & Poor’s short-term debt rating of at least ‘A-2’ (or, if no short-term debt rating, a long-term debt rating of ‘BBB+); or (ii) maintained with the corporate trust department of a federal depository institution or state-chartered depository institution subject to regulations regarding fiduciary funds on deposit similar to Title 12 of the U.S. Code of Federal Regulation Section 9.10(b), which, in either case, has corporate trust powers and is acting in its fiduciary capacity.

“Expiration Date” means the stated expiration date of a Liquidity Facility, as it may be extended from time to time as provided in such Liquidity Facility, or any earlier date on which

such Liquidity Facility shall terminate at the direction of the Authority, expire or be cancelled (other than the date on which a Liquidity Facility shall terminate as a result of an Automatic Termination Event or an event of default under the Reimbursement Agreement entered into in connection with such Liquidity Facility).

“Event of Default” means an event described in Section 8.01 hereof.

“Favorable Opinion of Special Counsel” means, with respect to any action the occurrence of which requires such an opinion, an Opinion of Special Counsel, addressed to the Trustee, to the effect that the action proposed to be taken will not, in and of itself, adversely affect any exclusion from gross income of interest with respect to the 2008 Certificates.

“Federal Securities” shall have the meaning ascribed thereto in the Contract.

“Fiscal Year” means the period beginning on July 1 of each year and ending on the next succeeding June 30, or any other annual accounting period hereafter selected and designated by the Authority as its Fiscal Year.

“Fixed Rate” means the per annum interest rate or interest rates evidenced by the 2008 Certificates in a Fixed Rate Mode determined pursuant to Section 2.16(b) hereof.

“Fixed Rate Certificates” means the 2008 Certificates in a Fixed Rate Mode.

“Fixed Rate Mode” means the Mode during which the 2008 Certificates evidence interest at a Fixed Rate.

“Fixed Rate Period” means, with respect to 2008 Certificates converted to the Fixed Rate Mode, the period from the Mode Change Date upon which the 2008 Certificates were converted to a Fixed Rate Mode to but not including the Maturity Date.

“Fixed Rate Remarketing Agent” means, an investment banking firm or firms selected by the Authority that has or have entered into a written agreement with the Authority to remarket or purchase and remarket the 2008 Certificates upon their being converted to a Fixed Rate Mode in accordance with the terms and provisions set forth herein.

“Flexible Mode” means the Mode during which the 2008 Certificates evidence interest at Flexible Rates.

“Flexible Rate” means, with respect to the 2008 Certificates in a Flexible Mode, the per annum interest rate determined for the 2008 Certificate pursuant to Section 2.14 hereof.

“Flexible Rate Certificates” means the 2008 Certificates in a Flexible Mode.

“Flexible Rate Period” means, with respect to the 2008 Certificates in a Flexible Mode, the period of from 1 to 397 calendar days (which Flexible Rate Period must end on a day preceding a Business Day) during which a Flexible Rate Certificate shall evidence interest at a Flexible Rate, as established by the Remarketing Agent pursuant to Section 2.14 hereof.

“Improvement Fund” means the fund by that name established pursuant to Section 2.02 of the Master Contract.

“Independent Certified Public Accountant” means any certified public accountant or firm of such accountants duly licensed and entitled to practice and practicing as such under the laws of the State, appointed and paid by the Authority, and who, or each of whom—

(1) is in fact independent according to the Statement of Auditing Standards No. 1 and not under the domination of the Authority;

(2) does not have a substantial financial interest, direct or indirect, in the operations of the Authority; and

(3) is not connected with the Authority as a member, officer or employee of the Authority, but who may be regularly retained to audit the accounting records of and make reports thereon to the Authority.

“Information Services” means Financial Information, Inc.’s “Daily Called Bond Service,” 30 Montgomery Street, 10th Floor, Jersey City, New Jersey 07302, Attention: Editor; FIS/Mergent, Inc., 5250 77 Center Drive, Suite 150, Charlotte, North Carolina 28217, Attn: Call Notification; Standard & Poor’s Securities Evaluation, Inc., 55 Water Street, 45th Floor, New York, New York 10041, Attention: Notification Department; Xcitek, 5 Hanover Square, New York, New York 10004; and, in accordance with then current guidelines of the Securities and Exchange Commission, such other addresses and/or such other services providing information with respect to the redemption of bonds or the prepayment of certificates of participation as the Authority may designate in a Certificate of the Authority filed with the Trustee.

“Initial Liquidity Facility” means the Standby Certificate Purchase Agreement, dated as of May 1, 2008, between the Authority and the Initial Liquidity Facility Provider.

“Initial Liquidity Facility Provider” means Bank of America, N.A.

“Insurer Indenture Event of Default” means and includes the occurrence of one or more of the following events:

(a) any principal or interest evidenced by the 2008 Certificates (including Liquidity Provider Certificates or Subrogated Certificates) is not paid by the 2008 Certificate Insurer when, as, and in the amounts required to be paid pursuant to the terms of the 2008 Certificate Insurance Policy; or

(b) (i) any material provision of the 2008 Certificate Insurance Policy relating to the obligation of the 2008 Certificate Insurer to make payments of principal and interest thereunder at any time for any reason ceases to be valid and binding on the 2008 Certificate Insurer in accordance with the terms of the 2008 Certificate Insurance Policy or the New York Department of Insurance, or a court or other governmental authority of appropriate jurisdiction shall find or rule or shall enter an order, judgment or decree that the 2008 Certificate Insurance Policy is not valid and binding on the 2008 Certificate Insurer or (ii) the 2008 Certificate Insurer shall (A) claim in writing that the 2008

Certificate Insurance Policy is not valid and binding on the 2008 Certificate Insurer, (B) repudiate the 2008 Certificate Insurer's obligations under the 2008 Certificate Insurance Policy or (C) initiate legal proceedings seeking an adjudication that the 2008 Certificate Insurance Policy, or any material provision thereof regarding the payment of principal or interest on 2008 Certificates (including Liquidity Provider Certificates) is not valid and binding on the 2008 Certificate Insurer; or

(c) a proceeding is instituted in a court having jurisdiction in the premises seeking an order for relief, rehabilitation, reorganization, conservation, liquidation or dissolution in respect to the 2008 Certificate Insurer or for any substantial part of its property under any applicable bankruptcy, insolvency or other similar law now or hereafter in effect, or for the appointment of a receiver, liquidator, assignee, custodian, trustee or sequestrator (or other similar official) and such proceeding shall not have been dismissed within sixty (60) days or such court enters an order granting the relief sought in such proceeding; or the New York Department of Insurance shall declare a moratorium on the payment of the 2008 Certificate Insurer's debts, or the 2008 Certificate Insurer shall commence a voluntary case under any applicable bankruptcy, insolvency or other similar law now or hereafter in effect, shall consent to the entry of an order for relief in an involuntary case under any such law or shall consent to the appointment of or taking possession by a receiver, liquidator, assignee, trustee, custodian or sequestrator (or other similar official) of the 2008 Certificate Insurer or for any substantial part of its property, or shall make a general assignment for the benefit of creditors, or shall fail generally to pay its debts (provided for purposes of this definition, "debts" shall not include any obligation of the 2008 Certificate Insurer under any insurance policy or surety bond) as they become due, or an order for rehabilitation, liquidation or dissolution of the 2008 Certificate Insurer shall be issued.

"Interest Accrual Period" means the period during which the 2008 Certificates accrue interest payable on the next Interest Payment Date applicable thereto. Each Interest Accrual Period shall commence on (and include) the last Interest Payment Date to which interest has been paid (or, if no interest has been paid, from the date of original authentication and delivery of the 2008 Certificates) to, but not including, the Interest Payment Date on which interest is to be paid. If, at the time of authentication of any 2008 Certificate, interest is in default or overdue with respect to the 2008 Certificates, such 2008 Certificate shall evidence interest from the date to which interest has previously been paid in full or made available for payment in full with respect to the 2008 Certificates.

"Interest Payment Date" means each date on which interest is to be paid and is: (i) with respect to the 2008 Certificates in a Daily Mode or a Weekly Mode, the first Business Day of each month; (ii) with respect to the 2008 Certificates in a Flexible Mode, each Mandatory Purchase Date applicable thereto; (iii) with respect to the 2008 Certificates in a Fixed Rate Mode or a Term Rate Mode, the first day of April or October, which is at least 3 months after the month in which such Long-Term Mode takes effect, and the first day of each April and October thereafter or, upon the receipt by the Trustee of a Favorable Opinion of Special Counsel, any other six-month interval chosen by the Authority (beginning with the first such day which is at least three months after the Mode Change Date) and, with respect to a Term Rate Mode, the final day of the current Interest Period if other than a regular six-month interval; (iv) (without

duplication as to any Interest Payment Date listed above) any Mode Change Date, other than a change between a Daily Mode and a Weekly Mode, and each Maturity Date; and (v) with respect to any Liquidity Provider Certificates, the day set forth in the applicable Reimbursement Agreement.

“Interest Period” means, for the 2008 Certificates in a particular Mode, the period of time that the 2008 Certificates evidence interest at the rate (per annum) which becomes effective at the beginning of such period, and shall include, a Daily Rate Period, a Weekly Rate Period, a Flexible Rate Period, a Term Rate Period, and a Fixed Rate Period. Notwithstanding the preceding sentence, regardless of Mode, so long as any 2008 Certificate is a Liquidity Provider Certificate, the Interest Period shall be determined in accordance with the applicable Liquidity Facility or the applicable Reimbursement Agreement.

“Liquidity Facility” means, as of any time, the Initial Liquidity Facility, the Replacement Liquidity Facility or an Alternate Liquidity Facility, as applicable, which provides for the payment of the purchase price of the 2008 Certificates upon the tender thereof in the event remarketing proceeds are insufficient therefor.

“Liquidity Facility Account” means an Eligible Account by that name established within the 2008 Purchase Fund pursuant to Section 3.09(b) hereof and held in the name of the Trustee for the benefit of the Owners.

“Liquidity Facility Provider” means, with respect to the Replacement Liquidity Facility, the Bank, and with respect to any Alternate Liquidity Facility for the 2008 Certificates, a bank, insurance company, pension fund or other financial institution acceptable to the 2008 Certificate Insurer, including the Bank.

“Liquidity Facility Provider Failure” means: (i) a failure of a Liquidity Facility Provider to pay a properly presented and conforming draw or request for advance; or (ii) the filing or commencement of any bankruptcy or insolvency proceedings by or against a Liquidity Facility Provider, provided such proceeding has not been dismissed within 60 consecutive days; or (iii) the declaration by a Liquidity Facility Provider of a moratorium on the payment of its unsecured debt obligations; or (iv) the written repudiation by a Liquidity Facility Provider of its Liquidity Facility.

“Liquidity Provider Certificates” means any 2008 Certificates purchased by a Liquidity Facility Provider with funds drawn on or advanced under the Liquidity Facility provided by such Liquidity Facility Provider.

“Long-Term Interest Period” means a Term Rate Period or a Fixed Rate Period.

“Long-Term Mode” means a Term Rate Mode or a Fixed Rate Mode.

“Mandatory Purchase Date” means: (i) with respect to a Flexible Rate Certificate, the first Business Day following the last day of each Flexible Rate Period with respect to such Flexible Rate Certificate; (ii) for the 2008 Certificates in a Term Rate Mode, the first Business Day following the last day of each Term Rate Period for such 2008 Certificates; (iii) any Mode Change Date; (iv) any Substitution Date; (v) the fifth Business Day prior to an Expiration Date;

(vi) the date specified by the Trustee following the occurrence of an event of default with respect to the Liquidity Facility or under the related Reimbursement Agreement which requires or gives the Liquidity Facility Provider the option to terminate the Liquidity Facility upon notice and requires that all Outstanding 2008 Certificates secured by such Liquidity Facility be tendered for purchase, which date shall be a Business Day not less than 7 days after the Trustee's receipt of notice of such event of default from the applicable Liquidity Facility Provider and in no event later than the Business Day preceding the termination date specified in the notice of event of default delivered to the Trustee by such Liquidity Facility Provider; (vii) for the 2008 Certificates in a Daily Mode or a Weekly Mode, any Business Day specified by the Authority in a notice delivered to the Trustee and consented to by the Liquidity Facility Provider, which Mandatory Purchase Date shall be not less than twenty (20) days after the Trustee's receipt of such notice from the Authority, and (viii) the Business Day prior to the Cancellation Date.

"Master Contract" means that certain Master Installment Purchase Contract, executed and entered into as a November 1, 1997, by and between the City and the Authority, as the same may be amended or supplemented from time to time.

"Maturity Date" means, with respect to the 2008 Certificates, the maturity date specified for the 2008 Certificates in Section 2.02 hereof or, if Serial Certificates or more than one Term Certificates are established for the 2008 Certificates pursuant to Section 2.18(d) hereof upon a change of the 2008 Certificates to a Fixed Rate Mode, the maturity dates established for such Serial Certificates or Term Certificates.

"Maximum Rate" or "Maximum Interest Rate" means, with respect to all 2008 Certificates other than Liquidity Provider Certificates, a rate of interest of 12% per annum, and with respect to Liquidity Provider Certificates, such rate not greater than 18% as is provided for in the applicable Liquidity Facility; provided, however, that such rate shall not in any event exceed the highest rate then permitted by law.

"Mode" means, as the context may require, the Daily Mode, the Weekly Mode, the Flexible Mode, the Term Rate Mode, or the Fixed Rate Mode.

"Mode Change Date" means with respect to the 2008 Certificates in a particular Mode, the day on which another Mode for the 2008 Certificates begins.

"Mode Change Notice" means the notice from the Authority to the other Notice Parties of the intention of the Authority to change the Mode with respect to the 2008 Certificates.

"Moody's" means Moody's Investors Service Inc., a corporation duly organized and existing under and by virtue of the laws of the State of Delaware, and its successors or assigns, except that if such corporation shall be dissolved or liquidated or shall no longer perform the services of a municipal securities rating agency, then "Moody's" shall be deemed to refer to any other nationally recognized municipal securities rating agency selected by the Authority.

"New Mode" shall have the meaning specified in Section 2.18(a)(i) hereof.

“1997 Certificates” means the \$25,585,000 Refunding Revenue Certificates of Participation (1997 Water Utility System Refinancing Project), evidencing and representing and proportionate interests of the owners thereof in the 1997 Payments to be made by the City.

“1997 Supplemental Contract” means the 1997 Supplemental Installment Purchase Contract, executed and entered into as of November 1, 1997, by and between the City and the Authority, supplementing the Master Contract.

“1997 Payments” means the installment payments required to be made by the City to the Authority under and pursuant to the 1997 Supplemental Contract.

“1997 Trust Agreement” means that certain Trust Agreement, dated as of November 1, 1997, by and between the Authority and State Street Bank and Trust Company, N.A., which has been succeeded by The Bank of New York Trust Company, N.A., as trustee, pursuant to which there was executed and delivered the 1997 Certificates.

“Notice Parties” means the Authority, the City, the Trustee, the Credit Enhancement Provider, if any, the Liquidity Facility Provider, if any, the Remarketing Agent, if any, and the Fixed Rate Remarketing Agent, if any.

“Opinion of Counsel” means a written opinion of counsel of recognized standing in the field of law being addressed in such opinion retained the Authority.

“Outstanding,” when used as of any particular time with reference to 2008 Certificates, means (subject to the provisions of Section 7.02 hereof) all 2008 Certificates except

- (1) 2008 Certificates theretofore cancelled by the Trustee or surrendered to the Trustee for cancellation;
- (2) 2008 Certificates paid or deemed to have been paid within the meaning of Section 9.01 hereof; and
- (3) 2008 Certificates in lieu of or in substitution for which other 2008 Certificates shall have been executed and delivered by the Trustee pursuant hereto.

“Owner” means any person who shall be the registered owner of any Outstanding 2008 Certificate.

“Parity Reserve Fund” means the fund by that name continued pursuant to Section 4.04 hereof.

“Parity Reserve Fund Obligation” means the 1997 Certificates, the 2008 Certificates and any other obligations hereafter issued in connection with a Supplemental Contract.

“Payment Agreement Payments” has the meaning given such term in the Master Contract.

“Payment Agreement Receipts” has the meaning given such term in the Master Contract.

“Permitted Investments” means any of the following obligations if and to the extent then permitted by law:

- (1) Federal Securities;
- (2) Obligations issued by the Resolution Funding Corporation and the Student Loan Marketing Association, or obligations, participations, or other instruments of or issued by, or fully guaranteed as to interest and principal by, the Government National Mortgage Association (excluding stripped mortgage backed securities which are valued at greater than par on the unpaid principal);
- (3) Bills of exchange or time drafts drawn on and accepted by a commercial bank (including the Trustee or any of its affiliates), otherwise known as bankers acceptances, which are eligible for purchase by the Federal Reserve System and which are drawn on any bank the short-term obligations of which are rated in the highest letter and numerical rating category as provided by Moody’s and by S&P; provided, that purchases of eligible bankers acceptances may not exceed 270 days’ maturity;
- (4) Commercial paper of “prime” quality of the highest ranking or of the highest letter and numerical rating category as provided by Moody’s and by S&P, which commercial paper is limited to issuing corporations that are organized and operating within the United States of America and that have total assets in excess of \$500,000,000 and that have an “A1” or higher rating for the issuer’s unsecured debentures, other than commercial paper, as provided by Moody’s and by S&P; provided, that purchases of eligible commercial paper may not exceed 180 days’ maturity nor represent more than 10% of the outstanding commercial paper of an issuing corporation;
- (5) Non-negotiable certificates of deposit issued by a state or national bank (including the Trustee or any of its affiliates) that have maturities of not more than 365 days or deposit accounts with a state or national bank and that are fully insured by the Federal Deposit Insurance Corporation or the short term obligations of which state or national bank are rated no lower that “A1” by Moody’s and “A+” by S&P;
- (6) Any repurchase agreement of any securities enumerated in subdivisions (1) and (2) with any state or national bank (including the Trustee or any of its affiliates) or government bond dealer reporting to, trading with, and recognized as a primary dealer by the Federal Reserve Bank of New York, which agreement is either (A) with any institution which has debt rated no lower than “A1” by Moody’s and “A+” by S&P or whose commercial paper is rated no lower than “P-1” by Moody’s and no lower than “A-1” by S&P; (B) with any corporation or other entity that falls under the jurisdiction of the Federal Bankruptcy Code; provided, that (a) the term of such repurchase agreement is less than one (1) year or due on demand; (b) the Trustee or a third party acting solely as agent for the Trustee has possession of the collateral; (c) the market value of the collateral (as determined at least once in every 14 days) exceeds the principal amount of the repurchase agreement plus accrued interest and the market value of the collateral is maintained at levels acceptable to Moody’s and to S&P; (d) failure to maintain the requisite collateral levels will require the Trustee to liquidate the collateral immediately;

and (e) the repurchase agreement securities are free and clear of any third-party lien or claim; or (C) with financial institutions insured by the Federal Deposit Insurance Corporation or any broker-dealer with "retail customers" which falls under the jurisdiction of the Securities Investors Protection Corporation; provided, that: (a) the market value of the collateral (as determined at least once in every 14 days) exceeds the principal amount of the repurchase agreement plus accrued interest and the market value of the collateral is maintained at levels acceptable to Moody's and to S&P; (b) the Trustee or a third party acting solely as agent for the Trustee has possession of the collateral; (c) the Trustee has a perfected first priority security interest in the collateral; (d) the collateral is free and clear of third-party liens and in the case of a Securities Investors Protection Corporation broker was not acquired pursuant to a repurchase agreement or reverse repurchase agreement; and (e) failure to maintain the requisite collateral percentage will require the Trustee to liquidate the collateral immediately;

(7) Certificates, notes, warrants, bonds or other evidence of indebtedness of the State or any local agencies therein which are rated in the highest short-term rating category or within one of the three highest long-term rating categories by Moody's and by S&P (excluding securities that do not have a fixed par value and/or whose terms do not promise a fixed dollar amount at maturity or call date);

(8) For amounts less than \$100,000, interest-bearing demand or time deposits (including certificates of deposit) in a nationally or state-chartered bank fully insured by the Federal Deposit Insurance Corporation, including the Trustee or any affiliate thereof, and of which an aggregate total of \$100,000 is not exceeded in any one financial institution;

(9) Investments in units of a money-market fund portfolio that is rated in the highest letter and numerical rating category by Moody's and by S&P (including funds for which the Trustee, its affiliates or subsidiaries provide investment advisory or other management services) and that is composed of obligations guaranteed by the full faith and credit of the United States of America or repurchase agreements collateralized by such obligations;

(10) A guaranteed investment contract with a financial institution or insurance company (or guaranteed by a financial institution or insurance company) which has at the date of execution thereof an outstanding issue of unsecured, uninsured and unguaranteed debt obligations or a claims paying ability rated within the two highest rating categories of any Rating Agency;

(11) Other investments approved in writing by the 2008 Certificate Insurer (or, if a Control Event has occurred, the Bank); and

(12) The Local Agency Investment Fund, the California Asset Management Program, or similar pooled fund operated by or on behalf of the State and which is authorized to accept investments by or on behalf of the Authority of the moneys held by the Trustee in any of the accounts or funds established pursuant hereto to the extent deposits and withdrawals may be made by the Trustee directly.

“Person” shall mean an individual, a corporation, an association, a joint venture, a partnership, a trust, an unincorporated organization or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

“Prepayment Date” means the date fixed for prepayment of any 2008 Certificate in any notice of prepayment given in accordance with the terms hereof.

“Purchase Date” means (i) for a 2008 Certificate in the Daily Mode or the Weekly Mode, any Business Day selected by the Beneficial Owner of said 2008 Certificate pursuant to the provisions of Section 3.01 hereof, and (ii) any Mandatory Purchase Date.

“Purchase Price” means an amount equal to the principal amount of the 2008 Certificates purchased on any Purchase Date, plus accrued interest to such Purchase Date (unless such Purchase Date is also an Interest Payment Date, in which case the Purchase Price shall not include accrued interest, which shall be paid in the normal course).

“Rate Determination Date” means any date on which the interest rate with respect to the 2008 Certificates shall be determined, which: (i) in the case of a Flexible Mode, shall be the first day of an Interest Period; (ii) in the case of a Daily Mode, shall be each Business Day commencing with the first day (which must be a Business Day) the 2008 Certificates become subject to the Daily Mode; (iii) in the case of the initial conversion to a Weekly Mode, shall be no later than the Business Day prior to the Mode Change Date for the 2008 Certificates, and thereafter, shall be each Wednesday or, if Wednesday is not a Business Day, then the Business Day next succeeding such Wednesday; (iv) in the case of a Term Rate Mode, shall be a Business Day no earlier than 15 Business Days and no later than the Business Day next preceding the first day of an Interest Period for the 2008 Certificates, as determined by the Remarketing Agent; and (v) in the case of a Fixed Rate Mode, shall be a date determined by the Remarketing Agent which shall be at least one Business Day prior to the Mode Change Date.

“Rating Agencies” means Moody’s and S&P, and their respective successors or assigns, or any other nationally recognized securities rating agency or agencies rating the 2008 Certificates at the request of the City.

“Rating Confirmation Notice” shall mean a written notice from the Rating Agencies then rating the 2008 Certificates, confirming that the rating on the 2008 Certificates (without giving effect to any Liquidity Facility) will not be lowered or withdrawn (other than a withdrawal of a short-term rating upon a change to a Fixed Rate Mode) as a result of the action proposed to be taken.

“Record Date” means: (i) with respect to the 2008 Certificates in a Short-Term Mode, the last Business Day before each Interest Payment Date; and (ii) with respect to the 2008 Certificates in a Long-Term Mode, the 15th day (whether or not a Business Day) of the month next preceding each Interest Payment Date.

“Reimbursement Agreement” means any reimbursement agreement, credit agreement, line of credit agreement, standby purchase agreement or other agreement, between a Credit Enhancement Provider or a Liquidity Facility Provider, as applicable, and the Authority and/or

the City, as the same may be amended from time to time pursuant to its terms, including the Reimbursement Agreement, dated as of July 1, 2011, by and between the City and the Bank.

“Remarketing Agent” means each Person selected by the Authority to act as remarketing agent for the 2008 Certificates pursuant to Section 3.12 hereof and approved by the 2008 Certificate Insurer (or, if a Control Event has occurred, the Bank).

“Remarketing Agreement” means an agreement approved by the 2008 Certificate Insurer, providing for the remarketing of the 2008 Certificates tendered for purchase, as the same may be amended from time to time pursuant to its terms.

“Remarketing Proceeds Account” means an Eligible Account by that name established within the 2008 Purchase Fund pursuant to Section 3.09(a) hereof and held in the name of the Trustee for the benefit of the Owners.

“Replacement Liquidity Facility” means the irrevocable, direct-pay letter of credit issued by the Bank with respect to the 2008 Certificates on the Substitution Date.

“Required Stated Amount” means, (i) in the case of each Liquidity Facility, at any time of calculation with respect to the 2008 Certificates, an amount equal to the aggregate principal amount of the 2008 Certificates then Outstanding together with interest accruing thereon (assuming an annual rate of interest equal to the Maximum Rate) for the minimum period specified by the Rating Agencies then rating the 2008 Certificates, as necessary to maintain the short-term rating of the 2008 Certificates, or (ii) in the case of each Credit Enhancement (other than a Credit Enhancement in the form of an insurance policy), at any time of calculation with respect to the 2008 Certificates, an amount equal to the aggregate principal amount of the 2008 Certificates then Outstanding together with interest accruing thereon (assuming an annual rate of interest equal to the Maximum Rate) for the minimum period specified by the Rating Agencies then rating the 2008 Certificates, as necessary to maintain the short-term rating (or, if no short term rating is then in effect, the rating) of the 2008 Certificates.

“Representation Letter” means the letter of representation to The Depository Trust Company, New York, New York, from the Authority.

“Reserve Funding Instruments” shall have the meaning given to such term in Section 4.04 hereof, including the 2008 Parity Reserve Fund Insurance Policy.

“Reserve Fund Requirement” shall have the meaning ascribed thereto in the Contract.

“S&P” means Standard & Poor’s Ratings Services, a division of The McGraw Hill Company, and its successors or assigns, except that if such entity shall be dissolved or liquidated or shall no longer perform the services of a municipal securities rating agency, then “S&P” shall be deemed to refer to any other nationally recognized municipal securities rating agency selected by the Authority.

“Securities Depositories” means: The Depository Trust Company, 55 Water Street, 50<sup>th</sup> Floor, New York, New York 10041-0099, Attention: Call Notification Department, Fax: (212) 855-7232; or, in accordance with then-current guidelines of the Securities and Exchange

Commission, such other securities depositaries as the Authority may designate in a Certificate of the Authority to the Trustee.

“Serial Certificate” means any 2008 Certificate not subject to mandatory prepayment from Sinking Fund Payments.

“Short-Term Mode” means the Daily Mode, the Weekly Mode or the Flexible Mode.

“Sinking Fund Payments” means the payments required under Section 2.03(a) hereof to be deposited in the 2008 Sinking Fund Subaccount under Section 4.03(b) hereof.

“Special Counsel” means any firm of nationally recognized municipal bond attorneys selected by the Authority and experienced in the issuance of municipal bonds and matters relating to the exclusion of the interest thereon from gross income for federal income tax purposes.

“State” means the State of California.

“Subrogated Certificate” means any Certificate of Participation with respect to which, pursuant to Section 10.05 of the Trust Agreement, the Bank or other credit enhancement provider, to the extent it has paid the principal of such Certificate of Participation from a drawing under the Replacement Liquidity Facility or other credit enhancement, has become subrogated to, and the assignee of, the rights to receive payment of such principal from the City pursuant to the Trust Agreement and has become the Owner of such Certificate of Participation.

“Substitution Date” means the date on which an Alternate Liquidity Facility is substituted for the Liquidity Facility then in effect.

“Supplemental Contract” shall have the meaning given such term in the Contract.

“Supplemental Trust Agreement” means any trust agreement then in full force and effect which has been duly executed and delivered by the Authority and the Trustee amendatory hereof or supplemental hereto; but only if and to the extent that such Supplemental Trust Agreement is specifically authorized hereunder.

“Tax Certificate” means, collectively, the Tax Certificate concerning certain matters pertaining to the use and investment of proceeds of the 2008 Certificates, executed and delivered by the City on the date of delivery of the 2008 Certificates, including any and all exhibits attached thereto.

“Tender Notice Deadline” means: (i) during the Daily Mode, 11:00 a.m. New York City time on any Business Day; and (ii) during the Weekly Mode, 5:00 p.m. New York City time on the Business Day 7 days prior to the applicable Purchase Date.

“Tender Notice” means a notice delivered by Electronic means or in writing that states: (i) the principal amount of the 2008 Certificates to be purchased pursuant to Section 3.01 hereof; (ii) the Purchase Date on which such 2008 Certificates are to be purchased; (iii) applicable

payment instructions with respect to such 2008 Certificates being tendered for purchase; and (iv) an irrevocable demand for such purchase.

“Term Certificates” means the 2008 Certificates subject to mandatory prepayment from Sinking Fund Payments.

“Term Rate” means the per annum interest rate for the 2008 Certificates in the Term Rate Mode determined pursuant to Section 2.16(a) hereof.

“Term Rate Mode” means the Mode during which the 2008 Certificates evidence interest at a Term Rate.

“Term Rate Period” means the period from (and including) the Mode Change Date or the date of initial conversion of the 2008 Certificates to a Term Rate Mode, as applicable, to (but excluding) the last day of the first period that 2008 Certificates shall be in the Term Rate Mode as established by the Authority pursuant to Section 2.16(a) hereof and, thereafter, the period from (and including) the beginning date of each successive Interest Rate Period selected for the 2008 Certificates by the Authority pursuant to Section 2.16(a) hereof while the 2008 Certificates are in the Term Rate Mode to (but excluding) the commencement date of the next succeeding Interest Period, including another Term Rate Period. Except as otherwise provided in this Trust Agreement, an Interest Period for the 2008 Certificates in the Term Rate Mode must be at least 180 days in length.

“Trust Agreement” means this Trust Agreement, dated as of May 1, 2008, between the Authority and the Trustee, as originally executed and as it may from time to time be amended or supplemented by all Supplemental Trust Agreements executed pursuant to the provisions hereof.

“Trustee” means The Bank of New York Mellon Trust Company, N.A., or any other association or corporation which may at any time be substituted in its place as provided in Section 6.01 hereof.

“2006 Certificates” means the Water Revenue Certificates of Participation 2006 Series A.

“2006 Supplemental Contract” means the 2006 Supplemental Installment Purchase Contract, dated as of November 1, 2006, by and between the City and the Authority, and consented to by the Trustee and Financial Guaranty Insurance Company.

“2006 Trust Agreement” means that certain Trust Agreement, dated as of November 1, 2006, by and between the Authority and the Trustee, delivered in connection with the 2006 Certificates.

“2008 Certificate Insurance Policy” means the financial guaranty insurance policy issued by the 2008 Certificate Insurer guaranteeing the scheduled payment of principal of and interest evidenced and represented by the 2008 Certificates.

“2008 Certificate Insurer” means Assured Guaranty Corp., its successors and assigns.

“2008 Certificates” means all of the Water Refunding Revenue Certificates of Participation, 2008 Series A, evidencing and representing proportionate interests of the owners thereof in the 2008 Payments to be made by the City, and executed and delivered in accordance with Article II hereof.

“2008 Debt Service Fund” means the fund by that name established pursuant to Section 4.02 hereof.

“2008 Interest Account” means the account by that name established within the 2008 Debt Service Fund pursuant to Section 4.03(a) hereof.

“2008 Interest Rate Swap Agreement” has the meaning given such term in the 2008 Supplemental Contract.

“2008 Parity Reserve Fund Insurance Policy” means the reserve fund financial guaranty insurance policy issued by the 2008 Certificate Insurer and deposited in the Parity Reserve Fund pursuant to Section 2.12 hereof.

“2008 Payments” means the installment payments of interest, principal, and prepayment premium, if any, payable by the City under and pursuant to the 2008 Supplemental Contract.

“2008 Prepayment Subaccount” means the subaccount by that name established within the 2008 Principal Account of the 2008 Debt Service Fund pursuant to Section 4.03(b) hereof.

“2008 Principal Account” means the account by that name established within the 2008 Debt Service Fund pursuant to Section 4.03(b) hereof.

“2008 Project” means the refinancing of improvements to the Water Utility System described in Exhibit A to the 2008 Supplemental Contract.

“2008 Purchase Fund” means the fund by that name established pursuant to Section 3.09 hereof.

“2008 Liquidity Facility Payment Account” means the account by that name established pursuant to Section 4.08 hereof.

“2008 Sinking Fund Subaccount” means the subaccount by that name within the 2008 Principal Account of the 2008 Debt Service Fund established pursuant to Section 4.03(b) hereof.

“2008 Supplemental Contract” means that certain 2008 Supplemental Installment Purchase Contract, dated as of May 1, 2008, by and between the City and the Authority, supplementing the Master Contract.

“Weekly Mode” means the Mode during which the 2008 Certificates evidence interest at the Weekly Rate.

“Weekly Rate” means the per annum interest rate with respect to the 2008 Certificates in the Weekly Mode determined pursuant to Section 2.15(b) hereof.

“Weekly Rate Period” means the period during which the 2008 Certificates evidence interest at a Weekly Rate, which shall be the period commencing on Thursday of each week to and including Wednesday of the following week, except the first Weekly Rate Period which shall be from the Mode Change Date for the 2008 Certificates to and including the Wednesday of the following week and the last Weekly Rate Period which shall be from and including the Thursday of the week prior to the Mode Change Date to and including the day next preceding the Mode Change Date.

“Written Request of the Authority” means an instrument in writing signed by the Auditor and Treasurer of the Authority or by any other officer of the Authority duly authorized by the Authority for that purpose.

Section 1.02. Equal Security. In consideration of the acceptance of the 2008 Certificates by the Owners thereof, this Trust Agreement shall be deemed to be and shall constitute a contract between the Authority and the Owners from time to time of all 2008 Certificates authorized, executed, and delivered hereunder and then Outstanding to secure the full and final payment of the interest, principal, and prepayment premiums, if any, evidenced and represented by the 2008 Certificates which may from time to time be authorized, executed, issued and delivered hereunder, subject to the agreements, conditions, covenants and provisions contained herein; and all agreements and covenants set forth herein to be performed by or on behalf of the Trustee shall be for the equal and proportionate benefit, protection and security of all Owners without distinction, preference or priority as to security or otherwise of any 2008 Certificates over any other 2008 Certificates by reason of the number or date thereof or the time of authorization, sale, execution, or delivery thereof or for any cause whatsoever, except as expressly provided herein or therein.

Section 1.03. New York City Time. All references herein to a particular time of day shall be New York City time unless the context clearly otherwise requires.

## ARTICLE II

### THE 2008 CERTIFICATES

Section 2.01. Conditions and Terms of 2008 Certificates. The Trustee is hereby authorized and directed to execute and deliver the 2008 Certificates in the aggregate principal amount of \$47,625,000, aggregating the principal installments of the 2008 Payments, and each evidencing and representing a proportionate interest in the 2008 Payments.

Section 2.02. Terms of the 2008 Certificates.

(a) The 2008 Certificates shall be issued as fully registered securities certificates without coupons in Authorized Denominations. The 2008 Certificates shall be registered initially in the name of “Cede & Co.,” as nominee of DTC, the initial Securities Depository, and shall be evidenced by one certificate in the total aggregate principal amount of the 2008 Certificates. Registered ownership of the 2008 Certificates, or any portion thereof, may not thereafter be transferred except as set forth in Section 2.06 hereof.

(b) The 2008 Certificates shall be dated the Delivery Date.

(c) Except as otherwise provided in the Liquidity Facility or the Reimbursement Agreement, or, in the case of 2008 Certificates being converted to a Fixed Rate, except as otherwise provided in Section 2.18(d) hereof, the 2008 Certificates shall mature on October 1, 2036.

(d) The 2008 Certificates shall be subject to prepayment as provided in Section 2.03 hereof and optional and mandatory tender for purchase as provided in Article III.

(e) The Trustee shall identify all payments (whether made by check or by wire transfer) of interest, principal, Purchase Price and Prepayment Price by CUSIP number of the 2008 Certificates.

(f) During each Interest Period for each Mode, the interest rate or rates with respect to the 2008 Certificates shall be determined in accordance with this Article II and shall be payable on the applicable Interest Payment Date for such Interest Period; provided that the interest rate or rates shall not exceed the Maximum Rate. All 2008 Certificates shall evidence interest in the same Mode, but need not evidence interest at the same rate at any one time. Interest with respect to the 2008 Certificates accruing at the Daily Rate, Weekly Rate or Flexible Rate shall be computed upon the basis of a 365- or 366-day year, as applicable, for the actual number of days elapsed. Interest with respect to the 2008 Certificates accruing at a Fixed Rate or a Term Rate shall be computed upon the basis of a 360-day year, consisting of twelve 30-day months. Each 2008 Certificate shall evidence interest on overdue principal and, to the extent permitted by law, on overdue interest at the rate evidenced by such 2008 Certificate on the date on which such principal became due and payable. Notwithstanding the foregoing, the interest rate and payment terms of Liquidity Provider Certificates shall be governed by the provisions of the Liquidity Facility or related Reimbursement Agreement, as applicable.

(g) Interest evidenced by each 2008 Certificate shall accrue from and including the Interest Accrual Date immediately preceding the date of authentication thereof, or, if such date of authentication shall be an Interest Accrual Date, from such Interest Accrual Date or if such date of authentication shall be prior to the second Interest Accrual Date, from the Delivery Date; provided, however, that if interest evidenced by the 2008 Certificates shall be in default, interest on the 2008 Certificates issued in exchange for 2008 Certificates surrendered for registration of transfer or exchange shall accrue from the date to which interest has been paid in full with respect to the 2008 Certificates or, if no interest has been paid with respect to the 2008 Certificates, from the Delivery Date.

(h) Payment of interest evidenced by the 2008 Certificates shall be made to the person appearing on the registration books of the Trustee as the Owner thereof as of the close of business on the applicable Record Date, such interest to be payable on each Interest Payment Date by the Trustee (i) by check mailed on such Interest Payment Date to such Owner's address as it appears on the registration books of the Trustee at the close of business on the Record Date or (ii) by wire transfer to any Owner of at least \$1,000,000 aggregate principal amount of 2008 Certificates or the Liquidity Facility Provider (in the case of Liquidity Provider Certificates) according to the written instructions provided by such Owner or the Liquidity Provider, as the case may be, on or prior to the applicable Record Date to the Trustee, which written instructions

shall remain in effect until revised by such Owner or Liquidity Facility Provider, as the case may be, by an instrument in writing delivered to the Trustee.

(i) If for any reason, the Liquidity Provider Certificates remain in book-entry and are not assigned a separate CUSIP number, the Trustee shall pay the principal of, prepayment premium, if any, and interest with respect to the 2008 Certificates (including the Liquidity Provider Certificates) in accordance with the letter of representations with DTC computed at the Basic Certificate Rate; and the Authority shall pay to the Trustee for payment to the Liquidity Facility provider outside the book-entry system the remainder of (i) the interest then due with respect to Liquidity Provider Certificates computed at the applicable interest rate minus (ii) the interest that would then be due with respect to Liquidity Provider Certificates if such interest were computed at the Basic Certificate Rate.

(j) The principal evidenced and represented by the 2008 Certificates other than Liquidity Provider Certificates shall be payable in lawful money of the United States of America upon the surrender thereof on the respective 2008 Certificate Payment Date or on prepayment prior thereto at the Corporate Trust Office of the Trustee. The principal evidenced and represented by Liquidity Provider Certificates shall be payable in lawful money of the United States of America by wire transfer to the Liquidity Facility Provider according to the written instructions provided by the Liquidity Provider on or prior to the applicable 2008 Certificate Payment Date to the Trustee, which written instructions shall remain in effect until revised by the Liquidity Facility Provider by an instrument in writing delivered to the Trustee.

(k) The first Mode for the 2008 Certificates shall be the Weekly Mode. The first Weekly Rate Period for the 2008 Certificates shall be the period commencing on and including the Delivery Date and ending on and including June 4, 2008. The First Interest Payment Date is June 2, 2008. The Mode for the 2008 Certificates may be changed in accordance with this Article II.

(l) In the absence of manifest error, the determination of any Daily Rate, Weekly Rate, Flexible Rate, Term Rate and Fixed Rate by the Remarketing Agent, the determination of each Flexible Rate Period for any 2008 Certificate in a Flexible Mode by the Remarketing Agent and the determination of the length of each Term Rate Period by the Authority shall be conclusive and binding upon the Authority, the other Notice Parties and each Owner.

(m) In the absence of manifest error, the record of interest rates maintained by the Trustee shall be conclusive and binding upon the Authority, the other Notice Parties and each Owner.

#### Section 2.03. Prepayment of Certificates.

(a) Mandatory Sinking Fund Prepayment. Except in the event of serialization of the 2008 Certificates in accordance with Section 2.18(d) hereof, the 2008 Certificates are subject to mandatory prepayment from Sinking Fund Payments prior to their Maturity Date, in part by lot, on October 1 of each year on and after October 1, 2008, in accordance with the schedule set forth below upon notice as hereinafter provided, from and in the amount of the principal installment of the 2008 Payments due and payable on such dates, at a prepayment price equal to the sum of the

principal amount evidenced and represented thereby plus accrued and unpaid interest evidenced and represented thereby to the Prepayment Date, without a prepayment premium.

Certificates Sinking Fund Payments

Mandatory Sinking Fund Payment Date (October 1)	Sinking Fund Payment	Mandatory Sinking Fund Payment Date (October 1)	Sinking Fund Payment
2008	\$290,000	2023	\$2,300,000
2009	285,000	2024	2,410,000
2010	285,000	2025	2,515,000
2011	285,000	2026	2,595,000
2012	310,000	2027	2,705,000
2013	310,000	2028	2,810,000
2014	340,000	2029	2,945,000
2015	340,000	2030	3,055,000
2016	365,000	2031	3,185,000
2017	365,000	2032	3,295,000
2018	395,000	2033	3,430,000
2019	395,000	2034	3,570,000
2020	395,000	2035	3,705,000
2021	425,000	2036	3,870,000
2022	450,000		

Notwithstanding the foregoing, no 2008 Certificate (other than a Liquidity Provider Certificate) shall be optionally prepaid while any Liquidity Provider Certificate is Outstanding unless all Outstanding Liquidity Provider Certificates are prepaid or purchased by the Trustee and cancelled concurrently with such prepayment or purchase.

If for any reason, the Liquidity Provider Certificates remain in book-entry but have not been assigned a separate CUSIP number, the Trustee shall apply the amounts in the 2008 Sinking Fund Subaccount set aside for prepayment to the purchase from the Liquidity Facility provider of Liquidity Provider Certificates in an aggregate principal amount not in excess of the principal amount intended to be prepaid at a purchase price equal to the prepayment price specified above. The Liquidity Provider Certificates so purchased shall be cancelled by the Trustee, and the principal amount thereof shall be credited against the principal amount of the 2008 Certificates otherwise required to be prepaid.

Notwithstanding the foregoing, if any such 2008 Certificates have been optionally prepaid pursuant to Section 2.03(c) hereof, the amounts of such Sinking Fund Payments shall be reduced as directed by the Authority, or if not so directed, proportionately in increments of Authorized Denominations by the principal amount evidenced and represented by all such 2008 Certificates so optionally prepaid.

All such Sinking Fund Payments shall be deposited in the 2008 Sinking Fund Subaccount of the 2008 Principal Account established pursuant to Section 4.03 hereof. On each Sinking

Fund Payment date, the Trustee shall apply the Sinking Fund Payment required on such date to the mandatory prepayment or payment of Term Certificates, upon the notice and in the manner provided in this Section 2.03(a) hereof; provided that, at any time prior to giving notice of such prepayment, the Trustee may apply moneys in the 2008 Sinking Fund Subaccount to the purchase of Term Certificates at public or private sale, as and when and at such prices (including brokerage and other charges) as directed in writing by the Authority, except that the purchase price shall not exceed the prepayment price that would be payable for Term Certificates upon prepayment by application of such Sinking Fund Payment. If, during the 12-month period immediately preceding said Sinking Fund Payment date, the Trustee has purchased Term Certificates with moneys in the 2008 Sinking Fund Subaccount, or, during said period and prior to giving said notice of prepayment, the City or the Authority has deposited Term Certificates with the Trustee (together with a request of the Authority or the City to apply such 2008 Certificates so deposited to the Sinking Fund Payment due on said Sinking Fund Payment date), or Term Certificates were at any time purchased or prepaid by the Trustee from the 2006 Prepayment Account and allocable to said Sinking Fund Payment, such 2008 Certificates so purchased, deposited, or prepaid shall be applied, to the extent of the full principal amount evidenced and represented thereby, to reduce said Sinking Fund Payment.

(b) Mandatory Prepayment of Liquidity Provider Certificates. Any Liquidity Provider Certificates from time to time Outstanding shall be subject to mandatory prepayment in the amounts and at the times and at the prepayment prices specified therefor in the Liquidity Facility with the Liquidity Facility Provider applicable thereto.

(c) Optional Prepayment.

(i) Each 2008 Certificate in a Daily Mode or a Weekly Mode shall be subject to prepayment at the option of the Authority, in whole or in part, in Authorized Denominations on any Business Day, at a prepayment price equal to 100% of the principal amount thereof, plus, accrued interest, if any, to the Prepayment Date, without premium.

(ii) Flexible Rate Certificates are not subject to optional prepayment prior to their respective Mandatory Purchase Dates. Flexible Rate Certificates shall be subject to prepayment at the option of the Authority in whole or in part on their respective Mandatory Purchase Dates at a prepayment price equal to 100% of the principal amount thereof, without premium.

(iii) Each 2008 Certificate in a Term Rate Mode shall be subject to prepayment at the option of the Authority, in whole or in part, on each Mandatory Purchase Date applicable to the 2008 Certificates in a Term Rate Mode, at a prepayment price equal to 100% of the principal amount thereof, without premium.

(iv) Each Certificate in a Term Rate Mode or a Fixed Rate Mode is subject to prepayment in whole or in part on any date (and if in part, in such order of maturity as the Authority shall specify and within a maturity by lot or by such other method as the Trustee determines to be fair and reasonable and in Authorized Denominations) commencing on the Interest Payment Date next following the tenth anniversary of the

change to a Term Rate Mode or a Fixed Mode at a prepayment price equal to 100% of the principal amount of 2008 Certificates being prepaid, together with accrued interest, if any, to the Prepayment Date, without premium. If the length of the Term Rate Period or the Fixed Rate Period for the 2008 Certificates is less than ten (10) years, then the 2008 Certificates shall not be subject to optional prepayment during the Term Rate Period or Fixed Rate Period, as applicable.

(v) In connection with a change to a Term Rate Mode or a Fixed Rate Mode for the 2008 Certificates, the Authority may waive or otherwise alter its rights to direct the prepayment of the 2008 Certificates set forth in (c)(iv) above; provided that notice describing such waiver or alteration shall be submitted to the Trustee and the Remarketing Agent, or Fixed Rate Remarketing Agent, as applicable, together with a Favorable Opinion of Special Counsel.

(d) Reserved.

(e) Selection of 2008 Certificates. If less than all of the Outstanding 2008 Certificates are to be prepaid at any one time, the Authority shall designate the Certificate Payment Dates or portions thereof of the 2008 Certificates to be prepaid; provided, that any Liquidity Provider Certificates that remain outstanding shall be selected for prepayment prior to 2008 Certificates that are not Liquidity Provider Certificates. If less than all Outstanding 2008 Certificates of any particular Certificate Payment Date are to be prepaid at any one time, the Trustee shall select the 2008 Certificates of such Certificate Payment Date to be prepaid by lot, except that if any 2008 Certificate or portion thereof to be prepaid is a Term Certificate, the Authority may specify in a Written Request of the Authority filed with the Trustee, the particular Sinking Fund Payments for such Term Certificate to be prepaid. For purposes of such selection, 2008 Certificates of each Certificate Payment Date shall be deemed to be composed of Authorized Denominations and any such Authorized Denomination may be separately prepaid. If the Authority elects to optionally prepay 2008 Certificates pursuant to Section 2.03(c) hereof, it will notify the Trustee of the prepayment date and the principal amount evidenced and represented by the 2008 Certificates of each Certificate Payment Date to be prepaid on such prepayment date at least 45 days prior to such prepayment date; provided, that the Trustee may, at its option, waive any such notice or accept any notice received at a later date.

(f) Notice of Prepayment. Notice of prepayment shall be mailed by the Trustee, not less than 30 nor more than 60 days prior to the prepayment date to (i) the respective Owners of the 2008 Certificates designated for prepayment at their addresses appearing on the registration books of the Trustee, (ii) the Securities Depositories and (iii) one or more Information Services. Notice of prepayment to the Securities Depositories and the Information Services shall be given by first-class mail, certified mail, overnight delivery or facsimile transmission or by other approved means. Each notice of prepayment shall state the date of such notice, the prepayment price, the place of prepayment (including the name and appropriate address of the Trustee), the CUSIP number (if any) of the 2008 Certificates to be prepaid, and, if less than all of the 2008 Certificates maturing on any one Certificate Payment Date are to be prepaid, the distinctive certificate numbers of the 2008 Certificates of such Certificate Payment Date to be prepaid and, in the case of 2008 Certificates to be prepaid in part only, the respective portions of the principal amount evidenced and represented thereby to be prepaid. Each such notice shall also state that

on said date there will become due and payable on each of said 2008 Certificates the prepayment price thereof and in the case of a 2008 Certificate to be prepaid in part only, the specified portion of the principal amount evidenced and represented thereby to be prepaid, together with accrued and unpaid interest evidenced and represented thereby to the prepayment date, and that from and after such prepayment date interest evidenced and represented thereby shall cease to accrue, and shall require that such 2008 Certificates be then surrendered at the address of the Trustee specified in the prepayment notice. Failure to receive such notice shall not invalidate any of the proceedings taken in connection with such prepayment.

Any prepayment may be cancelled if the notice of such prepayment has not been mailed to the respective Owners of the 2008 Certificates or if such notice expressly conditioned the prepayment upon the occurrence of one or more events. Notice of any such cancellation shall be given in the same manner as the notice of prepayment was given at least 3 Business Days prior to the date scheduled for prepayment.

If notice of prepayment has been duly given as aforesaid and money for the payment of the prepayment price of the 2008 Certificates called for prepayment is held by the Trustee, then on the prepayment date designated in such notice, 2008 Certificates so called for prepayment shall become due and payable, and from and after the date so designated interest evidenced and represented by such 2008 Certificates shall cease to accrue, and the Owners of such 2008 Certificates shall have no rights in respect thereof except to receive payment of the prepayment price thereof.

All 2008 Certificates prepaid pursuant to the provisions of this Section shall be cancelled and destroyed by the Trustee and shall not be redelivered.

(g) No Notice of Prepayment. Notwithstanding any other provision of this Trust Agreement to the contrary, no notice of prepayment is required to be given with respect to any prepayment occurring on a Mandatory Purchase Date or prepayment of Liquidity Provider Certificates.

(h) Mandatory Purchase in Lieu of Prepayment. Each Owner, by purchase and acceptance of any 2008 Certificate irrevocably grants to the Authority the option to purchase such 2008 Certificate on any date such 2008 Certificate is subject to optional prepayment provided in (c) above at a purchase price equal to the prepayment price then applicable to such 2008 Certificate, plus accrued interest thereon to the date of purchase. In order to exercise such option, the Authority shall deliver to the Trustee a Favorable Opinion of Special Counsel and shall direct the Trustee to provide notice of mandatory purchase in lieu of prepayment, such notice to be provided, as and to the extent applicable, in accordance with the provisions set forth in Section 3.02 hereof. On the date fixed for purchase of any 2008 Certificate pursuant to this Section 2.03(h), the Authority shall pay the purchase price of such 2008 Certificate to the Trustee in immediately available funds and the Trustee shall pay the same to the Owners of the 2008 Certificates being purchased against delivery thereof. All 2008 Certificates so purchased shall be delivered to the Trustee to hold for the benefit of the Authority or for cancellation upon the receipt of such instructions from the Authority. Without the prior written consent of the 2008 Certificate Insurer, no 2008 Certificates shall be purchased in lieu of prepayment by the

Authority, the City or any of its affiliates unless such 2008 Certificates are redeemed, defeased or cancelled.

Notwithstanding any other provision of this Trust Agreement, the purchase price of any 2008 Certificate subject to mandatory purchase in lieu of prepayment pursuant to this Section 2.03(h) shall be paid solely by the Authority and such 2008 Certificate shall not be eligible to be purchased and shall not be purchased from a drawing on any Liquidity Facility. In the event that the Authority lacks sufficient funds to pay the purchase price of any 2008 Certificate subject to mandatory purchase in lieu of prepayment pursuant to this Section 2.03(h) on the date fixed for such purchase, the Authority shall cancel such mandatory purchase in lieu of prepayment and shall return each such 2008 Certificate to the Owner who shall have tendered such 2008 Certificate for mandatory purchase in lieu of prepayment pursuant to this Section 2.03(h). The Trustee shall give notice that such mandatory purchase was not effected promptly following the date fixed for such purchase. Any failure to pay the purchase price of any 2008 Certificate subject to mandatory purchase pursuant to this Section 2.03(h) shall not constitute an Event of Default under this Trust Agreement.

Section 2.04. Form of 2008 Certificates. The 2008 Certificates while in Weekly Mode shall be substantially in the form set forth in Exhibit A hereto attached and by this reference herein incorporated. Upon a change in Mode of the 2008 Certificates to another Mode, and upon any subsequent change from one Mode to another Mode, a new form of 2008 Certificate shall be prepared, if and to the extent necessary, which contains the terms of the 2008 Certificates applicable in the new Mode.

Section 2.05. Execution of 2008 Certificates. The 2008 Certificates shall be executed by the Trustee by the manual signature of an authorized officer or signatory of the Trustee.

Section 2.06. Transfer and Payment of 2008 Certificates. Any 2008 Certificates may, in accordance with its terms, be transferred in the books required to be kept pursuant to the provisions of Section 2.08 hereof by the person in whose name it is registered, in person or by his duly authorized attorney, upon surrender of such 2008 Certificates at the Corporate Trust Office of the Trustee for cancellation accompanied by delivery of a duly executed written instrument of transfer in a form acceptable to the Trustee. Whenever any 2008 Certificate or 2008 Certificates shall be surrendered for transfer, the Trustee shall execute and deliver to the transferee a new 2008 Certificate or 2008 Certificates of the same Certificate Payment Date evidencing and representing a like aggregate principal amount in Authorized Denominations. The Trustee shall require the payment by the Owner requesting such transfer of any tax or other governmental charge required to be paid with respect to such transfer as a condition precedent to the exercise of such privilege.

The Trustee may deem and treat the registered owner of any 2008 Certificates as the absolute owner of such 2008 Certificates for the purpose of receiving payment thereof and for all other purposes, whether such 2008 Certificates shall be overdue or not, and the Trustee shall not be affected by any notice or knowledge to the contrary; and payment of the interest and principal and prepayment premium, if any, evidenced and represented by such 2008 Certificates shall be made only to such registered owner, which payments shall be valid and effectual to satisfy and discharge liability on such 2008 Certificates to the extent of the sum or sums so paid.

Except with respect to tenders pursuant to Sections 3.01 and 3.02 herein, the Trustee shall not be required to register the transfer of any 2008 Certificate during the period commencing on the date 15 days preceding the selection of 2008 Certificates for prepayment and ending on the date of mailing of notice of such prepayment, or any 2008 Certificate which has been selected for prepayment in whole or in part, from and after the day of mailing of a notice of prepayment of such 2008 Certificates selected for prepayment in whole or in part as provided in Section 2.03 hereof.

Section 2.07. Exchange of Certificates. 2008 Certificates may be exchanged at the Corporate Trust Office of the Trustee for 2008 Certificates evidencing and representing a like aggregate principal amount of 2008 Certificates of the same Certificate Payment Date of other Authorized Denominations. The Trustee shall require the payment by the Owner requesting such exchange of any tax or other governmental charge required to be paid with respect to such exchange as a condition precedent to the exercise of such privilege.

Except with respect to tenders pursuant to Sections 3.01 and 3.02 herein, the Trustee shall not be required to exchange any 2008 Certificate during the 15-day period preceding the selection of 2008 Certificates for prepayment, or any 2008 Certificate which has been selected for prepayment in whole or in part, from and after the day of mailing of a notice of prepayment of such 2008 Certificates selected for prepayment in whole or in part as provided in Section 2.03 hereof.

Section 2.08. Certificate Registration Books. The Trustee will keep at its Corporate Trust Office sufficient books for the registration and transfer of the 2008 Certificates which shall at all times be open to inspection by the Authority during regular business hours with reasonable prior notice, and upon presentation for such purpose the Trustee shall, under such reasonable regulations as it may prescribe, register or transfer the 2008 Certificates in such books as hereinabove provided.

Section 2.09. Mutilated, Destroyed, Stolen or Lost Certificates. If any 2008 Certificate shall become mutilated the Trustee, at the expense of the Owner, shall thereupon execute and deliver a new 2008 Certificate of like tenor and amount in exchange and substitution for the 2008 Certificate so mutilated, but only upon surrender to the Trustee of the 2008 Certificate so mutilated. Every mutilated 2008 Certificate so surrendered to the Trustee shall be cancelled and destroyed.

If any 2008 Certificate shall be lost, destroyed or stolen, evidence of such loss, destruction or theft may be submitted to the Trustee and, if such evidence is satisfactory to the Trustee and indemnity satisfactory to the Trustee has been given, the Trustee, at the expense of the Owner, shall thereupon execute and deliver a new 2008 Certificate of like tenor in lieu of and in substitution for the 2008 Certificate so lost, destroyed or stolen.

The Trustee may require payment of a reasonable sum for each new 2008 Certificate delivered under this Section 2.09 and of the expenses which may be incurred by the Authority and the Trustee in the premises. Any 2008 Certificate executed and delivered under the provisions of this Section in lieu of any 2008 Certificate alleged to be lost, destroyed or stolen shall be equally and proportionately entitled to the benefits of this Trust Agreement with all other

2008 Certificates secured by this Trust Agreement. The Trustee shall not be required to treat both the original 2008 Certificate and any replacement 2008 Certificate as being Outstanding for the purpose of determining the principal amount of 2008 Certificates which may be executed and delivered hereunder or for the purpose of determining any percentage of 2008 Certificates Outstanding hereunder, but both the original and replacement 2008 Certificate shall be treated as one and the same.

Section 2.10. Temporary Certificates. The 2008 Certificates executed and delivered under this Trust Agreement may be initially executed and delivered in temporary form exchangeable for definitive 2008 Certificates when ready for delivery. The temporary 2008 Certificates may be printed, lithographed or typewritten, shall be of such denominations as may be determined by the Trustee, shall be in fully registered form and may contain such reference to any of the provisions of this Trust Agreement as may be appropriate. Every temporary 2008 Certificate shall be executed and delivered by the Trustee, upon the same conditions and terms and in substantially the same manner as definitive 2008 Certificates. If the Trustee executes and delivers temporary 2008 Certificates it will execute and furnish definitive 2008 Certificates and thereupon the temporary 2008 Certificates may be surrendered, for cancellation, in exchange therefor at the Corporate Trust Office of the Trustee, and the Trustee shall deliver in exchange for such temporary 2008 Certificates definitive 2008 Certificates evidencing and representing an equal aggregate principal amount of 2008 Certificates of Authorized Denominations. Until so exchanged, the temporary 2008 Certificates shall be entitled to the same benefits under this Trust Agreement as definitive 2008 Certificates delivered hereunder.

Section 2.11. Use of Book-Entry System for Certificates.

(a) The 2008 Certificates initially shall be delivered in the form of a single executed fully registered securities certificate for each stated Maturity Date of such 2008 Certificates, representing the aggregate principal amount evidenced and represented by the 2008 Certificates of such Maturity Date. Upon initial delivery, the ownership of all such 2008 Certificates shall be registered in the registration records maintained by the Trustee pursuant to Section 2.08 hereof in the name of Cede & Co., as nominee of DTC, or such other nominee as DTC shall request pursuant to the Representation Letter. The Trustee may treat DTC (or its nominee) as the sole and exclusive owner of the 2008 Certificates registered in its name for the purposes of payment of the principal or prepayment price and interest evidenced and represented by such 2008 Certificates, selecting the 2008 Certificates or portions thereof to be prepaid, giving any notice permitted or required to be given to Owners hereunder, registering the transfer of 2008 Certificates, obtaining any consent or other action to be taken by Owners of the 2008 Certificates and for all other purposes whatsoever; and the Trustee shall not be affected by any notice to the contrary. Neither the Trustee nor the Authority shall have any responsibility or obligation to any Participant (which shall mean, for purposes of this Section, securities brokers and dealers, banks, trust companies, clearing corporations and other entities, some of whom directly or indirectly own DTC), any person claiming a beneficial ownership interest in the 2008 Certificates under or through DTC or any Participant, or any other person which is not shown on the registration records as being an Owner of 2008 Certificates, with respect to (i) the accuracy of any records maintained by DTC or any Participant, (ii) the payment by DTC or any Participant of any amount in respect of the principal or prepayment price or interest evidenced and represented by the 2008 Certificates (iii) any notice which is permitted or required to be given to Owners of

2008 Certificates hereunder, (iv) the selection by DTC or any Participant of any person to receive payment in the event of a partial prepayment of the 2008 Certificates, or (v) any consent given or other action taken by DTC as Owner of 2008 Certificates. Notwithstanding anything to the contrary herein, the Trustee shall pay all principal, prepayment premium, if any, and interest evidenced and represented by the 2008 Certificates only at the times, to the accounts, at the addresses and otherwise in accordance with the Representation Letter, and all such payments shall be valid and effective to satisfy fully and discharge the principal, prepayment premium, if any, and interest evidenced and represented by the 2008 Certificates to the extent of the sum or sums so paid. Upon delivery by DTC to the Trustee of written notice to the effect that DTC has determined to substitute a new nominee in place of its then existing nominee, the 2008 Certificates will be transferable to such new nominee in accordance with subsection (c) of this Section.

(b) In the event that the Authority determines that it is in the best interests of the beneficial owners of the 2008 Certificates that they be able to obtain securities certificates, the Trustee shall, upon the written instruction of the Authority, so notify DTC, whereupon DTC shall notify the Participants of the availability through DTC of securities certificates. In such event, the 2008 Certificates will be transferable in accordance with subsection (c) of this Section. DTC may determine to discontinue providing its services with respect to the 2008 Certificates at any time by giving written notice of such discontinuance to the Authority and the Trustee and discharging its responsibilities with respect thereto under applicable law. In such event, the 2008 Certificates will be transferable in accordance with subsection (c) of this Section. Whenever DTC requests the Authority and the Trustee to do so, the Trustee and the Authority will cooperate with DTC in taking appropriate action after reasonable notice to arrange for another securities depository to maintain custody of all certificates evidencing the 2008 Certificates then Outstanding. In such event, the 2008 Certificates will be transferable to such securities depository in accordance with subsection (c) of this Section, and thereafter, all references in this Trust Agreement to DTC or its nominee shall be deemed to refer to such successor securities depository and its nominee, as appropriate.

(c) In the event that any transfer or exchange of 2008 Certificates is authorized under subsection (a) or (b) of this Section, such transfer or exchange shall be accomplished upon receipt by the Trustee from the registered owner thereof of the 2008 Certificates to be transferred or exchanged and appropriate instruments of transfer to the permitted transferee, all in accordance with the applicable provisions of Sections 2.06 and 2.07 hereof. In the event securities certificates are delivered to Owners other than Cede & Co., its successor as nominee for DTC as Owner of all the 2008 Certificates, another securities depository as Owner of all the 2008 Certificates, or the nominee of such successor securities depository, the provisions of Sections 2.06 and 2.07 hereof shall also apply to, among other things, the registration, exchange and transfer of the 2008 Certificates and the method of payment of principal, prepayment premium, if any, and interest evidenced and represented by the 2008 Certificates.

(d) Liquidity Provider Certificates. Notwithstanding any other provisions hereof, the Trustee shall take all necessary action to obtain a separate CUSIP number and to qualify Liquidity Provider Certificates for book-entry in accordance with the procedures of DTC. If for any reason the Liquidity Provider Certificates are not assigned a separate CUSIP number or if a separate CUSIP number has been assigned but the Liquidity Provider so elects, at the request of

the Liquidity Facility Provider, Liquidity Provider Certificates shall be registered in the name of the Liquidity Facility Provider or its nominees or registered assigns, and not in the name of the Depository, DTC, Cede & Co. or other nominee or its registered assign. In such case, the Trustee shall take all necessary action to withdraw Liquidity Provider Certificates from the Depository in order to register Liquidity Provider Certificates in the name of the Liquidity Facility Provider, or the nominee or registered assigns thereof.

Section 2.12. Authorization of Delivery of 2008 Certificates; Application of Proceeds. On the Delivery Date, the Trustee authorized the execution and delivery of the 2008 Certificates to the purchaser thereof upon the Written Request of the Authority and upon receipt of the proceeds of the sale thereof. Upon receipt of the proceeds of the sale of the 2008 Certificates from the purchaser thereof (in the amount of \$46,581,988.19 (representing the \$47,625,000.00 aggregate principal amount of the 2008 Certificates, less underwriter's discount of \$153,920.63, and less \$826,615.80 transferred by the purchaser at the request of the Authority to the 2008 Certificate Insurer as payment of the premium for the 2008 Certificate Insurance Policy and \$62,475.38 transferred by the purchaser at the request of the Authority to the 2008 Certificate Insurer as payment of the premium for the 2008 Parity Reserve Fund Insurance Policy), the Trustee set aside and deposited the proceeds received from such sale in the following respective accounts or funds or with the following respective persons, in the following order of priority:

- (a) the Trustee deposited to the 2006 Debt Service Fund, established pursuant to Section 4.03 of the 2006 Trust Agreement, the amount of \$46,275,000.00;
- (b) the Trustee deposited to the Parity Reserve Fund, created pursuant to the 1997 Trust Agreement, the amount of \$36.57; and
- (c) the Trustee deposited the remainder of the proceeds of sale of the 2008 Certificates (such amount being \$306,951.62) in the Costs of Issuance Fund established pursuant to Section 4.05 hereof.

Simultaneously with the deposit of proceeds, the Trustee (i) retained in the Parity Reserve Fund, created pursuant to the 1997 Trust Agreement, which fund was continued pursuant to Section 4.04 hereof, the amount of \$1,834,515.50 from amounts in the Parity Reserve Fund deposited from the proceeds 2006 Certificates and (ii) deposited in the Parity Reserve Fund the 2008 Parity Reserve Fund Insurance Policy, together being an amount sufficient to cause the balance on deposit in, or credited to the Parity Reserve Fund to be equal to the Reserve Fund Requirement upon delivery of the 2008 Certificates.

Section 2.13. Reserved.

Section 2.14. Determination of Flexible Rates and Interest Periods During Flexible Mode. An Interest Period for the 2008 Certificates in the Flexible Mode shall be of such duration of from one to 397 calendar days, ending on a day preceding a Business Day or the Maturity Date, as the Remarketing Agent shall determine in accordance with the provisions of this Section 2.14. In making the determinations with respect to Interest Periods, subject to limitations imposed by the immediately preceding sentence, on each Rate Determination Date for a Flexible Rate Certificate, the Remarketing Agent shall select the Interest Period that would

result in the Remarketing Agent being able to remarket the 2008 Certificates at par in the secondary market at the lowest average interest cost under then-existing marketing conditions; provided, however, that if the Remarketing Agent has received notice from the Authority to the effect that the Mode for the 2008 Certificates is to be changed from the Flexible Mode to any other Mode, the Remarketing Agent shall select Interest Periods that do not extend beyond the resulting Mode Change Date. The Flexible Rate for the 2008 Certificates in a Flexible Mode shall be the rate of interest per annum determined by the Remarketing Agent to be the minimum interest rate which, if evidenced by the 2008 Certificates, would enable the Remarketing Agent to sell the 2008 Certificates under then existing market conditions, including length of Interest Period, on the effective date of such rate at a price equal to the principal amount thereof. Each 2008 Certificate in a Flexible Mode may evidence interest at a different Flexible Rate and may have an Interest Period within the Flexible Mode which differs from the Interest Period applicable to any 2008 Certificate in a Flexible Mode.

The Trustee, in consultation with the Remarketing Agent, shall take such actions as shall be necessary to distinguish 2008 Certificates having different Flexible Rate Periods, which actions may include obtaining different CUSIP numbers if determined desirable by the Trustee or the Remarketing Agent.

By 1:00 p.m. New York City time on each Rate Determination Date, the Remarketing Agent, with respect to each 2008 Certificate in the Flexible Mode that is subject to adjustment on such Rate Determination Date, shall determine the Flexible Rate for the Interest Period then selected for such 2008 Certificate and shall give notice of the Interest Period, the Purchase Date and the Flexible Rate for such 2008 Certificate, such notice to be given by Electronic means to the Trustee and the Authority. The Remarketing Agent shall make the Flexible Rate and Interest Period available after 2:00 p.m. New York City time on each Rate Determination Date by telephone or Electronic means to any Beneficial Owner or Notice Party other than the Authority requesting such information.

In the event the use of the Book-Entry System is discontinued, in order to receive payment of the Purchase Price of any 2008 Certificate in the Flexible Mode, the Owner of such 2008 Certificate must present such 2008 Certificate to the Trustee, by 12:00 noon New York City time on the applicable Mandatory Purchase Date. Upon receipt of such 2008 Certificate by 12:00 noon New York City time on a Mandatory Purchase Date, the Trustee shall pay the Purchase Price to such Owner by 2:30 p.m. New York City time on such Mandatory Purchase Date.

Section 2.15. Determination of Interest Rates During the Daily Mode and the Weekly Mode. The interest rate for the 2008 Certificates during the Daily Mode or Weekly Mode shall be the rate of interest per annum determined by the Remarketing Agent on and as of the applicable Rate Determination Date as the minimum rate of interest which, in the opinion of the Remarketing Agent under then-existing market conditions, would result in the sale of the 2008 Certificates in the Daily Rate Period or Weekly Rate Period, as applicable, at a price equal to 100% of the principal amount thereof.

(a) During the Daily Mode, the Remarketing Agent shall establish the Daily Rate by 10:00 a.m. New York City time on each Rate Determination Date. The Daily

Rate for any day during the Daily Mode which is not a Business Day shall be the Daily Rate established on the immediately preceding Rate Determination Date. The Remarketing Agent shall make the Daily Rate available no less frequently than once each week by telephone or Electronic means to the Authority, each other Notice Party and any Beneficial Owner requesting such rate.

(b) During the Weekly Mode, the Remarketing Agent shall establish the Weekly Rate by 4:00 p.m. New York City time on each Rate Determination Date. The Weekly Rate shall be in effect during the applicable Weekly Rate Period. The Remarketing Agent shall make the Weekly Rate available no later than 5:00 p.m. New York City time on the Business Day following the Rate Determination Date by telephone or Electronic means to the Authority, each other Notice Party and any Beneficial Owner requesting such rate.

Section 2.16. Determination of Term Rates and Fixed Rates.

(a) Term Rates. The interest rate for the 2008 Certificates in the Term Rate Mode shall be the minimum rate which, in the opinion of the Remarketing Agent, would result in a sale of the 2008 Certificates, under then existing market conditions, at a price equal to 100% of the principal amount thereof on the Rate Determination Date for a Term Rate Period of the duration selected by the Authority, written notice of which shall have been delivered by the Authority to the Remarketing Agent prior to such Rate Determination Date. Notwithstanding the foregoing, if the Authority shall deliver a Favorable Opinion of Special Counsel, the interest rate set for some or all of the affected 2008 Certificates may include a premium or a discount. In no event shall any Term Rate be greater than the Maximum Rate and no Term Rate Period may extend beyond the Maturity Date.

The Term Rate shall be determined by the Remarketing Agent not later than 4:00 p.m. New York City time on the Rate Determination Date and the Remarketing Agent shall make the Term Rate available by telephone or Electronic means after 5:00 p.m. New York City time on the Rate Determination Date to the Authority and each other Notice Party requesting such Term Rate. A copy of each such notice shall be provided to the 2008 Certificate Insurer.

Except as is otherwise provided in Section 2.17 hereof, once the 2008 Certificates are changed to a Term Rate Mode, the 2008 Certificates shall continue in the Term Rate Mode until changed to another Mode in accordance with Section 2.18 hereof. If the Authority shall have failed to select a new Term Rate Period prior to the applicable Rate Determination Date for such new Term Rate Period, the new Term Rate Period shall be the same length as the current Term Rate Period; provided however, that no Term Rate Period may extend beyond the Maturity Date.

(b) Fixed Rates. The Fixed Rate for the 2008 Certificates when being converted from a Short-Term Mode or a Term Rate Mode to the Fixed Rate Mode shall be determined by the Fixed Rate Remarketing Agent in the following manner: not later than 4:00 p.m. New York City time on the applicable Rate Determination Date, the Fixed Rate Remarketing Agent shall determine the Fixed Rate or Fixed Rates, as applicable. The Fixed Rate or Fixed Rates shall be the minimum interest rate(s) which, in the opinion of the applicable Fixed Rate Remarketing Agent, will result in a sale of the 2008 Certificates at a price equal to the principal amount

thereof on the Rate Determination Date. Notwithstanding the foregoing, if the Authority shall deliver a Favorable Opinion of Special Counsel, the interest rate set for some or all of the 2008 Certificates may include a premium or a discount. The Fixed Rate Remarketing Agent shall make the Fixed Rate or Fixed Rates, as applicable, available by telephone or by Electronic means after 5:00 p.m. New York City time on the Rate Determination Date to the Authority and each other Notice Party requesting notice of such Fixed Rate or Fixed Rates. A copy of each such notice shall be provided to the 2008 Certificate Insurer. The Fixed Rate or Rates, as applicable, so established for the 2008 Certificates shall remain in effect until the Maturity Date or Maturity Dates, as applicable, of the 2008 Certificates.

Section 2.17. Alternate Rates. When the 2008 Certificates are in a Daily Mode, a Weekly Mode, a Flexible Rate Mode or a Term Rate Mode, the following provisions shall apply in the event (i) the Remarketing Agent fails or is unable to determine the interest rate for the 2008 Certificates or to determine the interest rate or Flexible Rate Period for the 2008 Certificates within the Flexible Mode, (ii) the method by which the Remarketing Agent determines the interest rate or Interest Period with respect to the 2008 Certificates (or the selection by the Authority of the duration of a Term Rate Period for the 2008 Certificates) shall be held to be unenforceable by a court of law of competent jurisdiction, or (iii) the Remarketing Agent suspends its remarketing effort in accordance with the provisions of the Remarketing Agreement. The provisions set forth in this Section shall continue to apply until such time as the Remarketing Agent (or the Authority, if applicable) resumes making such determinations. In the case of clause (ii) above, the Remarketing Agent (or the Authority, if applicable) shall resume making such determination at such time as there is delivered to the Remarketing Agent or the Authority, as applicable, an opinion of Special Counsel to the effect that there are no longer any legal prohibitions against the Remarketing Agent or Authority, as applicable, making such determinations.

The following shall be the methods by which the interest rates and, in the case of the Flexible Rate Mode and Term Rate Modes, the Interest Periods, shall be determined for the 2008 Certificates or for any Flexible Rate Certificate as to which any of the events described in clauses (i), (ii) or (iii) above shall be applicable. Such methods shall be applicable from and after the date any of the events described in clauses (i), (ii) or (iii) of the immediately preceding paragraph shall become applicable until such time as the events described in clauses (i), (ii) or (iii) of the immediately preceding paragraph are no longer applicable to the 2008 Certificates or any Flexible Rate Certificate. Notwithstanding any other provision herein, these provisions shall not apply with respect to the selection of the length of the Term Rate Period for the 2008 Certificates in a Term Rate Mode if the Authority fails to select the length of the Term Rate Period for the 2008 Certificates for a reason other than as described in clause (ii) of the immediately preceding paragraph.

(a) For Flexible Rate Certificates, the next Interest Period shall be from, and including, the first day following the last day of the current Interest Period for the applicable Flexible Rate Certificates to, but excluding, the next succeeding Business Day, and thereafter the Interest Period for such Flexible Rate Certificate shall commence on each Business Day and extend to, but exclude, the next succeeding Business Day. For each such Interest Period, the interest rate for such Flexible Rate Certificates shall be the applicable Alternate Rate in effect on the Business Day that begins an Interest Period.

(b) If the 2008 Certificates are in a Daily Mode or a Weekly Mode, then the 2008 Certificates shall evidence interest during each subsequent Interest Period for the 2008 Certificates at the Alternate Rate in effect on the first day of such Interest Period.

(c) If the 2008 Certificates are in a Term Rate Mode, then the 2008 Certificates shall automatically convert to a Flexible Rate Mode, with an Interest Period commencing on the first day following the last day of the current Interest Period for the 2008 Certificates to, but excluding, the next succeeding Business Day, and thereafter the Interest Period for the 2008 Certificates shall commence on each Business Day and extend to, but exclude, the next succeeding Business Day. For each such Interest Period, the interest rate for the 2008 Certificates shall be the applicable Alternate Rate in effect at the beginning of each such Interest Period.

Section 2.18. Changes in Mode. Subject to compliance with the provisions set forth in this Section, the Authority may elect to effect a change in Mode with respect the 2008 Certificates (other than the 2008 Certificates in a Fixed Rate Mode); provided that all the 2008 Certificates of any series shall be converted.

(a) Changes to Modes Other Than Fixed Rate Mode. At the option of the Authority, the 2008 Certificates (other than the 2008 Certificates being changed to a Fixed Rate Mode, which shall be governed by the provisions set forth in Section 2.18(d) hereof) may be changed from one Mode to another Mode (other than a Fixed Rate Mode) as set forth below:

(i) Notice by Authority. At least five (5) Business Days (or such shorter time as may be agreed to by the Authority, the Trustee and the Remarketing Agent) prior to the date that notice of the proposed Mode Change Date is required to be given to the Owners by the Trustee as specified below, the Authority shall give written notice to each of the Notice Parties of its intention to effect a change in the Mode from the Mode then prevailing (for purposes of this Section, the "Current Mode") to another Mode (for purposes of this Section, the "New Mode") which shall be specified in such written notice. Such notice to the Notice Parties shall specify the proposed Mode Change Date and shall also include a statement as to whether a Liquidity Facility is expected to be in effect with respect to the 2008 Certificates following such change and, if a Liquidity Facility is expected to be in effect, such notice shall identify the anticipated provider of such Liquidity Facility. If the change is to a Term Rate Mode, such notice shall specify the length of the initial Term Rate Period.

(ii) Notice to Owners. Notice of the proposed change in Mode, unless otherwise specified in Section 2.18(d) hereof, shall be given by the Trustee to the Owners of the 2008 Certificates not less than the 15th day next preceding the applicable Mode Change Date; provided that no notice need be given for a Mode Change Date occurring on the first Business Day following the last day of a Flexible Rate Period or a Term Rate Mode or on a Substitution Date. Such notice shall state the Mode to which the conversion will be made and the proposed Mode Change Date and, if applicable, shall be combined with the notice of mandatory purchase required to be delivered by the Trustee pursuant to Section 3.02 hereof. If the Book-Entry System is no longer in effect, such notice shall also provide information with respect to required delivery of physical 2008

Certificates and procedures for payment of Purchase Price. Notwithstanding any other provision of this Trust Agreement, the Trustee shall not mail such written notice if the 2008 Certificates are being converted from a Flexible Mode until the Trustee shall have received a written confirmation from the Remarketing Agent to the effect that no Interest Period for the 2008 Certificates extends beyond the proposed Mode Change Date. The Trustee shall provide a copy of such notice to the Authority and to each of the other Notice Parties.

(iii) Determination of Interest Rates and Interest Periods. The New Mode shall commence on the Mode Change Date and the interest rate(s), together, in the case of a change to the Flexible Mode, with the Interest Period or Interest Period(s), as applicable, shall be determined by the Remarketing Agent (or the Authority in the case of the Interest Period for the 2008 Certificates being converted to a Term Rate Mode) in the manner provided in Section 2.14, Section 2.15 and Section 2.16 hereof, as applicable.

(iv) Conditions Precedent:

(A) The Mode Change Date shall be: (1) in the case of a change from a Flexible Mode, the next Mandatory Purchase Date for all of the Flexible Rate 2008 Certificates; (2) in the case of a change from a Daily Mode or a Weekly Mode, any Business Day; and (3) in the case of a change from a Term Rate Mode to another Mode, or from a Term Rate Period to a Term Rate Period of a different duration, the Mode Change Date shall be limited to (aa) any Interest Payment Date on which the 2008 Certificates are subject to optional prepayment or (bb) the last Interest Payment Date of the current Term Rate Period. The 2008 Certificates shall be subject to mandatory tender for purchase on such Mode Change Date in accordance with Section 3.02 hereof, and, except as is otherwise provided herein, the 2008 Certificates shall be purchased on the Mode Change Date at a Purchase Price equal to 100% of the principal amount thereof; provided, however, that if the 2008 Certificates are to be purchased on an Interest Payment Date other than the last Interest Payment Date applicable to the 2008 Certificates, and if the 2008 Certificates would otherwise be subject to optional prepayment on such Mode Change Date at a prepayment price of more than 100% of the principal amount thereof, then the 2008 Certificates shall be purchased at a Purchase Price equal to such prepayment price.

(B) If the 2008 Certificates to be converted are in the Flexible Mode, no Interest Period for the 2008 Certificates set after delivery by the Authority to the Remarketing Agent of the notice of the intention to effect a change in Mode shall extend beyond the day preceding the proposed Mode Change Date.

(C) As and to the extent applicable, the Authority shall select a Remarketing Agent for the 2008 Certificates, and shall provide for the delivery of a Liquidity Facility if required.

(D) The Authority shall have obtained and provided to the Trustee the written consent of the 2008 Certificate Insurer to the change in Mode.

(E) The following items shall have been delivered to the Authority, Trustee, the 2008 Certificate Insurer and the Remarketing Agent on or prior to the Mode Change Date:

(1) in the case of a change from any Mode other than a change from a Daily Mode to a Weekly Mode or a change from a Weekly Mode to a Daily Mode, a Favorable Opinion of Special Counsel dated the Mode Change Date;

(2) if there is to be a Liquidity Facility delivered in connection with such change, the items required by Section 3.11 hereof; and

(3) a notice from the Rating Agencies of the rating(s) to be assigned to the 2008 Certificates on such Mode Change Date.

(v) Rescission of Election. The Authority may rescind any election by it to change a Mode in accordance with this Section 2.18(a) as provided in Section 2.18(f) hereof.

(b) Reserved.

(c) Reserved.

(d) Change to Fixed Rate Mode. At the option of the Authority, the 2008 Certificates (other than the 2008 Certificates in a Fixed Rate Mode) may be converted to a Fixed Rate Mode. Any such conversion shall be made as set forth below.

(i) Mode Change Date Provisions. The Mode Change Date shall be:

(A) in the case of a change from a Flexible Mode, the next Mandatory Purchase Date for the Flexible Rate 2008 Certificates of the 2008 Certificates;

(B) in the case of a change from a Daily Mode or a Weekly Mode, any Business Day; and

(C) in the case of a change from a Term Rate Mode, the Mode Change Date shall be limited to (1) any Interest Payment Date on which the 2008 Certificates are subject to optional prepayment or (2) the next Mandatory Purchase Date for the 2008 Certificates being converted, as the case may be. The 2008 Certificates in a Term Rate Mode shall be subject to mandatory tender for purchase pursuant to Section 3.02 hereof and shall be purchased on such Mode Change Date at a Purchase Price equal to 100% of the principal amount thereof; provided that if the 2008 Certificates would otherwise be subject to optional prepayment on such Mode Change Date at a prepayment price of more than 100% of the principal amount thereof, the 2008 Certificates shall be purchased at a Purchase Price equal to such prepayment price.

(ii) Serialization Provisions. Upon conversion of the 2008 Certificates to a Fixed Rate Mode, unless otherwise directed by the Authority, the 2008 Certificates will be converted to Serial Certificates maturing in such years and such principal amounts as correspond to the years and principal amounts set forth in the mandatory Sinking Fund Payment schedule set forth in Section 2.03 hereof

(iii) Notice by Authority. At least 5 Business Days (or such shorter time as may be agreed to by the Trustee, and the Remarketing Agent, if any) prior to the date that notice of the Mode Change Date is required to be given to the Owners by the Trustee as specified in paragraph (iii) below, the Authority shall give written notice to each of the Notice Parties. Such notice shall state that the Mode will be changed to the Fixed Rate Mode, shall set forth the proposed Mode Change Date, and shall be accompanied by the appointment of one or more firms of investment bankers to remarket the 2008 Certificates being changed to the Fixed Rate Mode (such firm or firms of investment bankers being hereinafter referred to as the "Fixed Rate Remarketing Agent"). Together with such notice, the Authority shall file with the Trustee and the 2008 Certificate Insurer a Favorable Opinion of Special Counsel. No conversion to a Fixed Rate Mode shall occur unless the Authority shall also file with the Trustee and the 2008 Certificate Insurer a Favorable Opinion of Special Counsel to the same effect dated the Mode Change Date.

(iv) Notice to Owners. Not less than the 15th day next preceding the Mode Change Date, the Trustee shall mail notice of such proposed change to the Owners of the 2008 Certificates, such notice to state that the Mode on the 2008 Certificates will be changed to a Fixed Rate Mode and to set forth the proposed Mode Change Date. Such notice shall be combined with the notice of mandatory purchase required to be delivered by the Trustee pursuant to Section 3.02 hereof. If the Book-Entry System is no longer in effect, such notice shall also provide information with respect to required delivery of physical 2008 Certificates and the procedures for payment of Purchase Price. Notwithstanding any other provision of this Trust Agreement, the Trustee shall not mail such written notice if the 2008 Certificates are being converted from a Flexible Mode until the Trustee shall have received a written confirmation from the Remarketing Agent to the effect that no Interest Period for the 2008 Certificates extends beyond the proposed Mode Change Date. The Trustee shall provide a copy of such notice to the Authority and to each of the other Notice Parties.

(v) General Provisions Applying to Change to Fixed Rate Mode. The change to a Fixed Rate Mode shall not occur unless the Authority shall have selected a Fixed Rate Remarketing Agent to remarket the 2008 Certificates being changed to the Fixed Rate Mode and the following items shall have been delivered to the Authority and each of the Notice Parties, such items to be delivered on or prior to the Mode Change Date:

- (A) a Favorable Opinion of Special Counsel dated the Mode Change Date;
- (B) the written consent of the 2008 Certificate Insurer to the change in Mode; and

(C) notice from the Rating Agencies of the rating(s) to be assigned the 2008 Certificates on such Mode Change Date.

(vi) Determination of Fixed Rates. The Fixed Rate (or Fixed Rates in the case of Serial Certificates) for the 2008 Certificates shall be established by the applicable Fixed Rate Remarketing Agent on the Rate Determination Date applicable thereto. Such Fixed Rate Remarketing Agent shall set the interest rate or interest rates with respect to the 2008 Certificates in accordance with the provisions set forth in Section 2.16(b) hereof. Such Fixed Rate or Fixed Rates, as applicable, shall remain in effect until the Maturity Date or Maturity Dates, as applicable, of the 2008 Certificates. The applicable Remarketing Agent shall make the Fixed Rate or Rates available by telephone or Electronic means not later than 5:00 p.m., New York City time, on the Rate Determination Date to the Authority, the Trustee and each of the other Notice Parties requesting such notice.

(vii) Modification of Serialization Provisions, Prepayment Provisions and Price. Upon conversion of the 2008 Certificates to a Fixed Rate Mode, the 2008 Certificates shall be subject to the serialization provisions set forth in subsection (ii) above, shall be subject to the optional prepayment and mandatory sinking fund prepayment provisions set forth in Section 2.03 hereof and shall be remarketed at par. Notwithstanding the foregoing or any other provision of this Trust Agreement to the contrary, the Authority may elect to change the serialization provisions, the optional prepayment provisions or the mandatory sinking fund prepayment provisions and/or remarket some or all of the 2008 Certificates at a premium or discount to par if the Authority shall file with the Trustee and the 2008 Certificate Insurer a Favorable Opinion of Special Counsel.

(viii) Rescission of Election. The Authority may rescind any election by it to change a Mode in accordance with this Section 2.18(d) as provided in Section 2.18(f) hereof.

(e) Failure to Satisfy Conditions Precedent to a Mode Change. In the event that the Authority has not withdrawn any election by it to change a Mode as provided herein and the conditions described above in subsections (a), (b), (c) or (d) of this Section, as applicable, have not been satisfied by the applicable Mode Change Date, then the New Mode shall not take effect (although any mandatory purchase shall be made on such date if notice has been sent to the Owners stating that the 2008 Certificates would be subject to mandatory purchase on such date). If the failed change in Mode was from a Flexible Mode, the 2008 Certificates shall remain in the Flexible Mode with interest rates and Interest Periods to be established by the Remarketing Agent on the failed Mode Change Date in accordance with Section 2.14 hereof. If the failed change in Mode was from a Daily Mode, the 2008 Certificates shall remain in the Daily Mode, and if the failed change in Mode was from a Weekly Mode, the 2008 Certificates shall remain in the Weekly Mode, in each case with interest rates established in accordance with the applicable provisions of Section 2.15 hereof on and as of the failed Mode Change Date. If the failed change in Mode was from a Term Rate Mode, then the 2008 Certificates shall stay in the Term Rate Mode for an Interest Period ending on the following Interest Payment Date for the 2008

Certificates in the Term Rate Mode and the interest rate shall be established by the Remarketing Agent on the failed Mode Change Date in accordance with Section 2.16(a) hereof.

(f) Rescission of Election. Notwithstanding anything herein to the contrary, the Authority may rescind any election by it to change a Mode as described above prior to the Mode Change Date by giving written notice thereof to the Notice Parties prior to such Mode Change Date. If the Trustee receives notice of such rescission prior to the time the Trustee has given notice to the Owners of the 2008 Certificates, then such notice of change in Mode shall be of no force and effect. If the Trustee receives notice from the Authority of rescission of a Mode change after the Trustee has given notice thereof to the Owners of the 2008 Certificates, then if the proposed Mode Change Date would have been a Mandatory Purchase Date, such date shall continue to be a Mandatory Purchase Date.

If the proposed change in Mode was from a Flexible Mode, the 2008 Certificates shall remain in the Flexible Mode with interest rates and Interest Periods to be established by the Remarketing Agent on the proposed Mode Change Date in accordance with Section 2.14 hereof. If the proposed change in Mode was from a Daily Mode, the 2008 Certificates shall remain in the Daily Mode, and if the proposed change in Mode was from a Weekly Mode, the 2008 Certificates shall remain in the Weekly Mode, in each case with interest rates established in accordance with the applicable provisions of Section 2.15 hereof on and as of the proposed Mode Change Date. If the proposed change in Mode was from a Term Rate Mode, then the 2008 Certificates shall stay in the Term Rate Mode for an Interest Period ending on the following Interest Payment Date for the 2008 Certificates in the Term Rate Mode and the interest rate shall be established by the Remarketing Agent on the proposed Mode Change Date in accordance with Section 2.16(a) hereof. If the Remarketing Agent is unable to determine the interest rate on the proposed Mode Change Date, the provisions of Section 2.17 shall apply.

(g) Form of Notices. Upon request, the form of any notice from the Trustee to the Owners of the 2008 Certificates required by this Section 2.18 and by Section 3.02 shall be furnished by the Authority to the Trustee.

### ARTICLE III

#### TENDERS OF 2008 CERTIFICATES; REMARKETING

Section 3.01. Optional Tenders of Certificates in a Daily Mode or a Weekly Mode. Subject to Section 3.06 hereof, during any Daily Mode for the 2008 Certificates and during any Weekly Mode for the 2008 Certificates, any 2008 Certificate or portion thereof in a principal amount equal to an Authorized Denomination shall be purchased on any Business Day at a price equal to the Purchase Price, upon delivery of a Tender Notice to the Trustee by the Tender Notice Deadline. Immediately upon receipt of a Tender Notice, the Trustee shall notify the Remarketing Agent and provide the Remarketing Agent with a copy of such Tender Notice. Notwithstanding any other provision of this Trust Agreement to the contrary, the provisions set forth in this Section 3.01 shall not apply to any Certificate in a Delayed Remarketing Period.

Section 3.02. Mandatory Tender for Purchase on Mandatory Purchase Date. The 2008 Certificates shall be subject to mandatory purchase on each Mandatory Purchase Date applicable

to the 2008 Certificates. The Trustee shall give notice of each such mandatory purchase, such notice to be given by mail to the Owners of the 2008 Certificates subject to mandatory purchase no less than 15 days prior to the applicable Mandatory Purchase Date, provided that, if the mandatory purchase is directed as a result of an event of default under the Liquidity Facility, such notice may be given no less than 10 days prior to the applicable Mandatory Purchase Date or as late as the Mandatory Purchase Date. No notice shall be required to be given nor shall any notice be given with respect to any 2008 Certificate in a Flexible Rate Mode in connection with the Mandatory Purchase Date occurring at the end of each Interest Period for the 2008 Certificates. The form of the notice of mandatory purchase shall be provided to the Trustee by the Authority.

Any notice to be given pursuant to this Section 3.02 shall state the Mandatory Purchase Date, shall set forth the Purchase Price applicable on such Mandatory Purchase Date, and shall identify the 2008 Certificates to be purchased. Such notice shall also state that interest on the 2008 Certificates subject to mandatory purchase shall cease to accrue from and after the Mandatory Purchase Date. The failure to mail such notice with respect to any 2008 Certificate shall not affect the validity of the mandatory purchase of any other 2008 Certificate with respect to which notice was so mailed. Any notice mailed will be conclusively presumed to have been given, whether or not actually received by any Owner. If the Book-Entry System is no longer in effect, such notice shall also provide information with respect to required delivery of physical certificates and the procedures for payment of Purchase Price. A copy of any notice delivered by the Trustee pursuant to this Section 3.02 shall also be provided to each of the Notice Parties.

Section 3.03. Purchases of Certificates in Daily Mode, Weekly Mode, Flexible Mode and Term Rate Mode; Payment of Purchase Price; Notices.

(a) On each date on which 2008 Certificates in a Daily Mode, a Weekly Mode, a Flexible Mode or a Term Rate Mode are to be purchased:

(i) the Remarketing Agent shall notify the Trustee and the Authority by 12:00 noon New York City time of the principal amount of such tendered 2008 Certificates it has remarketed and of the principal amount of such tendered 2008 Certificates it has not remarketed, such notice to be provided by Electronic means;

(ii) subject to Section 3.06(b)(ii), the Remarketing Agent shall cause the proceeds of the remarketing by the Remarketing Agent of such tendered 2008 Certificates to be paid to the Trustee in immediately available funds not later than 11:15 a.m., New York City time, on the Purchase Date for such tendered 2008 Certificates;

(iii) the Remarketing Agent shall notify the Trustee by Electronic means not later than 1:00 p.m. New York City time of such information as may be necessary to register and deliver such remarketed 2008 Certificates, such notice to be provided by Electronic means; and

(iv) if the affected 2008 Certificates are no longer in the Book-Entry System, the Trustee shall authenticate new 2008 Certificates for the respective purchasers thereof

which shall be available for pick-up by the Remarketing Agent not later than 2:30 p.m. New York City time.

(b) On each date on which a 2008 Certificate is to be purchased, the Trustee shall draw on the applicable Liquidity Facility, if any, by 12:00 p.m. New York City time in an amount equal to the Purchase Price of all such 2008 Certificates less remarketing proceeds received per Section 3.03(a)(ii) for payment by 3:00 p.m. New York City time and shall notify the 2008 Certificate Insurer of such draw; provided, however, that if the draw is in connection with a Mandatory Purchase Date resulting from a Substitution Date, the draw shall be made on the existing Liquidity Facility that is being replaced. In no event shall the Trustee draw on a Liquidity Facility to pay the Purchase Price of any 2008 Certificate not covered by such Liquidity Facility or to pay the Purchase Price of a 2008 Certificate owned by the Authority or the City.

(c) If the Trustee is notified in writing by a Liquidity Facility Provider that an Automatic Termination Event has occurred, with respect to its Liquidity Facility, then the Trustee shall provide prompt written notice thereof to the Owners of the 2008 Certificates to which such Liquidity Facility relates and shall provide copy of such notice to each of the Notice Parties.

(d) If the Trustee does not have funds in the applicable Remarketing Proceeds Account and the applicable Liquidity Facility Account sufficient to pay the Purchase Price of such 2008 Certificates on any Purchase Date, the Trustee shall give the Authority notice of such insufficiency by 2:45 p.m. New York City time on such Purchase Date.

Section 3.04. Source of Funds for Purchase of 2008 Certificates in Daily Mode, Weekly Mode, Flexible Mode, or Term Rate Mode. By 3:00 p.m. New York City time on the date on which a 2008 Certificate in a Daily Mode, a Weekly Mode, a Flexible Mode or a Term Rate Mode is to be purchased, the Trustee shall purchase tendered 2008 Certificates from the tendering Owners at the applicable Purchase Price by wire transfer in immediately available funds. Except as otherwise provided in the case of the payment of a mandatory purchase price pursuant to Section 3.02, funds for the payment of such Purchase Price shall be derived solely from the following sources in the order of priority indicated and neither the Trustee nor the Remarketing Agent shall be obligated to provide funds from any other source:

(a) immediately available funds on deposit in the Remarketing Proceeds Account excluding funds received from the Authority or the City;

(b) immediately available funds on deposit in the applicable Liquidity Facility Account, if any; and

(c) in the Authority's sole discretion, moneys provided by the Authority that may lawfully be used for such purpose.

Notwithstanding the foregoing, any mandatory purchase of the 2008 Certificates made at the direction of the provider of the Liquidity Facility shall be payable solely from funds drawn under the Liquidity Facility and deposited into the Liquidity Facility Payment Account established

pursuant to Section 4.08 hereof, and any amounts mentioned in clause (a) or clause (c) above shall be used to reimburse the Bank for such payment.

Section 3.05. Delivery of Certificates in Daily Mode, Weekly Mode, Flexible Mode or Term Rate Mode. On each date on which a 2008 Certificate in a Daily Mode, a Weekly Mode, a Flexible Mode or a Term Rate Mode is to be purchased, such 2008 Certificate shall be delivered as follows:

(a) Each 2008 Certificate sold by the Remarketing Agent and for which payment has been received as described in Section 3.04(a) hereof shall be delivered by the Remarketing Agent to the purchaser of such Certificate by 3:00 p.m. New York City time; and

(b) Each 2008 Certificate purchased by the Trustee with moneys described in Section 3.04(b) hereof or purchased from proceeds from the 2008 Liquidity Facility Payment Account shall be registered immediately in the name of the applicable Liquidity Facility Provider or its nominee (which may be the Securities Depository) as provided in Section 2.11(d), if any, on or before 3:00 p.m. New York City time. The Trustee shall not release any Liquidity Provider Certificates unless the Trustee shall have received evidence that the Liquidity Facility has been reinstated to an amount equal to the principal amount of unremarketed 2008 Certificates, including Liquidity Provider Certificates, plus interest at the Maximum Rate for the number of days required under the Liquidity Facility.

(c) Each 2008 Certificate purchased by the Authority with moneys described in Section 3.04(c) hereof shall be registered immediately in the name of the Authority or its nominee on or before 3:00 p.m. New York City time. Any 2008 Certificate so owned by the Authority shall continue to be Outstanding under the terms of this Trust Agreement and be subject to all of the terms and conditions of the Trust Agreement and shall be subject to remarketing by the applicable Remarketing Agent; provided, however, that the Authority shall not be considered a Owner for the purpose of voting such 2008 Certificates under this Trust Agreement.

Section 3.06. Book-Entry Tenders.

(a) Notwithstanding any other provision of this Trust Agreement to the contrary, all tenders for purchase of 2008 Certificates during any period in which 2008 Certificates so tendered are registered in the name of Cede & Co. (or the nominee of any successor Securities Depository) shall be subject to the terms and conditions set forth in the Representations Letter and to any regulations promulgated by DTC (or any successor Securities Depository). For so long as the 2008 Certificates are registered in the name of Cede & Co., as nominee for DTC, the tender option rights of Owners of 2008 Certificates may be exercised only by a Direct Participant of DTC (as such term is described in Schedule A attached to the Representation Letter) acting, directly or indirectly, on behalf of a Beneficial Owner of 2008 Certificates by giving notice of its election to tender 2008 Certificates or portions thereof at the times and in the manner described above. Beneficial Owners will not have any rights to tender 2008 Certificates directly to the Trustee.

Procedures under which a Beneficial Owner may direct a Direct Participant of DTC, or an Indirect Participant of DTC (as such term is described in Schedule A attached to the Representation Letter) acting through a director participant of DTC, to exercise a tender option right in respect of 2008 Certificates or portions thereof in an amount equal to all or a portion of such Beneficial Owner's beneficial ownership interest therein, shall be governed by standing instructions and customary practices determined by such Direct Participant or Indirect Participant. For so long as the 2008 Certificates are registered in the name of Cede & Co., as nominee for DTC, delivery of the 2008 Certificates required to be tendered for purchase shall be effected by the transfer in the Book-Entry System on the applicable Purchase Date of a book-entry credit to the account of the Trustee of a beneficial interest in such 2008 Certificates.

(b) Notwithstanding anything expressed or implied herein to the contrary, so long as the Book-Entry System for the 2008 Certificates is maintained by the Authority:

(i) there shall be no requirement of physical delivery to, or by, the applicable Remarketing Agent or the Trustee of:

(A) any 2008 Certificates subject to optional or mandatory purchase as a condition to the payment of the Purchase Price therefor;

(B) any 2008 Certificates that have become Liquidity Facility Certificates; or

(C) any remarketing proceeds of such 2008 Certificates or Liquidity Facility Certificates to any Owner other than the Securities Depository or its nominee, as applicable; and

(ii) except as provided in (iii) below, the Trustee shall not have any responsibility for paying the Purchase Price of any tendered 2008 Certificate or for remitting remarketing proceeds to any person and such remarketing proceeds may be remitted directly to the Securities Depository by the applicable Remarketing Agent; and

(iii) the Trustee's sole responsibilities in connection with the purchase and remarketing of a tendered 2008 Certificate shall be:

(A) to draw upon the Liquidity Facility (1) in the event the Remarketing Agent for the 2008 Certificates notifies the Trustee as provided herein that any of the 2008 Certificates have not been remarketed on or before the Purchase Date therefor, which draw shall be in an amount equal to the difference between such Purchase Price and any remarketing proceeds received by the Remarketing Agent in connection with a partial remarketing of such 2008 Certificates, or (2) if no such notice is received, the entire amount of the Purchase Price, and to remit the amount so drawn to or upon the order of the Securities Depository for the benefit of the tendering Beneficial Owners;

(B) remit any proceeds derived from the remarketing of a Liquidity Facility Certificate to the applicable Liquidity Facility Provider; and

(C) remit any funds deposited by the Authority for the payment of the Purchase Price of tendered 2008 Certificates to the Securities Depository for the benefit of the tendering Beneficial Owners.

(iv) If the Trustee is party to a custodian or custody agreement with the Liquidity Provider with respect to Liquidity Provider Certificates, the Trustee in its capacity as custodian for the Liquidity Provider shall hold and release Liquidity Provider Certificates in accordance with the terms of such agreement.

Section 3.07. Tender Provisions Applicable Upon Discontinuation of Book-Entry System. If at any time the 2008 Certificates shall no longer be in the Book-Entry System, the procedures set forth below shall apply.

(a) Each 2008 Certificate shall be delivered (with all necessary endorsements) at or before 12:00 noon New York City time on the Purchase Date at the corporate trust office of the Trustee; provided, however, that payment of the Purchase Price shall be made pursuant to this Section 3.07(a) only if the 2008 Certificate so delivered to the Trustee conforms in all respects to the description thereof in the notice provided pursuant to Section 3.01 or Section 3.02 hereof, as applicable. Payment of the Purchase Price with respect to purchases pursuant to the provisions set forth in this Section shall be made to the Owners of tendered 2008 Certificates by wire transfer in immediately available funds by the Trustee by 3:00 p.m. New York City time on the Purchase Date.

(b) The Trustee shall hold all 2008 Certificates properly tendered to it for purchase hereunder as agent and bailee of, and in escrow for the benefit of, the respective Owners of the 2008 Certificates that shall have so tendered such 2008 Certificates until moneys representing the Purchase Price of such 2008 Certificates shall have been delivered to or for the account of or to the order of such Owners.

(c) If a 2008 Certificate to be purchased is not delivered by the Owner to the Trustee by 12:00 noon New York City time on the date in which such 2008 Certificate is to be purchased, the provisions set forth in Section 3.08 hereof shall apply.

(d) If the Trustee is party to a custodian or custody agreement with the Liquidity Provider with respect to Liquidity Provider Certificates, the Trustee in its capacity as custodian for the Liquidity Provider shall hold and release Liquidity Provider Certificates in accordance with the terms of such agreement.

Section 3.08. Certificates Deemed Purchased. If funds sufficient to pay the Purchase Price of any Certificate are held by the Trustee on any Purchase Date, such 2008 Certificate shall be deemed to have been purchased and shall be purchased according to the terms hereof, for all purposes of this Trust Agreement, irrespective of whether or not such 2008 Certificate shall have been delivered to the Trustee, and neither the former Owner of such 2008 Certificate nor any other person shall have any claim thereon, under this Trust Agreement or otherwise, for any amount other than the Purchase Price thereof.

In the event any 2008 Certificate purchased according to the terms hereof shall not be presented to the Trustee, the Trustee shall segregate and hold uninvested the moneys for the

Purchase Price of such 2008 Certificate in trust, without liability for interest thereon, for the benefit of the former Owners of such 2008 Certificate, who shall, except as provided in the following sentence, thereafter be restricted exclusively to such moneys for the satisfaction of any claim for the Purchase Price of such 2008 Certificate. Any moneys which the Trustee shall segregate and hold in trust for the payment of the Purchase Price of any 2008 Certificate and remaining unclaimed for two (2) years after the date of purchase shall be paid to the Authority. After the payment of such unclaimed moneys to the Authority, the former Owner of such 2008 Certificate shall look only to the Authority for the payment thereof.

Section 3.09. Establishment of 2008 Purchase Fund. The Trustee shall create, establish and maintain, a separate fund to be designated as the "2008 Purchase Fund" (the "2008 Purchase Fund"). Moneys deposited in the 2008 Purchase Fund shall be kept separate from and not commingled with other moneys deposited hereunder or with any other moneys of the Authority. The Trustee shall further create, establish and maintain separate accounts within the 2008 Purchase Fund, such separate account to be designated as the "Remarketing Proceeds Account," the "Liquidity Facility Account" and the and the "Authority Account." The 2008 Purchase Fund shall be held in trust solely for the benefit of the Owners of tendered 2008 Certificates and the Trustee shall not have any interest in, claim on or right to, any accounts within the 2008 Purchase Fund or the 2008 Purchase Fund.

(a) Remarketing Proceeds Account. Upon receipt of the proceeds of a remarketing of any 2008 Certificate on the date such 2008 Certificate is to be purchased, the Trustee shall deposit such remarketing proceeds in the Remarketing Proceeds Account, such remarketing proceeds to be applied to the payment of the Purchase Price of such 2008 Certificate. The Authority shall not have any right, title or interest in any of the funds held on deposit in any Remarketing Proceeds Account nor any remarketing proceeds held for any period of time by any Remarketing Agent.

(b) Liquidity Facility Account. Upon receipt of the proceeds of a draw on a Liquidity Facility, the Trustee shall deposit such Liquidity Facility proceeds in the applicable Liquidity Facility Account, such Liquidity Facility proceeds to be applied to the payment of the Purchase Price of the 2008 Certificates to the extent that the moneys on deposit in the Remarketing Proceeds Account shall not be sufficient. Any amounts deposited in a Liquidity Facility Account and not needed for the payment of the Purchase Price of the 2008 Certificates shall be immediately returned to the applicable Liquidity Facility Provider.

(c) Authority Account. Upon receipt of funds from the Authority provided at its sole discretion pursuant to Section 3.04(c) hereof, the Trustee shall deposit such funds in the Authority Account, such funds to be applied to the payment of the Purchase Price of the 2008 Certificates. Any amounts deposited in an Authority Account and not needed for the payment of the Purchase Price of the 2008 Certificates shall be immediately returned to the Authority.

(d) Investment of Funds on Deposit in the 2008 Purchase Funds. Amounts held in the Remarketing Proceeds Account, the Liquidity Facility Account and the

Authority Account shall not be commingled with any other funds held by the Trustee and shall be held uninvested.

(e) Eligible Accounts. Each of the Remarketing Proceeds Account and the Liquidity Facility Account shall meet the requirements of an Eligible Account and be held in the name of the Trustee for the benefit of the Owners. In the event the Remarketing Proceeds Account or the Liquidity Facility Account no longer meet the requirements of an Eligible Account, the Trustee shall promptly (and, in any case, within not more than 30 calendar days) move such account to another financial institution such that each account will meet the requirements of an Eligible Account.

Section 3.10. Insufficient Funds for Tenders; Delayed Remarketing Period.

(a) If sufficient funds are not available to pay the Purchase Price of all tendered 2008 Certificates to be purchased on any Purchase Date (such 2008 Certificates being hereinafter referred to as the "Tendered Certificates"): (i) no purchase of such Tendered Certificates shall be consummated on such Purchase Date; (ii) all such Tendered Certificates shall be returned to the Owners thereof; (iii) all remarketing proceeds shall be returned to the applicable Remarketing Agent for return to the persons providing such moneys; and (iv) such insufficiency and the failure to pay the Purchase Price on any Payment Date shall not constitute an Event of Default under this Trust Agreement.

(b) All such Tendered Certificates shall evidence interest at the Maximum Rate during the period of time (such period of time being hereinafter referred to as a "Delayed Remarketing Period") from and including the applicable Purchase Date to (but not including) the date that all such Tendered Certificates are successfully remarketed.

(c) The Authority may direct the conversion of such Tendered Certificates to a different Mode during a Delayed Remarketing Period in accordance with Section 2.18 hereof; provided that the Authority shall not be required to comply with the notice requirements described in Section 2.18 hereof.

(d) During a Delayed Remarketing Period, the Remarketing Agent shall continue to use its best efforts to remarket such Tendered Certificates. Once the Remarketing Agent has advised the Trustee that it has a good faith belief that it is able to remarket all of such Tendered Certificates, the Trustee shall give written notice by mail to the Owners of such Tendered Certificates not later than five (5) Business Days prior to the proposed Purchase Date, which notice shall state: (i) that such Tendered Certificates will be subject to mandatory tender for purchase on the proposed Purchase Date; (ii) the proposed Purchase Date; (iii) the Mode applicable to such Tendered Certificates from and after the proposed Purchase Date; (iv) the procedures for such mandatory tender for purchase; (v) the Purchase Price applicable to such Tendered Certificates; and (vi) the consequences of a failed remarketing.

(e) During a Delayed Remarketing Period, the Trustee may, upon direction of the Authority, apply amounts on deposit in the 2008 Prepayment Subaccount of the 2008 Principal Account to the prepayment of such Tendered Certificates, as a whole or in part on any Business Day during such Delayed Remarketing Period, at a prepayment price equal to the principal

amount thereof, together with interest accrued thereon to the date fixed for prepayment, without premium. Notwithstanding any provisions herein to the contrary, the Trustee shall give five (5) Business Days' notice of such prepayment to the Owners of the 2008 Certificates to be prepaid.

(f) During a Delayed Remarketing Period, interest on such Tendered Certificates shall be paid to the Owners thereof (i) on the first Business Day of each calendar month occurring during such Delayed Remarketing Period and (ii) on the day after the last day of such Delayed Remarketing Period.

Section 3.11. Liquidity Facility; Alternate Liquidity Facility.

(a) The Authority shall provide a Liquidity Facility approved by the 2008 Certificate Insurer for the 2008 Certificates in a Daily Mode, a Weekly Mode, a Flexible Mode and in a Term Rate Mode. Each such Liquidity Facility (and any Alternate Liquidity Facility provided in replacement thereof) shall provide for the purchase of the 2008 Certificates upon their optional or mandatory tender in accordance with Section 3.01 and Section 3.02 hereof. Any Liquidity Facility (or Alternate Liquidity Facility) shall be a facility provided by a Liquidity Facility Provider in an amount equal to the Required Stated Amount.

(b) If a Liquidity Facility is in effect with respect to the 2008 Certificates, on each date on which a 2008 Certificate is to be purchased, the Trustee, by demand given by Electronic means before 12:30 p.m. New York City time, shall draw on the applicable Liquidity Facility in accordance with the terms thereof so as to receive thereunder by 2:30 p.m. New York City time on such date an amount, in immediately available funds, sufficient, together with the proceeds of the remarketing of such 2008 Certificates on such date, to enable the Trustee to pay the Purchase Price in connection therewith. The proceeds of such draw shall be paid to the Trustee, who shall deposit said proceeds in the applicable Liquidity Facility Account pursuant to Section 3.09(b) hereof or, in the case of the Replacement Liquidity Facility, the 2008 Liquidity Facility Payment Account.

(c) If the Authority shall have delivered a Liquidity Facility to the Trustee in accordance with subsection (a) of this Section, the Authority: (i) shall maintain such Liquidity Facility or an Alternate Liquidity Facility, in an amount equal to the Required Stated Amount prior to its termination; and (ii) shall not voluntarily terminate such Liquidity Facility or any Alternate Liquidity Facility without providing at least 30 days written notice to the Trustee and each of the other Notice Parties.

(d) The Authority may provide an Alternate Liquidity Facility approved by the 2008 Certificate Insurer with respect to the 2008 Certificates on any Business Day not later than the 5<sup>th</sup> Business Day prior to the Expiration Date of the Liquidity Facility then in effect for the 2008 Certificates. The Authority shall give at least 30 days' written notice to the Trustee and each of the Notice Parties of its intent to furnish an Alternate Liquidity Facility to the Trustee, which notice shall specify the nature of such Liquidity Facility, the identity of the Liquidity Facility Provider and the proposed Substitution Date. The Trustee shall give notice of each Mandatory Purchase Date resulting from the proposed delivery of an Alternate Liquidity Facility in accordance with the provisions set forth in Section 3.02 hereof.

(e) On or before the Substitution Date, there shall be delivered to the Trustee: (i) the Alternate Liquidity Facility in substitution for the Liquidity Facility then in effect, (ii) a Favorable Opinion of Special Counsel which shall also be filed with the 2008 Certificate Insurer and (iii) a written Opinion of Counsel for the provider of Alternate Liquidity Facility to the effect that such Alternate Liquidity Facility is a legal, valid, and binding obligation of the provider thereof and covering such other matters as the Authority shall require. Upon the satisfaction of the conditions described in the preceding sentence, the Trustee shall accept such Alternate Liquidity Facility and shall surrender the Liquidity Facility then in effect to the provider thereof on the Substitution Date; provided, however, that if there are insufficient remarketing proceeds to pay the Purchase Price of all 2008 Certificates subject to mandatory purchase on such Substitution Date, the Trustee shall not surrender the Liquidity Facility then in effect until the Trustee shall have drawn upon the existing Liquidity Facility to pay the Purchase Price for the 2008 Certificates subject to mandatory purchase on such Substitution Date. Notwithstanding any other provision of this Trust Agreement to the contrary, if any condition precedent to the substitution of an Alternate Liquidity Facility is not satisfied, the substitution shall not occur but the affected 2008 Certificates shall remain subject to mandatory purchase on the proposed Substitution Date.

(f) In addition to the notice provided pursuant to Section 3.11(d) hereof, the Trustee shall give written notice to the Owners of the 2008 Certificates and each of the Notice Parties of the extension of the Expiration Date of any Liquidity Facility, such notice to be given by mail as promptly as possible upon receipt by the Trustee of notification of such extension.

#### Section 3.12. Appointment of Remarketing Agent.

(a) While the 2008 Certificates are in a Mode which requires the appointment of a Remarketing Agent, the Authority shall appoint a Remarketing Agent for the 2008 Certificates. Any Remarketing Agent shall be approved by the 2008 Certificate Insurer, shall be a member of the National Association of Securities Dealers, Inc., shall have a capitalization of at least \$50,000,000 and shall be authorized by law to perform all the duties set forth herein.

(b) By acceptance of appointment as Remarketing Agent for the 2008 Certificates, the Remarketing Agent shall be deemed to have agreed: (i) to remarket the 2008 Certificates in accordance with the provisions set forth herein; (ii) to keep such books and records as shall be consistent with prudent industry practice; and (iii) to make such books and records available for inspection by each of the Notice Parties at all reasonable times.

(c) The Remarketing Agent may at any time resign and be discharged of the duties and obligations created herein as set forth in the Remarketing Agreement entered into by such Remarketing Agent and the Authority. The Remarketing Agent may suspend its remarketing efforts in accordance with the provisions set forth in Remarketing Agreement entered into by the Remarketing Agent and the Authority. The Remarketing Agent may be removed at any time, at the direction of the Authority in accordance with the provisions set forth in the Remarketing Agreement entered into by the Remarketing Agent and the Authority. The Authority shall provide written notice to each of the Notice Parties of the appointment of any successor Remarketing Agent.

(d) If the Remarketing Agent consolidates with, merges or converts into, or transfers all or substantially all of its assets, to another entity meeting the requirements specified in subparagraph (a) above, the resulting, surviving or transferee entity shall be the successor Remarketing Agent without any further act.

### Section 3.13. Duties of Remarketing Agent.

(a) Each Remarketing Agent shall use its best efforts to offer for sale at the par amount thereof: (i) all 2008 Certificates (or portions thereof to be remarketed) for which notice of optional tender pursuant to Section 3.01 hereof has been given; (ii) all 2008 Certificates that are required to be purchased (A) on a Mandatory Purchase Date described in clauses (i), (ii), (iii), (iv) or (vii) of the definition of Mandatory Purchase Date set forth in Section 1.01 hereof and (B) on a Mandatory Purchase Date described in clause (v) of the definition of Mandatory Purchase Date set forth in Section 1.01 hereof if no Liquidity Facility is required to be delivered by the Authority in connection with such Mandatory Purchase Date; and (iii) all Liquidity Facility Certificates that are: (A) purchased on a Purchase Date described above in clause (i) or (ii) of this Section 3.13, (B) with respect to which the Liquidity Facility Provider has provided notice that it is ready to reinstate the Available Amount, such notice to have been provided to the Authority, the Trustee and the Remarketing Agent, (C) with respect to which an Alternate Liquidity Facility is in effect, or (D) which are being marketed as Fixed Rate Certificates (if the Remarketing Agent shall have been engaged to be the Fixed Rate Remarketing Agent).

If a notice of prepayment or a notice of mandatory purchase shall have been given with respect to a 2008 Certificate, the Remarketing Agent shall provide a copy of such notice to each Person to which such Certificate is remarketed.

Notwithstanding any provision of this Trust Agreement to the contrary, if there shall have occurred and be continuing (i) a Control Event and no other Credit Enhancement Provider Failure or Liquidity Facility Provider Failure, the Remarketing Agent shall continue remarketing 2008 Certificates or (ii) a Control Event and either another Credit Enhancement Provider Failure or a Liquidity Facility Provider Failure, the Remarketing Agent shall not be required to remarket 2008 Certificates.

## ARTICLE IV

### 2008 PAYMENTS; 2008 PROJECT

Section 4.01. 2008 Payments Held in Trust. The 2008 Payments shall be held in trust by the Trustee for the benefit of the Owners from time to time of the 2008 Certificates and each Credit Enhancement Provider, but shall nonetheless be disbursed, allocated and applied solely for the uses and purposes provided herein.

Section 4.02. Deposit of 2008 Payments. The Trustee hereby agrees to establish, maintain and hold in trust a separate fund designated as the 2008 Debt Service Fund, for so long as any 2008 Certificates shall be Outstanding hereunder. All 2008 Payments (except as otherwise provided) received by the Trustee shall be immediately deposited in the 2008 Debt Service Fund and shall be disbursed and applied only as hereinafter provided.

Section 4.03. Establishment and Maintenance of Accounts for Use of Money in the 2008 Debt Service Fund. All money in the 2008 Debt Service Fund shall be set aside by the Trustee in the following respective special accounts within the 2008 Debt Service Fund (each of which is hereby created and each of which the Trustee hereby agrees and covenants to maintain) in the following order of priority:

- (a) 2008 Interest Account (with a 2008 Fees Subaccount therein), and
- (b) 2008 Principal Account (with a 2008 Prepayment Subaccount and a 2008 Sinking Fund Subaccount therein).

All money in each of such accounts and subaccounts shall be held in trust by the Trustee for the benefit of the Owners and each Credit Enhancement Provider and shall be applied, used and withdrawn only for the purposes hereinafter authorized in this Section.

(a) 2008 Interest Account. On the Delivery Date, the Trustee shall deposit in the 2008 Interest Account any Payment Agreement Receipts relating to the 2008 Interest Rate Swap Agreement which the City has directed under the 2008 Interest Rate Swap Agreement to be transferred to the Trustee for deposit in the 2008 Interest Account and any amounts transferred to the Trustee pursuant to Section 2.03 of the 2008 Supplemental Contract for the payment of payments due under the 2008 Interest Rate Swap Agreement. On the Business Day immediately preceding each Interest Payment Date, the Trustee shall set aside from the 2008 Debt Service Fund and deposit in the 2008 Interest Account that amount of money which is equal to the amount of interest evidenced and represented by the 2008 Certificates becoming due and payable on each such Interest Payment Date, unless such amounts are required to be used to reimburse the Bank pursuant to clause (c) below. The Trustee will also apply amounts on deposit in the 2008 Fees Subaccount to pay on behalf of the City, the Payment Agreement Payments required to be paid under the 2008 Interest Rate Swap Agreement and to pay the Remarketing Agent fees as the same shall become due on each due date therefor until such 2008 Fees Subaccount shall be depleted (expected to be on or about November 29, 2008). Investment earnings on amounts on deposit in the 2008 Fees Subaccount shall be transferred to the City for deposit in the Revenue Fund.

No deposit need be made in the 2008 Interest Account if the amount contained therein (exclusive of amounts transferred for the payment of amounts due under the 2008 Interest Rate Swap Agreement) is at least equal to the aggregate amount of interest evidenced and represented by the 2008 Certificates becoming due and payable on such Interest Payment Date.

Except as otherwise provided herein, all money in the 2008 Interest Account shall be used and withdrawn by the Trustee solely for the purpose of paying the interest (including accrued interest evidenced and represented by any 2008 Certificates purchased or prepaid prior to their respective Certificate Payment Date) with respect to the 2008 Certificates as it shall become due and payable, or for reimbursing the Bank and paying the Payment Agreement Payments due under the 2008 Interest Rate Swap Agreement as they shall become due and payable. The Trustee shall be under no obligation to calculate the amount of Payment Agreement Payments due under the 2008 Interest Rate Swap Agreement and shall be entitled to

rely conclusively on the information received by it with respect to the amount of the Payment Agreement Payments due and owing by the City.

(b) 2008 Principal Account. On the Business Day immediately preceding each October 1, commencing on October 1, 2008, the Trustee shall set aside from the 2008 Debt Service Fund and deposit in the 2008 Principal Subaccount an amount of money equal to the principal amount evidenced and represented by the Outstanding Serial Certificates with a Certificate Payment Date of such October 1, and in the 2008 Sinking Fund Subaccount in the 2008 Principal Account the amount of all Sinking Fund Payments required to be made on such October 1.

Amounts to be applied to the optional prepayment of the principal component of the 2008 Certificates pursuant to Section 2.03(c) hereof shall be deposited in the 2008 Prepayment Subaccount of the 2008 Principal Account.

No deposit need be made in the 2008 Principal Account if the amount contained therein is at least equal to the aggregate amount of the principal evidenced and represented by the Outstanding Serial Certificates with a Certificate Payment Date of such October 1 and the amount contained in the 2008 Sinking Fund Subaccount therein is at least equal to the aggregate amount of all Sinking Fund Payments required to be made on such October 1.

All money in the 2008 Principal Account shall be used and withdrawn by the Trustee solely for the purpose of paying the principal evidenced and represented by the Serial Certificates as they shall become due and payable, whether at their respective Certificate Payment Dates or on prior prepayment, and all money in the 2008 Sinking Fund Subaccount of the 2008 Principal Account shall be used and withdrawn by the Trustee only to purchase or to prepay or to pay Term Certificates, and with respect to the 2008 Sinking Fund Subaccount, on each Sinking Fund Payment date, the Trustee shall apply the Sinking Fund Payment required on that date to the prepayment (or payment at Certificate Payment Date, as the case may be) of the Term Certificates upon the notice and in the manner provided in Article II; provided, that at any time prior to giving such notice of such prepayment, the Trustee may, upon the Written Request of the Authority and receipt of moneys sufficient therefor, purchase for cancellation Term Certificates in accordance with Section 2.03(a) hereof, and provided further that so long as the Liquidity Facility is in place, amounts in the 2008 Principal Account shall be used as provided in clause (c) below.

(c) Notwithstanding anything herein to the contrary, all monies in the 2008 Debt Service Fund, including the 2008 Interest Account and the 2008 Principal Account, shall be used to reimburse any draws on the Liquidity Facility pursuant to Section 4.08 hereof.

Section 4.04. Parity Reserve Fund. The Parity Reserve Fund created pursuant to Section 3.04 of the 1997 Trust Agreement is hereby continued. The Trustee hereby agrees and covenants to maintain the Parity Reserve Fund so long as the Contract has not been discharged in accordance with its terms or any 2008 Certificates remain Outstanding hereunder. Amounts on deposit in the Parity Reserve Fund are pledged to the payment of the 1997 Certificates, the 2008 Certificates (including Liquidity Provider Certificates and Subrogated Certificates) and any other obligations hereafter issued in connection with a Supplemental Contract and shall be applied

only for such purposes as hereinafter provided. The Trustee shall deposit in the Parity Reserve Fund from the proceeds of the 2008 Certificates, the amount specified in Section 2.12, such amount being sufficient to cause the balance on deposit in or credited to the Parity Reserve Fund, to be equal to the Reserve Fund Requirement upon delivery of the 2008 Certificates. The Trustee shall deposit in the Parity Reserve Fund such other amounts transferred to the Trustee by the City pursuant to Section 2.04(b)(2) of the Contract, as directed by the Authority in a Written Request of the Authority. Moneys on deposit in the Parity Reserve Fund shall be transferred by the Trustee to the 2008 Debt Service Fund to pay principal and interest evidenced and represented by the 2008 Certificates on any Interest Payment Date or to reimburse the Liquidity Facility Provider for any unreimbursed drawing made under the Liquidity Facility to pay such principal and interest on any such Interest Payment Date in the event amounts on deposit therein are insufficient for such purposes. The Trustee shall also, from such amounts on deposit in the Parity Reserve Fund, transfer or cause to be transferred to any applicable debt service fund established under the 1997 Trust Agreement and under any other trust agreement under which any obligations are issued in connection with a Supplemental Contract, without preference or priority between transfers made pursuant to this sentence and the preceding sentence, and in the event of any insufficiency of such moneys ratably without discrimination or preference, that sum or sums, if any, equal to the amount required to be deposited therein pursuant to such trust agreement under which any obligations are issued in connection with a Supplemental Contract. All investments in the Parity Reserve Fund shall (notwithstanding anything in the 1997 Trust Agreement to the contrary) be valued on or before October 1 of each year at the lesser of the cost or market value thereof. Following such valuation, any moneys on deposit in the Parity Reserve Fund representing an excess of the Reserve Fund Requirement will be transferred by the Trustee to the City for deposit in the Revenue Fund. The Trustee may create such subaccounts in the Parity Reserve Fund as may be necessary or convenient for the purposes of this Section 4.04.

The Reserve Fund Requirement may be provided by one or more surety bonds, insurance policies, or letters of credit as described in the definition of Reserve Fund Requirement ("Reserve Funding Instruments") set forth in the Contract.

Notwithstanding anything to the contrary contained in this Trust Agreement, at any time one or more Reserve Funding Instruments are on deposit in the Parity Reserve Fund, the Trustee shall: (i) withdraw and use all cash, if any, on deposit in the Parity Reserve Fund prior to using and withdrawing any amounts derived from payments under any Reserve Funding Instruments; and (ii) draw on all Reserve Funding Instruments on a pro rata basis based on the draw limit of each Reserve Funding Instrument. Amounts received by the Trustee from the City pursuant to Section 2.04(c)(2) of the Master Contract as a replenishment of amounts withdrawn from the Parity Reserve Fund shall be applied (i) first on a pro rata basis to reimburse draws on any Reserve Funding Instruments and (ii) to replenish cash withdrawn from the Parity Reserve Fund.

In the event the 2008 Certificate Insurance Policy is cancelled in accordance with the Reimbursement Agreement between the Bank and the City, any Reserve Funding Instrument provided by the 2008 Certificate Insurer will be cancelled concurrently therewith.

Section 4.05. Establishment and Application of Costs of Issuance Fund. The Trustee hereby agrees to establish, maintain and hold in trust a separate fund designated as the Costs of Issuance Fund, which fund is hereby created and which fund the Authority hereby agrees to

maintain with the Trustee until November 29, 2008. The Trustee shall deposit to the Costs of Issuance Fund the amounts specified in Section 2.12 hereof. All money in the Costs of Issuance Fund shall be used and withdrawn by the Trustee to pay the Costs of Issuance relating to the 2008 Certificates upon receipt of a Written Request of the Authority filed with the Trustee, each of which shall be sequentially numbered and shall state the person to whom payment is to be made, the amount to be paid, the purpose for which the obligation was incurred and that such payment is a proper charge against said fund. On November 29, 2008, or upon the earlier Written Request of the Authority, any remaining balance in the Costs of Issuance Fund shall be transferred to the City for deposit in the 2008 Debt Service Fund.

Section 4.06. Deposit and Investments of Money in Accounts and Funds. All money held by the Trustee in any of the accounts or funds established pursuant hereto shall be invested in Permitted Investments at the Written Request of the Authority filed with the Trustee which such Permitted Investments shall, as nearly as practicable, mature on or before the dates on which such money is anticipated to be needed for disbursement hereunder, and the Trustee shall have no liability or responsibility for any loss resulting from any investment made in accordance herewith; provided, that if no such Written Request is received by the Trustee, the Trustee shall invest such money in those Permitted Investments described in clause (9) of the definition thereof provided, however, that any such investment shall be made by the Trustee only if, prior to the date on which such investment is to be made, the Trustee shall have received a Written Request of the Authority specifying a specific money market fund and, if no such Written Request of the Authority is so received, the Trustee shall hold such moneys uninvested. Except as otherwise provided herein with respect to the Parity Reserve Fund, all interest or profits received on any money so invested shall be deposited in the 2008 Debt Service Fund.

The Authority acknowledges that to the extent regulations of the Comptroller of the Currency or other applicable regulatory entity grant the Authority the right to receive brokerage confirmations of security transactions as they occur, the Authority specifically waives receipt of such confirmations to the extent permitted by law. The Trustee will furnish the Authority periodic cash transaction statements which include detail for all investment transactions made by the Trustee hereunder.

The Trustee or any of its affiliates may act as principal or agent, sponsor, advisor or manager in connection with any investments made by the Trustee hereunder. For investment purposes, the Trustee may commingle the funds and accounts established hereunder, but shall account for each separately.

The Trustee shall not be liable for any loss from any Permitted Investment acquired, held, or disposed of at the written request of the Authority. Any Permitted Investments that are registered securities shall be registered in the name of the Trustee.

Section 4.07. Assignment to Trustee; Enforcement of Obligations.

(a) The Authority hereby transfers, assigns and sets over to the Trustee all of the 2008 Payments and any and all rights and privileges it has under the Contract, including, without limitation, the right to collect and receive directly all of the 2008 Payments, and any 2008 Payments collected or received by the Authority shall be deemed to be held, and to have been

collected or received, by the Authority as the agent of the Trustee, and shall forthwith be paid by the Authority to the Trustee.

The Trustee also shall, subject to the provisions of the Trust Agreement, take all steps, actions and proceedings required to be taken as provided in any Opinion of Counsel delivered to it, reasonably necessary to maintain in force for the benefit of the Owners of the 2008 Certificates and each Credit Enhancement Provider the Trustee's rights in and priority to the following security granted to it for the payment of the 2008 Certificates: the Trustee's rights as assignee of the 2008 Payments under the Contract and as beneficiary of any other rights to security for the 2008 Certificates which the Trustee may receive in the future.

(b) The Trustee may, in performing the obligations set out in Section 4.07(a) above, rely and shall be protected in acting or refraining from acting upon an Opinion of Counsel furnished by the City.

Section 4.08. 2008 Liquidity Facility Payment Account; Payment of Principal and Interest and Mandatory Purchase Price of the 2008 Certificates. The Trustee shall establish and maintain a separate fund known as the "2008 Liquidity Facility Payment Account" and shall, (i) in each Business Day preceding each Interest Payment Date of the 2008 Certificates, before 5:00 P.M. New York City time on such day, draw on the Liquidity Facility in accordance with the terms thereof so as to receive by 1:00 P.M. New York City time on said Interest Payment Date, an amount, in immediately available funds, equal to the amount of interest and principal, if any (including any Sinking Fund Payment) due on such date, payable with respect to the 2008 Certificates on such Interest Payment Date, and (ii) on each Mandatory Purchase Date, before 12:00 P.M. New York City time draw on the Liquidity Facility in accordance with the terms thereof so as to receive by 3:00 P.M. New York City time on said Interest Payment Date, an amount, in immediately available funds, equal to the amount of the interest and principal due on such date, payable with respect to the 2008 Certificates. All monies held in the 2008 Liquidity Facility Account shall be held uninvested in trust for the benefit of the Owners of the 2008 Certificates.

Funds for the payment of interest and principal, if any, payable with respect to the 2008 Certificates on such Interest Payment Date or Mandatory Purchase Date shall be derived from the immediately available funds on deposit in the 2008 Liquidity Facility Payment Account received from the Bank from draws under the Liquidity Facility, and not from amounts on deposit in the 2008 Interest Account, the 2008 Principal Account or any other account established hereunder. The Liquidity Facility Provider will be reimbursed from such draws from amounts on deposit in the 2008 Interest Account, the 2008 Principal Account or, in the case of a Mandatory Purchase Date, amounts in the Remarketing Account, if any.

If the Liquidity Facility Provider shall make a payment under the Liquidity Facility and is not reimbursed by the Trustee from amounts on deposit in the 2008 Interest Account or 2008 Principal Account or Parity Reserve Fund, its rights with respect to the 2008 Certificates so paid or interest thereon so paid shall be as set forth in Section 10.05 hereof, including its rights to demand payment of such amounts under the 2008 Certificate Insurance Policy. If the Liquidity Facility Provider fails to pay under the Liquidity Facility upon the presentation of a proper draw request by the Trustee and the City has not defaulted under the related Reimbursement

Agreement, to the extent available, amounts on deposit in the 2008 Interest Account, the 2008 Principal Account and the Parity Reserve Fund will be applied to the payment of regularly scheduled interest and principal payable on the applicable Interest Payment Date with respect to the 2008 Certificates.

## ARTICLE V

### COVENANTS OF THE AUTHORITY AND THE TRUSTEE

Section 5.01. Compliance with Trust Agreement. The Trustee will not execute or deliver any 2008 Certificates in any manner other than in accordance with the provisions hereby; and the Authority will not suffer or permit any default by it to occur hereunder, but will faithfully comply with, keep, observe and perform all the agreements and covenants to be observed or performed by it contained herein and in the 2008 Certificates.

Section 5.02. Observance of Laws and Regulations. The Authority and the Trustee will faithfully comply with, keep, observe and perform all valid and lawful obligations or regulations now or hereafter imposed on them by contract, or prescribed by any law of the United States of America or of the State of California, or by any officer, board or commission having jurisdiction or control, as a condition of the continued enjoyment of each and every franchise, right or privilege now owned or hereafter acquired by them, including their right to exist and carry on their respective businesses, to the end that such franchises, rights and privileges shall be maintained and preserved and shall not become abandoned, forfeited or in any manner impaired.

Section 5.03. Accounting Records and Reports. The Trustee will keep or cause to be kept proper books of record and accounts in which complete and correct entries shall be made of all transactions made by the Trustee relating to the receipts, disbursements, allocation and application of the 2008 Payments and the proceeds of the 2008 Certificates, and such books shall be available for inspection by the Authority, at reasonable hours and under reasonable conditions. Not more than 180 days after the close of each Fiscal Year, the Trustee shall furnish or cause to be furnished to the Authority and the 2008 Certificate Insurer a complete financial statement covering receipts, disbursements, allocation and application of 2008 Payments received by the Trustee for such Fiscal Year. The Authority shall keep or cause to be kept such information as required under the Tax Certificate.

Section 5.04. Prosecution and Defense of Suits. The Authority will defend against every suit, action or proceeding at any time brought against the Trustee upon any claim to the extent arising out of the receipt, application or disbursement of any of the 2008 Payments and the proceeds of the 2008 Certificates or to the extent involving the failure of the Authority to fulfill its obligations hereunder; provided that the Trustee or any affected Owner at its election may appear in and defend any such suit, action or proceeding. The Authority will indemnify and hold harmless the Trustee against any and all liability claimed or asserted by any person to the extent arising out of such failure by the Authority, and will indemnify and hold harmless the Trustee against any attorney's fees or other expenses which it may incur in connection with any litigation to which it may become a party by reason of its actions hereunder, except for any loss, cost, damage or expense resulting from the active or passive negligence, willful misconduct or breach of duty by the Trustee. Notwithstanding any contrary provision hereof, this covenant shall

remain in full force and effect even though all 2008 Certificates secured hereby may have been fully paid and satisfied.

Section 5.05. Amendments to Contract. Except for any Supplemental Contract delivered in accordance with the terms of the Contract, the Authority shall not supplement, amend, modify or terminate any of the terms of the Contract, or consent to any such supplement, amendment, modification or termination, without the prior written consent of the Trustee, which such consent shall be given only if (a) such supplement, amendment, modification or termination will not materially adversely affect the interests of the Owners or result in any material impairment of the security hereby given for the payment of the 2008 Certificates, or (b) the Trustee first obtains the written consent of the Owners of a majority in aggregate principal amount evidenced and represented by the 2008 Certificates then Outstanding to such supplement, amendment, modification or termination; provided, that no such supplement, amendment, modification or termination shall reduce the amount of 2008 Payments to be made to the Authority or the Trustee by the City pursuant to the Contract, or extend the time for making such 2008 Payments in any manner that would require the amendment of the Trust Agreement in any manner not in compliance with Section 7.01 hereof, or permit the creation of any lien prior to or on a parity with the lien created hereby on the 2008 Payments without the written consent of all of the Owners of the 2008 Certificates then Outstanding.

Section 5.06. Recording and Filing. The Trustee upon receipt of a Written Request of the Authority, at the expense of the Authority, shall file, record, register, renew, refile and rerecord all such documents, including financing statements (or continuation statements in connection therewith), all in such manner, at such times and in such places as may be required and to the extent permitted by law in order to fully perfect, preserve and protect the security of the Owners and the rights and interests of the Trustee; provided, however, that the Trustee will not be required to execute a special or general consent to service of process, or to qualify as a foreign corporation in connection with any such filing, recording, registration, refile or rerecording in any jurisdiction in which it is not now so subject.

Section 5.07. Further Assurances. Whenever and so often as reasonably requested to do so by the Trustee or any Owner, the Authority will promptly execute and deliver or cause to be executed and delivered all such other and further assurances, documents or instruments, and promptly do or cause to be done all such other and further things as may be necessary or reasonably required in order to further and more fully vest in the Trustee and the Owners all rights, interests, powers, benefits, privileges and advantages conferred or intended to be conferred upon them hereby.

## ARTICLE VI

### THE TRUSTEE

#### Section 6.01. The Trustee.

(a) The Bank of New York Mellon Trust Company, N.A., shall serve as the Trustee for the purpose of receiving all money which the Authority is required to deposit with the Trustee hereunder and for the purpose of allocating, applying and using such money as provided

herein and for the purpose of paying the interest and principal and prepayment premiums, if any, evidenced and represented by the 2008 Certificates presented for payment, and for the purpose of canceling all paid or prepaid 2008 Certificates as provided herein. The Authority agrees that it will at all times maintain a Trustee having a corporate trust office in either San Francisco, California or Los Angeles, California.

(b) The Authority may at any time, unless there exists any Event of Default as defined in Section 8.01 hereof, remove the Trustee initially appointed and any successor thereto and may appoint a successor or successors thereto by an instrument in writing; provided that any successor appointed under this Trust Agreement shall be approved by the 2008 Certificate Insurer and shall be a bank, national banking association with trust powers or trust company doing business and having a principal office in either San Francisco, California or Los Angeles, California, having (or if such bank, national banking association or trust company is a member of a bank holding company system, its bank holding company has) a combined capital (exclusive of borrowed capital) and surplus of at least \$50,000,000 and subject to supervision or examination by federal or state authority. If such bank, national banking association or trust company publishes a report of condition at least annually, pursuant to law or to the requirements of any supervising or examining authority above referred to, then for the purpose of this Section the combined capital and surplus of such bank, national banking association or trust company shall be deemed to be its combined capital and surplus as set forth in its most recent report of condition so published. The Trustee may at any time resign by giving written notice of such resignation to the Authority and by mailing to the Owners notice of such resignation. Upon receiving such notice of resignation, the Authority shall promptly appoint a successor Trustee by an instrument in writing. Any removal or resignation of a Trustee and appointment of a successor Trustee shall become effective only upon the acceptance of appointment by the successor Trustee. If, within 30 days after notice of the removal or resignation of the Trustee no successor Trustee shall have been appointed and shall have accepted such appointment, the removed or resigning Trustee may petition any court of competent jurisdiction for the appointment of a successor Trustee, which court may thereupon, after such notice, if any, as it may deem proper and prescribe and as may be required by law, appoint a successor Trustee having the qualifications required hereby. Any successor trustee shall signify its acceptance of the duties under this Trust Agreement by an instrument in writing provided to the Authority and the Notice Parties.

(c) In the event that the Trustee breaches its obligations hereunder or under any other financing document in connection with the issuance of the 2008 Certificates, at the request of the 2008 Certificate Insurer, the Authority shall remove and replace the Trustee in accordance with the terms of the foregoing clause (b).

(d) The Trustee shall only hold the duties set forth in this Trust Agreement and no duties shall be implied against the Trustee. Following the occurrence of an Event of Default, the Trustee shall exercise such of the rights and powers vested in it hereby, and use the same degree of care and skill in their exercise, as a prudent person would exercise or use under the circumstances in the conduct of his own affairs.

Section 6.02. Liability of the Trustee.

(a) The recitals of facts, agreements and covenants herein and in the 2008 Certificates shall be taken as recitals of facts, agreements and covenants of the Authority, and the Trustee assumes no responsibility for the correctness of the same or makes any representation as to the sufficiency or validity hereof or of the 2008 Certificates, or shall incur any responsibility in respect thereof other than in connection with the rights or obligations assigned to or imposed upon it herein, in the 2008 Certificates or in law or equity. The Trustee shall not be liable in connection with the performance of its duties hereunder except for its own active or passive negligence or willful misconduct.

(b) The Trustee shall not be liable for any error of judgment made in good faith by a responsible officer, unless it shall be proved that the Trustee was negligent in ascertaining the pertinent facts.

(c) The Trustee shall not be liable with respect to any action taken or omitted to be taken by it in good faith in accordance with the direction of the Owners of not less than a majority in aggregate principal amount of the 2008 Certificates at the time Outstanding, relating to the time, method and place of conducting any proceeding for any remedy available to the Trustee, or exercising any trust or power conferred upon the Trustee hereunder.

(d) The Trustee shall be under no obligation to exercise any of the rights or powers vested in it hereby at the request, order or direction of any of the Owners pursuant to the provisions hereof unless such Owners shall have offered to the Trustee reasonable security or indemnity against the costs, expenses and liabilities that may be incurred therein or thereby. The Trustee has no obligation or liability to the Owners for the payment of interest, principal or prepayment premium, if any, evidenced and represented by the 2008 Certificates from its own funds; but rather the Trustee's obligations shall be limited to the performance of its duties hereunder.

(e) The Trustee shall not be deemed to have knowledge of any default hereunder or default under the Contract unless and until it shall have actual knowledge thereof or shall have received written notice thereof at its Corporate Trust Office. Except as otherwise expressly provided herein, the Trustee shall not be bound to ascertain or inquire as to the performance or observance of any of the terms, conditions, covenants or agreements herein or of any of the documents executed in connection with the 2008 Certificates or as to the existence of a default hereunder.

(f) The Trustee shall be entitled to advice of counsel and other professionals concerning all matters of trust and its duty hereunder, but the Trustee shall not be answerable for the professional malpractice of any attorney-at-law or certified public accountant in connection with the rendering of his professional advice in accordance with the terms hereof, if such attorney-at-law or certified public accountant was selected by the Trustee with due care.

(g) The Trustee shall not be concerned with or accountable to anyone for the subsequent use or application of any moneys which shall be released or withdrawn in accordance with the provisions hereof.

(h) Whether or not therein expressly so provided, every provision hereof or of the Contract or any related documents relating to the conduct or affecting the liability of or affording protection to the Trustee shall be subject to the provisions of this article.

(i) The Trustee makes no representation or warranty, express or implied, as to the title, value, design, compliance with specifications or legal requirements, quality, durability, operation, condition, merchantability or fitness for any particular purpose for the use contemplated by the Authority or City of the 2008 Project. In no event shall the Trustee be liable for incidental, indirect, special or consequential damages in connection with or arising from the Contract or this Trust Agreement for the existence, furnishing or use of the 2008 Project.

(j) The Trustee shall be protected in acting upon any notice, requisition, resolution, request, consent, order, certificate, facsimile transmission, electronic mail, report, opinion, bond or other paper or document believed by it to be genuine and to have been signed or presented by the proper party or parties. The Trustee may consult with counsel, who may be counsel of or to the Authority, with regard to legal questions, and the opinion of such counsel shall be full and complete authorization and protection in respect of any action taken or suffered by it hereunder in good faith and in accordance therewith.

(k) Whenever in the administration of its rights and obligations hereunder the Trustee shall deem it necessary or desirable that a matter be established or proved prior to taking or suffering any action hereunder, such matter (unless other evidence in respect thereof be herein specifically prescribed) may, in the absence of bad faith on the part of the Trustee, be deemed to be conclusively proved and established by a Certificate of the Authority, which certificate shall be full warrant to the Trustee for any action taken or suffered under the provisions hereof upon the faith thereof, but in its discretion the Trustee may in lieu thereof accept other evidence of such matter or may require such additional evidence as it may deem reasonable.

(l) No provision of this Trust Agreement shall require the Trustee to expend or risk its own funds or otherwise incur any financial liability in the performance of any of its duties hereunder, or in the exercise of its rights or powers.

(m) The Trustee shall have no responsibility, opinion or liability with respect to any information, statement or recital in any offering memorandum or other disclosure material prepared or distributed with respect to the execution and delivery of the 2008 Certificates.

(n) All immunities, indemnifications and releases from liability granted herein to the Trustee shall extend to the directors, employees, officers and agents thereof.

(o) Any company into which the Trustee may be merged or converted or with which it may be consolidated or any company resulting from any merger, conversion or consolidation to which it shall be a party or any company to which the Trustee may sell or transfer all or substantially all of its corporate trust business, so long as such company shall meet the requirements set forth in Section 6.01 hereof, shall be the successor to the Trustee and vested with all of the title to the trust estate and all of the trusts, powers, discretions, immunities, privileges and all other matters as was its predecessor, without the execution or filing of any paper or further act, anything herein to the contrary notwithstanding.

(p) The Trustee may become the owner or pledgee of any 2008 Certificates with the same rights it would have if it were not Trustee.

(q) The Trustee shall not be considered in breach of or in default in its obligations hereunder or progress in respect thereto in the event of enforced delay (“unavoidable delay”) in the performance of such obligations due to unforeseeable causes beyond its control and without its fault or negligence, including, but not limited to, acts of God or of the public enemy or terrorists, acts of a government, acts of the other party, fires, floods, epidemics, quarantine restrictions, strikes, freight embargoes, earthquakes, explosion, mob violence, riot, inability to procure or general sabotage or rationing of labor, equipment, facilities, sources of energy, material or supplies in the open market, litigation or arbitration involving a party or others relating to zoning or other governmental action or inaction pertaining to the project, malicious mischief, condemnation, and unusually severe weather or delays of suppliers or subcontractors due to such causes or any similar event and/or occurrences beyond the control of the Trustee.

(r) The Trustee agrees to accept and act upon instructions or directions pursuant to this Trust Agreement sent by unsecured e-mail, facsimile transmission or other similar unsecured electronic methods, provided, however, that, the Trustee shall have received an incumbency certificate listing persons designated to give such instructions or directions and containing specimen signatures of such designated persons, which such incumbency certificate shall be amended and replaced whenever a person is to be added or deleted from the listing. If the Authority elects to give the Trustee e-mail or facsimile instructions (or instructions by a similar electronic method) and the Trustee in its discretion elects to act upon such instructions, the Trustee’s understanding of such instructions shall be deemed controlling. The Trustee shall not be liable for any losses, costs or expenses arising directly or indirectly from the Trustee’s reliance upon and compliance with such instructions notwithstanding such instructions conflict or are inconsistent with a subsequent written instruction. The Authority agrees to assume all risks arising out of the use of such electronic methods to submit instructions and directions to the Trustee, including without limitation the risk of the Trustee acting on unauthorized instructions, and the risk of interception and misuse by third parties.

(s) The permissive right of the Trustee to do things enumerated in this Indenture shall not be construed as a duty and it shall not be answerable for other than its negligence or willful misconduct.

Section 6.03. Compensation and Indemnification of Trustee. The Authority covenants to pay to the Trustee from time to time, and the Trustee shall be entitled to, reasonable compensation for all services rendered by it in the exercise and performance of any of the powers and duties hereunder of the Trustee, and the Authority will pay or reimburse the Trustee upon its request for all expenses, disbursements and advances incurred or made by the Trustee in accordance with any of the provisions hereof (including the reasonable compensation and the expenses and disbursements of its counsel and of all persons not regularly in its employ) except any such expense, disbursement or advance as may arise from its negligence, default or willful misconduct. The Authority, to the extent permitted by law, shall indemnify, defend and hold harmless the Trustee against any loss, damages, liability or expense incurred without negligence, default or willful misconduct on the part of the Trustee arising out of or in connection with (i) the acceptance or administration of the trusts created hereby, or the exercise or performance of any

of its powers or duties hereunder, or (ii) any untrue statement or alleged untrue statement of any material fact or omission or alleged omission to state a material fact necessary to make the statements made, in the light of the circumstances under which they were made, not misleading in any official statement or other offering circular utilized in connection with the sale of any of the 2008 Certificates, including costs and expenses (including attorneys' fees) of defending itself against any claim or liability in connection with the exercise or performance of any of its powers hereunder; provided, however, that the Trustee shall in no event condition any draw upon the Liquidity Facility, any request for payment under the Credit Enhancement or any payment to Owners from such draws under the Liquidity Facility or such payments under the Credit Enhancement upon the provision of any indemnification for such performance. The rights of the Trustee and the obligations of the Authority under this Section shall survive the discharge of the 2008 Certificates and the Trust Agreement and the resignation or removal of the Trustee.

## ARTICLE VII

### AMENDMENT OF THE TRUST AGREEMENT

Section 7.01. Amendment of the Trust Agreement. The Trust Agreement and the rights and obligations of the Authority and of the Owners may be amended at any time by a Supplemental Trust Agreement which shall become binding when the written consents of the Owners of a majority in aggregate principal amount of the 2008 Certificates then Outstanding, exclusive of 2008 Certificates disqualified as provided in Section 7.02 hereof, are filed with the Trustee; provided, that before executing any such Supplemental Trust Agreement the Trustee may first obtain at the Authority's expense an Opinion of Counsel that such Supplemental Trust Agreement complies with the provisions of the Trust Agreement, on which opinion the Trustee may conclusively rely. No such amendment shall (1) extend the Certificate Payment Date of, or change the payment dates of, or reduce the rate of interest or principal or prepayment premium, if any, evidenced and represented by any 2008 Certificate without the express written consent of the Owner of such Certificate, or (2) reduce the percentage of 2008 Certificates required for the written consent to any such amendment, or (3) modify any rights or obligations of the Trustee without its prior written assent thereto.

The Trust Agreement and the rights and obligations of the Authority and of the Owners may also be amended at any time by a Supplemental Trust Agreement which shall become binding upon adoption without the consent of any Owners, but only to the extent permitted by law, for any purpose that will not materially adversely affect the interests of the Owners, including (without limitation) for any one or more of the following purposes:

- (a) to add to the agreements and covenants required herein to be performed by the Authority other agreements and covenants thereafter to be performed by the Authority, or to surrender any right or power reserved herein to or conferred herein on the Authority;
- (b) to make such provisions for the purpose of curing any ambiguity or of correcting, curing or supplementing any defective provision contained herein or in regard to questions arising hereunder which the Authority may deem desirable or necessary and not inconsistent herewith;

(c) to add to the agreements and covenants required herein, such agreements and covenants as may be necessary to qualify the Trust Agreement under the Trust Indenture Act of 1939;

(d) to make any amendments or supplements necessary or appropriate to preserve or protect the exclusion of interest evidenced and represented by the 2008 Certificates from gross income for federal income tax purposes under the Code or the exemption of such interest from State of California personal income taxes;

(e) to make such amendments or supplements as may be necessary or appropriate to maintain any then current rating on the 2008 Certificates by any of the Rating Agencies;

(f) to add to the rights of the Trustee;

(g) to modify, alter, amend or supplement this Trust Agreement in any other respect, including amendments which would otherwise be described in the first paragraph of this Section 7.01, if the effective date of such amendments is a date on which all 2008 Certificates affected thereby are subject to mandatory tender for purchase pursuant to the provisions of this Trust Agreement or if notice of the proposed amendments is given to Owners of the affected 2008 Certificates at least thirty (30) days before the proposed effective date of such amendments and, on or before such effective date, such Owners have the right to demand purchase of their 2008 Certificates pursuant to the provisions of this Trust Agreement; or

(h) for any other purpose that does not materially and adversely affect the interests of the Owners of the 2008 Certificates.

Section 7.02. Disqualified Certificates. 2008 Certificates owned or held by or for the account of the Authority or the City shall not be deemed Outstanding for the purpose of any consent or other action or any calculation of Outstanding 2008 Certificates provided in this article, and shall not be entitled to consent to or take any other action provided in this article. Upon request of the Trustee, the Authority and the City shall specify in a certificate to the Trustee those 2008 Certificates disqualified pursuant to this Section and the Trustee may conclusively rely on such certificate.

Section 7.03. Endorsement or Replacement of Certificates After Amendment. After the effective date of any action taken as hereinabove provided, the Authority may determine that the 2008 Certificates may bear a notation by endorsement in form approved by the Authority as to such action, and in that case upon demand of the Owner of any Outstanding 2008 Certificates and presentation of such Owner's 2008 Certificate for such purpose at the Corporate Trust Office of the Trustee a suitable notation as to such action shall be made on such Certificate. If the Authority shall so determine, new 2008 Certificates so modified as, in the opinion of the Authority, shall be necessary to conform to such action shall be prepared and executed, and in that case upon demand of the Owner of any Outstanding 2008 Certificate a new 2008 Certificate or Certificates shall be exchanged at the Corporate Trust Office of the Trustee without cost to

each Owner for its 2008 Certificate or 2008 Certificates then Outstanding upon surrender of such Outstanding 2008 Certificates.

Section 7.04. Amendment by Mutual Consent. Subject to Section 10.02 hereof, the provisions of this article shall not prevent any Owner from accepting any amendment as to the particular 2008 Certificates held by him, provided that due notation thereof is made on such 2008 Certificates.

Section 7.05. Consent of Liquidity Facility Provider. Notwithstanding anything to the contrary contained in this Trust Agreement, this Trust Agreement may not be amended without the prior written consents of the Liquidity Facility Provider and 2008 Certificate Insurer.

Section 7.06. Notice. The Trustee shall give notice to the Rating Agencies of any amendments pursuant to this Article VII.

## ARTICLE VIII

### EVENTS OF DEFAULT AND REMEDIES OF OWNERS

Section 8.01. Events of Default: Acceleration; Waiver of Default. If an Event of Default (as that term is defined in the Contract) shall happen, then such Event of Default shall constitute a default hereunder, and in each and every such case during the continuance of such Event of Default the Trustee after receiving indemnification to its satisfaction or the Owners of not less than a majority in aggregate principal amount of the 2008 Certificates then Outstanding shall exercise the remedies provided to the Authority in the Contract; provided, that nothing contained herein shall affect or impact the right of action of any Owner to institute suit directly against the City to enforce payment of the obligation evidenced and represented by such Owner's 2008 Certificates. In determining whether a payment default has occurred hereunder, or whether a payment on the 2008 Certificates has been made hereunder, no effect shall be given to payments made under the 2008 Certificate Insurance Policy. Upon the occurrence of any Event of Default, the Trustee shall give notice to the Credit Enhancement Provider and the Liquidity Facility Provider.

Section 8.02. Other Remedies of the Trustee. The Trustee shall have the right—

(a) by mandamus or other action or proceeding or suit at law or in equity to enforce the Authority's rights under the Contract against the City or any director, officer or employee thereof, and to compel the City or any such director, officer or employee to perform or carry out its or his duties under law and the agreements and covenants required to be performed by it or him contained in the Contract;

(b) by suit in equity to enjoin any acts or things which are unlawful or violate the rights of the Trustee; or

(c) by suit in equity upon the happening of any Event of Default hereunder to enforce the Authority's rights under the Contract to require the City and its directors, officers and employees to account as the trustee of an express trust.

Section 8.03. Non-Waiver. A waiver of any default or breach of any duty or contract by the Trustee shall not affect any subsequent default or breach of duty or contract or impair any rights or remedies on any such subsequent default or breach of duty or contract. No delay or omission by the Trustee to exercise any right or remedy accruing upon any default or breach of duty or contract shall impair any such right or remedy or shall be construed to be a waiver of any such default or breach of duty or contract or any acquiescence therein, and every right or remedy conferred upon the Trustee by law or by this article may be enforced and exercised from time to time and as often as shall be deemed expedient by the Trustee.

If any action, proceeding or suit to enforce any right or to exercise any remedy is abandoned or determined adversely to the Trustee, the Trustee, and the City shall be restored to their former positions, rights and remedies as if such action, proceeding or suit had not been brought or taken.

Section 8.04. Remedies Not Exclusive. No remedy herein conferred upon or reserved to the Trustee or the Owners is intended to be exclusive of any other remedy, and each such remedy shall be cumulative and shall be in addition to every other remedy given hereunder or now or hereafter existing in law or in equity or by statute or otherwise and may be exercised without exhausting and without regard to any other remedy conferred by law.

Section 8.05. No Liability by the City to the Owners. Except for the payment when due of the 2008 Payments and the performance of the other agreements and covenants required to be performed by it contained in the Contract, the City shall not have any obligation or liability to the Owners with respect to the Trust Agreement or the preparation, execution, delivery or transfer of the 2008 Certificates or the disbursement of the 2008 Payments by the Trustee to the Owners, or with respect to the performance by the Trustee of any right or obligation required to be performed by it contained herein.

Section 8.06. No Liability by the Trustee to the Owners. Except as expressly provided herein, the Trustee shall not have any obligation or liability to the Owners with respect to the payment when due of the 2008 Payments by the City, or with respect to the performance by the City of the other agreements and covenants required to be performed by its contained in the Contract.

Section 8.07. Control of Remedies by Credit Enhancement Provider or Liquidity Facility Provider. As long as no Control Event has occurred, notwithstanding anything in this Trust Agreement to the contrary, the 2008 Certificate Insurer shall have the right to direct all remedies upon the occurrence of an Event of Default. If a Control Event has occurred and the Bank's Credit Enhancement is in effect, notwithstanding anything in this Trust Agreement to the contrary, the Bank shall have the right to direct all remedies upon the occurrence of an Event of Default. If a Control Event has occurred and the Bank's Credit Enhancement is no longer in effect, notwithstanding anything in this Trust Agreement to the contrary, the Liquidity Facility Provider shall have the right to direct all remedies upon the occurrence of an Event of Default.

Notwithstanding the foregoing, if a Liquidity Facility is in effect, and the Provider thereof has failed to honor its payment obligations under the Liquidity Facility in respect of the purchase price of Certificates upon tender thereof, fifty-one percent (51%) of the Certificate

holders of the Certificates enhanced by such Liquidity Facility (excluding Certificates owned by the City and Bank Certificates), shall have the right at any time, by an instrument or instruments in writing executed and delivered to the Trustee, to direct the method and place of conducting all proceedings to be taken in connection with the enforcement of such payment obligations; provided that such direction shall be in accordance with applicable law.

Section 8.08. Application of Funds in case of an Event of Default. All moneys received by the Trustee pursuant to any right given or action taken under the provisions of this Article VIII shall be deposited into the 2008 Debt Service Fund and shall be applied by the Trustee in the following order upon presentation and surrender of the several 2008 Certificates: First, Costs and Expenses: to the payment of reasonable fees and expenses of the Trustee (including reasonable fees and disbursements of its counsel) incurred in and about the performance of its powers and duties under this Trust Agreement; Second, Interest: to the payment to the persons entitled thereto of all installments of interest then due or which have accreted in the order of the maturity of such installment, and, if the amount available shall not be sufficient to pay in full any installment or installments maturing on the same date, then to the payment thereof ratably, according to the amounts due thereon, to the persons entitled thereto, without any discrimination or preference; and Third, Principal: to the payment to the persons entitled thereto of the unpaid principal of any 2008 Certificates that shall have become due, whether at maturity or by call for prepayment, in the order of their due dates, with interest on the overdue principal and interest at a rate equal to the rate paid with respect to the 2008 Certificates and, if the amount available shall not be sufficient to pay in full all the amounts due with respect to the 2008 Certificates on any date, together with such interest, then to the payment thereof ratably, according to the amounts of principal due on such date to the persons entitled thereto, without any discrimination or preference.

## ARTICLE IX

### DEFEASANCE

Section 9.01. Discharge of Trust Agreement. When the obligations of the City under the Contract shall cease pursuant to Article VI of the Contract (except for the right of the Trustee and the obligation of the City to have the money and Federal Securities mentioned therein applied to the payment of 2008 Payments as therein set forth) and (i) the 2008 Certificates are in Fixed Rate Mode at the time moneys or Federal Securities are deposited, (ii) the deposit of money and Federal Securities is sufficient to pay the 2008 Certificates at the Maximum Rate to the earlier of the first possible tender or redemption date, (iii) the City shall have received a Rating Confirmation Notice on any 2008 Certificate that shall remain Outstanding following such redemption, and (iv) all other sums payable hereunder, including to the 2008 Certificate Insurer and Bank, have been paid, then and in such case the obligations created by this Trust Agreement shall thereupon cease, terminate and become void except for the right of the Owners and the obligation of the Trustee to apply such moneys and Federal Securities to the payment of the 2008 Certificates as herein set forth and the right of the Trustee to collect any fees or expenses due hereunder and the Trustee shall turn over to the City, as an overpayment of 2008 Payments, all balances remaining in any other funds or accounts other than moneys and Federal Securities held for the payment of the 2008 Certificates at maturity or on prepayment, which moneys and Federal Securities shall continue to be held by the Trustee in trust for the benefit of

the Owners and shall be applied by the Trustee to the payment, when due, of the principal and interest and premium if any represented by the 2008 Certificates, and after such payment, this Trust Agreement shall become void.

If moneys or Federal Securities are deposited with and held by the Trustee as hereinabove provided, the Trustee shall mail a notice, first-class postage prepaid, to the Owners at the addresses listed on the registration books kept by the Trustee pursuant to Section 2.08 hereof, stating that (a) moneys or Federal Securities are so held by it, and (b) that this Trust Agreement has been released in accordance with the provisions of this Section.

In connection with any defeasance of any of the 2008 Certificates pursuant to this Article, the 2008 Certificate Insurer (or, if a Control Event has occurred, the Bank) shall receive (i) a Favorable Opinion of Special Counsel and (ii) an escrow agreement and an Opinion of Counsel regarding the validity and enforceability of the escrow agreement, such escrow agreement shall provide that: (1) any substitution of securities shall require a verification by an independent certified public accountant and the prior written consent of the 2008 Certificate Insurer; (2) the Authority will not exercise any optional redemption of the 2008 Certificates secured by the escrow agreement or any other redemption other than mandatory sinking fund redemptions unless (a) the right to make any such redemption has been expressly reserved in the escrow agreement and such reservation has been disclosed in detail in the official statement for the refunding obligations, and (b) as a condition of any such redemption there shall be provided to the 2008 Certificate Insurer (or, if a Control Event has occurred, the Bank) a verification of an independent certified public accountant as to the sufficiency of escrow receipts without reinvestment to meet the escrow requirements remaining following such redemption; and (3) the Authority shall not amend the escrow agreement or enter into a forward purchase agreement or other agreement with respect to rights in the escrow without the prior written consent of the 2008 Certificate Insurer (or, if a Control Event has occurred, the Bank).

Notice of discharge of the Trust Agreement under this Article IX shall be provided to the Rating Agencies by the Trustee.

Notwithstanding the provisions of this Section: (i) amounts of principal of and interest on any 2008 Certificates paid by the 2008 Certificate Insurer under the 2008 Certificate Insurance Policy shall not be deemed to have been paid for purposes of this Trust Agreement and such 2008 Certificates shall remain Outstanding and such amounts shall continue to be due and owing until paid; and (ii) this Trust Agreement shall not be discharged unless all amounts due or to become due to the 2008 Certificate Insurer hereunder or under the 2008 Certificate Insurance Policy have been paid in full or duly provided for.

Section 9.02. Deposit of Money or Securities with Trustee. Whenever in this Trust Agreement or the Contract it is provided or permitted that there be deposited with or held in trust by the Trustee money or securities (certified to be sufficient by a report of an Independent Certified Public Accountant) in the necessary amount to pay or prepay any 2008 Certificates, the money or securities to be so deposited or held may include money or securities held by the Trustee in the funds and accounts established pursuant to this Trust Agreement and shall be --

(a) lawful money of the United States of America in an amount equal to the principal amount represented by such 2008 Certificates and all unpaid interest represented thereby to maturity, except that, in the case of 2008 Certificates which are to be prepaid prior to maturity and in respect of which notice of such prepayment shall have been given as in Article II provided or provision satisfactory to the Trustee shall have been made for the giving of such notice, the amount to be deposited or held shall be the principal amount plus accrued interest to such date of prepayment plus a prepayment premium, if any, represented by such 2008 Certificates; or

(b) Federal Securities which are not subject to redemption except by the holder thereof prior to maturity (including any such securities issued or held in book-entry form) or municipal obligations which have been defeased under irrevocable escrow instructions with Federal Securities and which are rated in the highest rating category by the Rating Agencies, the principal of and interest on which when due will provide, in its opinion of an Independent Certified Public Accountant, delivered to the Trustee, money sufficient to pay the principal plus prepayment premium, if any, plus all accrued interest to maturity or to the prepayment date, as the case may be, represented by the 2008 Certificates to be paid or prepaid, as such amounts become due, provided that, in the case of 2008 Certificates which are to be prepaid prior to the maturity thereof, notice of such prepayment shall have been given as in Article II provided or provision satisfactory to the Trustee shall have been made for the giving of such notice;

provided, in each case, that the Trustee shall have been irrevocably instructed (by the terms of this Trust Agreement and the Contract or by Written Request of the City) to apply such money to the payment of such principal plus prepayment premium, if any, plus interest represented by such 2008 Certificates.

Section 9.03. Unclaimed Money. Anything contained herein to the contrary notwithstanding, any money held by the Trustee in trust for the payment and discharge of any of the 2008 Certificates which remains unclaimed for two years after the date when such 2008 Certificates have become due and payable, either at their stated Certificate Payment Dates or by call for prepayment prior to Certificate Payment Date, if such money was held by the Trustee at such date, or for two years after the date of deposit of such money if deposited with the Trustee after the date when such Certificates have become due and payable, shall be repaid by the Trustee to the City as its absolute property free from trust, and the Trustee shall thereupon be released and discharged with respect thereto and the Owners shall look only to the City for the payment of the 2008 Payments evidenced and represented by such 2008 Certificates; provided, however, that before being required to make any such payment to the City, the Trustee shall, at the request of and at the expense of the City, cause to be mailed to all Owners and the Securities Depositories and the Information Services a notice that such money remains unclaimed and that, after a date named in such notice, which date shall not be less than 30 days after the date of the first publication of each such notice, the balance of such money then unclaimed will be returned to the City.

## ARTICLE X

### CERTIFICATE INSURANCE PROVISIONS

Section 10.01. Payment Under the 2008 Certificate Insurance Policy. The payment when due of the principal and interest with respect to the 2008 Certificates shall be insured by the 2008 Certificate Insurance Policy. As long as the 2008 Certificate Insurance Policy shall be in full force and effect, the Authority and the Trustee agree to comply with the following provisions with respect to the 2008 Certificates:

(a) In the event that, on the second Business Day, and again on the Business Day, prior to an interest payment date for the 2008 Certificates the Trustee has not received sufficient moneys to pay all of the principal and interest with respect to the 2008 Certificates (including amounts required to reimburse the Bank for the payment of such principal and interest) due on the second following, or following, Business Day, as the case may be, the Trustee shall promptly on such Business Day moneys are not received, notify the 2008 Certificate Insurer or its designee on the same Business Day by telephone, electronic mail or facsimile, confirmed in writing by registered or certified mail of the amount of the deficiency, the obligations which such deficiency is applicable and whether such obligations will be deficient as to principal or interest or both. If the deficiency is cured in whole or in part prior to or on the interest payment date, the Trustee shall so notify the 2008 Certificate Insurer or its designee.

(b) The Trustee shall, after giving notice to the 2008 Certificate Insurer, as provided above, make available to the 2008 Certificate Insurer and, at the 2008 Certificate Insurer's direction, to any fiscal agent, the registration books of the Authority maintained by the Trustee and all records relating to the funds maintained under the documentation.

(c) The Trustee shall provide the 2008 Certificate Insurer and any fiscal agent with a list of registered owners of the 2008 Certificates entitled to receive principal or interest payments from the 2008 Certificate Insurer under the terms of the 2008 Certificate Insurance Policy, and shall make arrangements with the 2008 Certificate Insurer, the fiscal agent or another designee of the 2008 Certificate Insurer to (i) mail checks or drafts to the registered owners of the 2008 Certificates (including the Bank) entitled to receive full or partial interest payments from the 2008 Certificate Insurer and (ii) pay principal upon the 2008 Certificates surrendered to the 2008 Certificate Insurer, the fiscal agent or another designee of the 2008 Certificate Insurer by the registered owners of the 2008 Certificates (including the Bank) entitled to receive full or partial principal payments from the 2008 Certificate Insurer.

(d) The Trustee shall, at the time it provides notice to the 2008 Certificate Insurer of any deficiency pursuant to clause (a) above, notify registered owners of the 2008 Certificates (including the Bank) entitled to receive the payment of principal or interest thereon from the 2008 Certificate Insurer (i) as to such deficiency and its entitlement to receive principal or interest, as applicable, (ii) that the 2008 Certificate Insurer will remit to them all or a part of the interest payments due on the related payment date upon proof of its entitlement thereto and delivery to the 2008 Certificate Insurer or any fiscal agent, in form satisfactory to the 2008 Certificate Insurer, of an appropriate assignment of the registered owner's right to payment, (iii) that, if they are entitled to receive partial payment of principal from the 2008 Certificate Insurer,

they must surrender the related the 2008 Certificates for payment first to the Trustee, which will note on such the 2008 Certificates the portion of the principal paid by the Trustee and second to the 2008 Certificate Insurer or its designee, together with an appropriate assignment, in form satisfactory to the 2008 Certificate Insurer, to permit ownership of the 2008 Certificates to be registered in the name of the 2008 Certificate Insurer, which will then pay the unpaid portion of principal, and (iv) that, if they are entitled to receive full payment of principal from the 2008 Certificate Insurer, they must surrender the 2008 Certificates for payment to the 2008 Certificate Insurer or its designee, rather than the Trustee, together with the an appropriate assignment, in form satisfactory to the 2008 Certificate Insurer, to permit ownership of the 2008 Certificates to be registered in the name of the 2008 Certificate Insurer.

(e) In addition, if the Trustee has written notice that any Owner of a 2008 Certificate (including the Bank) has been required to disgorge payments of principal or interest with respect to the 2008 Certificates to the City or its trustee in bankruptcy or creditors or others pursuant to a final judgment by a court of competent jurisdiction that such payment constitutes a voidable preference to such Owner within the meaning of any applicable bankruptcy laws, then the Trustee shall notify the 2008 Certificate Insurer or its designee of such fact by telephone or telegraphic notice, confirmed in writing by registered or certified mail.

(f) The Trustee is hereby irrevocably designated, appointed, directed and authorized to act as attorney-in-fact for Owners of the 2008 Certificates (including the Bank) as follows:

(i) If and to the extent there is a deficiency in amounts required to fully pay interest on the 2008 Certificates, the Trustee shall (i) execute and deliver to the 2008 Certificate Insurer, in form satisfactory to the 2008 Certificate Insurer, an instrument appointing the 2008 Certificate Insurer as agent for such Owners in any legal proceeding related to the payment of such interest and an assignment to the 2008 Certificate Insurer of the claims for interest to which such deficiency relates and which are paid by the 2008 Certificate Insurer, (ii) receive as designee of the respective Owners (and not as Trustee) in accordance with the tenor of the 2008 Certificate Insurance Policy payment from the 2008 Certificate Insurer with respect to the claims for interest so assigned and (iii) disburse the same to such respective Owners; and

(ii) If and to the extent of a deficiency in amounts required to pay principal with respect to the 2008 Certificates, the Trustee shall (i) execute and deliver to the 2008 Certificate Insurer, in form satisfactory to the 2008 Certificate Insurer, an instrument appointing the 2008 Certificate Insurer as agent for such Owner in any legal proceeding relating to the payment of such principal and an assignment to the 2008 Certificate Insurer of any of the 2008 Certificates surrendered to the 2008 Certificate Insurer of so much of the principal thereof as has not previously been paid or for which moneys are not held by the Trustee and available for such payment (but such assignment shall be effective only if payment from the 2008 Certificate Insurer is received), (ii) receive as designee of the respective Owners (and not as Trustee) in accordance with the tenor of the 2008 Certificate Insurance Policy payment therefor from the 2008 Certificate Insurer and (iii) disburse the same to such Owners.

(g) In the event that the Trustee shall have made a claim under the 2008 Certificate Insurance Policy with respect to principal and/or interest due on any payment date with respect to the 2008 Certificates and the Bank shall have paid on such payment date a draw made by the Trustee on the Bank's Credit Enhancement for such principal and/or interest, then, notwithstanding anything to the contrary, the amount paid by the 2008 Certificate Insurer with respect to the 2008 Certificates (the "Held Amount") on such payment date pursuant to such claim under the 2008 Certificate Insurance Policy shall be held uninvested by the Trustee until the Trustee shall have received notice from the 2008 Certificate Insurer that: (A) the Bank has directed the 2008 Certificate Insurer to reimburse the Bank for such draw pursuant to the Reimbursement Agreement between the Bank and the City, in which case the Trustee shall immediately pay the Held Amount to the Bank; or (B) the Bank has failed to direct the 2008 Certificate Insurer to reimburse the Bank for such draw within the time period set forth in the Reimbursement Agreement between the Bank and the City, in which case the Trustee shall immediately return the Held Amount to the 2008 Certificate Insurer. If the Held Amount is returned to the 2008 Certificate Insurer, the Authority shall pay interest at the Reimbursement Rate on such Held Amount from the date paid by the 2008 Certificate Insurer until such return to the 2008 Certificate Insurer. Payments with respect to claims for interest and principal with respect to the 2008 Certificates disbursed by the Trustee from proceeds of the 2008 Certificate Insurance Policy shall not be considered to discharge the obligation of the Authority with respect to such 2008 Certificates, and the 2008 Certificate Insurer shall become the Owner of such unpaid 2008 Certificates and claims for the interest in accordance with the tenor of the assignment made to it under the provisions of this Section 10.01 or otherwise.

(h) Irrespective of whether any such assignment is executed and delivered, the Authority and the Trustee hereby for the benefit of the 2008 Certificate Insurer that:

(i) to the extent the 2008 Certificate Insurer makes payments, directly or indirectly (as by paying through the Trustee), on account of the principal or interest with respect to the 2008 Certificates, the 2008 Certificate Insurer will be subrogated to the rights of the Owners of the 2008 Certificates to receive the amount of such principal and interest, with interest thereon as provided and solely from the sources stated in this Trust Agreement and the 2008 Certificates, and

(ii) they will accordingly pay to the 2008 Certificate Insurer the amount of such principal and interest, with interest thereon as provided in this Trust Agreement and the 2008 Certificates, but only from the sources and in the manner provided herein for the payment of the principal and interest with respect to the 2008 Certificates to Owners, and will otherwise treat the 2008 Certificate Insurer as the Owner of such rights to the amount of such principal and interest.

(i) The Authority hereby agrees to pay or reimburse the 2008 Certificate Insurer, to the extent permitted by law, (A) all amounts paid by the 2008 Certificate Insurer under the terms of the 2008 Certificate Insurance Policy, and (B) any and all charges, fees, costs and expenses which the 2008 Certificate Insurer may reasonably pay or incur, including, but not limited to, fees and expenses of attorneys, accountants, consultants and auditors and reasonable costs of investigations, in connection with (i) any accounts established to facilitate payments under the 2008 Certificate Insurance Policy, (ii) the administration, enforcement, defense or preservation

of any rights in respect of this Trust Agreement or any other financing document, including defending, monitoring or participating in any litigation or proceeding (including any bankruptcy proceeding in respect of the Authority or any affiliate thereof) relating to this Trust Agreement or any other financing document, any party to this Trust Agreement or any other financing document or the transaction contemplated by this Trust Agreement or any other financing documents, (iii) the foreclosure against, sale or other disposition of any collateral securing any obligations under this Trust Agreement or any other financing document, or the pursuit of any remedies under this Trust Agreement or any other financing document, to the extent such costs and expenses are not recovered from such foreclosure, sale or other disposition, or (iv) any amendment, waiver or other action with respect to, or related to, this Trust Agreement or any other financing document whether or not executed or completed; costs and expenses shall include a reasonable allocation of compensation and overhead attributable to time of employees of the 2008 Certificate Insurer spent in connection with the actions described in clauses (ii) - (iv) above. In addition, the 2008 Certificate Insurer reserves the right to charge a reasonable fee as a condition to executing any amendment, waiver or consent proposed in respect of this Trust Agreement or any other financing document. The Authority will pay interest on the amounts owed in this paragraph from the date of any payment due or paid, at the per annum rate of interest publicly announced from time to time by JP Morgan Chase Bank, National Association at its principal office in New York, New York as its prime lending rate (any change in such prime rate of interest to be effective on the date such change is announced by JPMorgan Chase Bank, National Association) plus three percent (3%) per annum (the "Reimbursement Rate"). The Reimbursement Rate shall be calculated on the basis of the actual number of days elapsed over a 360-day year. In the event JPMorgan Chase Bank ceases to announce its prime rate publicly, the prime rate shall be the publicly announced prime rate or base lending rate of such national bank, as the 2008 Certificate Insurer shall specify.

(j) In addition to any and all rights of reimbursement, subrogation and any other rights pursuant hereto or under law or in equity, the Authority agrees to pay or reimburse the 2008 Certificate Insurer, to the extent permitted by law, any and all charges, fees, costs, claims, losses, liabilities (including penalties), judgments, demands, damages, and expenses which the 2008 Certificate Insurer or its officers, directors, shareholders, employees, agents and each Person, if any, who controls the 2008 Certificate Insurer within the meaning of either Section 15 of the Securities Act of 1933, as amended, or Section 20 of the Securities Exchange Act of 1934, as amended, may reasonably pay or incur, including, but not limited to, fees and expenses of attorneys, accountants, consultants and auditors and reasonable costs of investigations, of any nature in connection with, in respect of or relating to the transactions contemplated by this Trust Agreement or any other financing document by reason of:

(a) any omission or action (other than of or by the 2008 Certificate Insurer) in connection with the offering, issuance, sale, remarketing or delivery of the 2008 Certificates;

(b) the negligence, bad faith, willful misconduct, misfeasance, malfeasance or theft committed by any director, officer, employee or agent of the Authority in connection with any transaction arising from or relating to this Trust Agreement or any other financing document;

(c) the violation by the Authority of any law, rule or regulation, or any judgment, order or decree applicable to it;

(d) the breach by the Authority of any representation, warranty or covenant under this Trust Agreement or any other financing document or the occurrence, in respect of the Authority under this Trust Agreement or any other financing document of any "event of default" or any event which, with the giving of notice or lapse of time or both, would constitute any "event of default"; or

(e) any untrue statement or alleged untrue statement of a material fact contained in any official statement relating to the 2008 Certificates, if any, or any omission or alleged omission to state therein a material fact required to be stated therein or necessary to make the statements therein not misleading, except insofar as such claims arise out of or are based upon any untrue statement or omission in information included in an official statement, if any, and furnished by the 2008 Certificate Insurer in writing expressly for use therein.

(k) The 2008 Certificate Insurer shall be entitled to pay principal of or interest on the 2008 Certificates that shall become Due for Payment but shall be unpaid by reason of Nonpayment (as such terms are defined in the 2008 Certificate Insurance Policy) and any amounts due on the 2008 Certificates as a result of acceleration of the maturity thereof in accordance with this Trust Agreement, whether or not the 2008 Certificate Insurer has received a Notice (as defined in the 2008 Certificate Insurance Policy) of Nonpayment or a claim upon the 2008 Certificate Insurance Policy.

(l) In addition, the 2008 Certificate Insurer shall, to the extent it makes any payment of principal or interest on the 2008 Certificates, become subrogated to the rights of the recipients of such payments in accordance with the terms of 2008 Certificate Insurance Policy, and to evidence such subrogation (i) in the case of claims for interest, the Trustee shall note the 2008 Certificate Insurer's rights as subrogee on the registration books of the Authority maintained by the Trustee, upon receipt of proof of payment of interest thereon to the registered holders of the 2008 Certificates, and (ii) in the case of claims for principal, the Trustee, if any, shall note the 2008 Certificate Insurer's rights as subrogee on the registration books of the Authority maintained by the Trustee, upon surrender of the 2008 Certificates together with receipt of proof of payment of principal thereof.

Section 10.02. Additional Provisions Related to the 2008 Certificate Insurance Policy.

(a) Subject to Section 10.03, the 2008 Certificate Insurer shall be deemed to be sole Owner of the 2008 Certificates it insures for the purpose of exercising any voting right or privilege or giving any consent or direction or taking any other action that the 2008 Certificate Owners are entitled to take pursuant to this Trust Agreement, including any consent to any modification, amendment or supplement to this Trust Agreement pursuant to Section 7.01 hereof.

(b) Copies of any amendments made to the documents executed in connection with the issuance of the 2008 Certificates which are consented to by the 2008 Certificate Insurer shall be sent to Standard & Poor's.

(c) The 2008 Certificate Insurer shall receive written notice of the resignation or removal of the Trustee and any Trustee for the 2008 Certificates and the appointment of a successor thereto.

(d) The 2008 Certificate Insurer shall receive written copies of all notices required to be delivered to Owners of 2008 Certificates.

(e) The 2008 Certificate Insurer shall have the right to receive such additional information as it may reasonably request.

(f) The Authority will permit the 2008 Certificate Insurer to discuss the affairs, finances and accounts of the Authority or any information the 2008 Certificate Insurer may reasonably request regarding the security for the 2008 Certificates with appropriate officers of the Authority, and will use best efforts to enable the 2008 Certificate Insurer to have access to the facilities, books and records of the Authority on any business day upon reasonable prior notice.

(g) The Trustee shall notify the 2008 Certificate Insurer of any failure of the Authority to provide notices, certificates and other information under the financing documents.

(h) If the Trustee receives any moneys from proceeds of the 2008 Certificate Insurance Policy, the Trustee shall hold such moneys separate and apart from all other moneys held by the Trustee under this Trust Agreement and shall apply such moneys only to the payment of the principal or prepayment price or interest with respect to the 2008 Certificates for which such payments were received.

(i) In the event that the principal and/or interest due on the 2008 Certificates shall be paid by the 2008 Certificate Insurer pursuant to 2008 Certificate Insurance Policy, the 2008 Certificates shall remain outstanding for all purposes, not be defeased or otherwise satisfied and not be considered paid by the Authority, and the assignment and pledge of the trust estate and all covenants, agreements and other obligations of the Authority to the registered owners shall continue to exist and shall run to the benefit of the 2008 Certificate Insurer, and the 2008 Certificate Insurer shall be subrogated to the rights of such registered owners, including, without limitation, any rights that such owners may have in respect of securities law violations arising from the offer and sale of the 2008 Certificates.

(j) The 2008 Certificate Insurer shall be deemed to be the Owners of all of the 2008 Certificates for purposes of (a) exercising all remedies and directing the Trustee to take actions or for any other purposes following an Event of Default (as defined herein), and (b) granting any consent, direction or approval or taking any action permitted or required by the Owners of the 2008 Certificates.

(k) Notwithstanding anything in this Trust Agreement to the contrary so long as the 2008 Certificate Insurance Policy shall be in full force and effect and the 2008 Certificate Insurer

shall not be in default of any of its obligations thereunder, upon the occurrence and continuance of an Event of Default, as defined herein, the Trustee may, with the consent of the 2008 Certificate Insurer, and shall at the direction of the 2008 Certificate Insurer or the Bondholders with the prior written consent of the 2008 Certificate Insurer, by written notice to the Authority and the 2008 Certificate Insurer, as applicable (i) declare the payments under the Contract representing the principal of the 2008 Certificates immediately due and payable, in accordance with the terms of the Contract or (ii) annul any declaration of acceleration.

(l) In the event of any reorganization or liquidation, the 2008 Certificate Insurer shall have the right to vote on behalf of all Owners of the 2008 Certificates guaranteed by the 2008 Certificate Insurer, absent a default by the 2008 Certificate Insurer under the 2008 Certificate Insurance Policy.

(m) The Authority, to the extent permitted by law, but solely from amounts payable under the Contract, to the extent such amounts are not required to pay the 2008 Certificates shall indemnify, defend and hold harmless the 2008 Certificate Insurer against any loss, damages, liability or expense incurred without negligence, default or willful misconduct on the part of the 2008 Certificate Insurer arising out of or in connection with (i) the exercise or performance of any of its powers or duties hereunder, or (ii) any untrue statement or alleged untrue statement of any material fact or omission or alleged omission to state a material fact necessary to make the statements made, in the light of the circumstances under which they were made, not misleading in any official statement or other offering circular utilized in connection with the sale of any of the 2008 Certificates, including costs and expenses (including attorneys' fees) of defending itself against any claim or liability in connection with the exercise or performance of any of its powers hereunder. The rights of the 2008 Certificate Insurer and the obligations of the Authority under this Section shall survive the discharge of the 2008 Certificates and this Trust Agreement. Notwithstanding the foregoing, the Authority will not be liable for any losses, costs or expenses resulting from the willful misconduct or negligence of the 2008 Certificate Insurer, or resulting from a misrepresentation or omission made by the 2008 Certificate Insurer in any offering document or other disclosure materials or filings (including any filings made with any insurance regulator, the Securities & Exchange Commission or any other government body) concerning the 2008 Certificate Insurer.

(n) The 2008 Certificate Insurer shall be provided with the following information:

(i) the financial statements of the City and other information furnished by the City to the Authority within fifteen Business Days after receipt thereof by the City pursuant to Section 4.09(b) of the Master Purchase Contract;

(ii) notice of any draw upon the Reserve Fund within two Business Days after knowledge thereof other than (A) withdrawals of amounts in excess of the Reserve Fund Requirement, and (B) withdrawals in connection with a refunding of 2008 Certificates;

(iii) notice of any default under this Trust Agreement known to the Trustee or the Authority within five Business Days after knowledge thereof;

(iv) notice of the advance refunding or redemption of any of the 2008 Certificates within five Business Days after the Trustee receives notice thereof from the City, including the principal amount, maturities and CUSIP numbers thereof;

(v) as soon as practicable, notice of the commencement of any proceeding by or against the Authority or the City commenced under the United States Bankruptcy Code or any other applicable bankruptcy, insolvency, receivership, rehabilitation or similar law (an "Insolvency Proceeding");

(vi) as soon as practicable, notice of the making of any claim in connection with any Insolvency Proceeding seeking the avoidance as a preferential transfer of any payment of principal of, or interest on, the 2008 Certificates; and

(vii) as soon as practicable, a full transcript of all proceedings relating to the execution of any amendment, supplement or waiver to this Trust Agreement, the Master Contract or any other related document.

Section 10.03. 2008 Certificate Insurer Default. In the event that the 2008 Certificate Insurer is in payment default under the 2008 Certificate Insurance Policy, an Insurer Indenture Event of Default has occurred and is continuing with respect to the 2008 Certificate Insurance Policy or the 2008 Certificate Insurance Policy is no longer in effect (and all amounts due to the 2008 Certificate Insurer are then paid in full), all references herein to the 2008 Certificate Insurer and all provisions herein for the benefit of the 2008 Certificate Insurer shall be of no effect; provided, however, that the rights of the 2008 Certificate Insurer derived through subrogation and assignment shall remain in full force and effect.

Section 10.04. Modification, Cancellation, Termination or Substitution of 2008 Certificate Insurance Policy. The Authority shall not consent to the surrender, cancellation, termination, amendment or modification in any material respect of the 2008 Certificate Insurance Policy by the 2008 Certificate Insurer, or to the substitution of a different Credit Enhancement for the 2008 Certificate Insurance Policy, unless the Authority and the Trustee shall have received the consent of the Bank, and the Authority and the Trustee shall consent to any such surrender, cancellation, termination, amendment or modification of the 2008 Certificate Insurance Policy by the 2008 Certificate Insurer if so directed by the Bank within seven days of receiving such direction. If, upon receipt of such consent or direction from the Bank, the 2008 Certificate Insurance Policy is so surrendered, cancelled, terminated, amended or modified in any material respect by the 2008 Certificate Insurer, or a different Credit Enhancement is so substituted for the 2008 Certificate Insurance Policy, the 2008 Certificates shall be subject to mandatory tender.

Section 10.05. Additional Provisions with respect to Rights of the Bank.

(a) To the extent the Bank pays the principal of or interest on the 2008 Certificates from one or more drawings under its Credit Enhancement and has not been reimbursed for such payment by the Authority or the Trustee, on behalf of the Authority, in accordance with the terms of the Reimbursement Agreement between the Bank and the City, (i) such amounts of principal of and interest on such 2008 Certificates shall be deemed not to have been paid for

purposes of this Trust Agreement and such 2008 Certificates shall remain Outstanding and shall continue to be due and owing until paid or otherwise satisfied; (ii) all rights of the Owners of such 2008 Certificates with respect to receiving payment of such principal from the Authority shall, without any further action on the part of such Owners or the Trustee, be assigned to the Bank and the Bank shall become subrogated to such rights; (iii) as to any such payment of principal of the 2008 Certificates from a drawing under the Bank's Credit Enhancement, the Bank shall become the Owner of such 2008 Certificate, which shall be evidenced as set forth in the next sentence; and (iv) as to any such payment of interest on such 2008 Certificates from a drawing under the Bank's Credit Enhancement, the Bank shall become the owner of all rights to such interest, constituting the Assigned Rights to Interest with respect thereto. The Trustee shall designate any portion of payment of principal on 2008 Certificates paid from one or more drawings under the Bank's Credit Enhancement, whether by virtue of mandatory sinking fund pro rata redemption, maturity or other advancement of maturity, on its books as a reduction in the principal amount of 2008 Certificates registered to the then current Owner, whether DTC or its nominee or otherwise, and shall issue, as a replacement 2008 Certificate, a Subrogated Certificate to the Bank, registered in the name of the Bank, in a principal amount equal to the amount of principal so paid (without regard to Authorized Denominations); provided that the Trustee's failure to so designate any payment or issue any Subrogated Certificate shall have no effect on the amount of principal or interest payable by the Authority on any 2008 Certificate, the subrogation rights of the Bank or the Bank's ownership of such 2008 Certificate to the extent principal thereof has been paid from a drawing under the Bank's Credit Enhancement.

(b) In addition, to the extent the Bank pays the principal of or interest on 2008 Certificates from one or more drawings under the Bank's Credit Enhancement and has not been reimbursed from such payment by the Authority or the Trustee, on behalf of the Authority, in accordance with the terms of the Reimbursement Agreement between the Bank and the City, the Bank shall be subrogated to the rights of the Owners of such 2008 Certificates with respect to the 2008 Certificate Insurance Policy in respect of any such payment of principal or interest that is insured under the 2008 Certificate Insurance Policy (a "Covered Payment"); provided, however, that the Bank's subrogation rights with respect to the 2008 Certificate Insurance Policy in respect of the foregoing payments of principal and interest are subject to the terms and conditions of the 2008 Certificate Insurance Policy.

(c) To exercise such rights of subrogation as to a Covered Payment, the Bank must notify the Trustee and the 2008 Certificate Insurer on or before 5:00 p.m. New York City time on the date that is 30 days after a Covered Payment has been made that the Bank is making a claim (a "Claim") under the 2008 Certificate Insurance Policy, which claim shall (i) specifically reference the policy number of the 2008 Certificate Insurance Policy and shall be presented to the 2008 Certificate Insurer at its address specified herein or pursuant hereto, (ii) state the date of the Covered Payment, (iii) state the amount of the Covered Payment, and (iv) in all cases comply with the requirements of this Trust Agreement and the 2008 Certificate Insurance Policy. Upon payment of a Claim, the provisions of this Section shall apply to the same extent as if the 2008 Certificate Insurer had made such payment directly on the related Series of 2008 Certificates. In the event the Bank does not make a claim on or before 5:00 p.m. New York City time on the date that is 30 days after a Covered Payment, the 2008 Certificate Insurer shall have no further obligation to the Bank with respect thereto and a principal amount of the related Series of

Certificates equal to the principal that has been paid by the Bank shall be deemed to be fully discharged in accordance herewith.

(d) At all times from and after the occurrence of a Control Event with respect to the 2008 Certificate Insurance Policy, the Bank shall be an expressly intended third party beneficiary hereof and shall be deemed to be the sole Owner of the 2008 Certificates for the purpose of exercising any voting right or privilege or giving any consent or direction or taking any other action that the Owners of the 2008 Certificates are entitled to exercise, give or take pursuant to this Trust Agreement with respect to (i) Events of Default and remedies hereunder and under the Contract, (ii) the duties and obligations of the Trustee, and (iii) granting or withholding any consent wherever Owner consent is required.

(e) Notwithstanding any contrary provision hereof or of the Contract, following any Control Event, any references herein and in the Contract to the payment of the reasonable fees and expenses of the 2008 Certificate Insurer shall be deemed to refer to the reasonable fees and expenses of the Bank incurred in connection therewith; provided that any such fees and expenses previously incurred by the 2008 Certificate Insurer shall continue to be payable to the 2008 Certificate Insurer.

## ARTICLE XI

### MISCELLANEOUS

Section 11.01. Benefits of this Trust Agreement Limited to Parties. Nothing contained herein, expressed or implied, is intended to give to any person other than the Authority, the Trustee, the 2008 Certificate Insurer, the Bank and the Owners any right, remedy or claim under or by reason hereof. Any agreement or covenant required herein to be performed by or on behalf of the Authority or any member, officer or employee thereof shall be for the sole and exclusive benefit of the Trustee, the 2008 Certificate Insurer, the Bank and the Owners. The 2008 Certificate Insurer and the Bank shall be third-party beneficiaries of this Trust Agreement.

Section 11.02. Successor is Deemed Included In All References To Predecessor. Whenever herein either the Authority or any member, officer or employee thereof is named or referred to, such reference shall be deemed to include the successor to the powers, duties and functions that are presently vested in the Authority or such member, officer or employee, and all agreements and covenants required hereby to be performed by or on behalf of the Authority or any member, officer or employee thereof shall bind and inure to the benefit of the respective successors thereof whether so expressed or not.

Section 11.03. Execution of Documents by Owners. Any declaration, request or other instrument which is permitted or required herein to be executed by Owners may be in one or more instruments of similar tenor and may be executed by Owners in person or by their attorneys appointed in writing. The fact and date of the execution by any Owner or his attorney of any declaration, request or other instrument or of any writing appointing such attorney may be proved by the certificate of any notary public or other officer authorized to make acknowledgments of deeds to be recorded in the state or territory in which he purports to act that the person signing such declaration, request or other instrument or writing acknowledged to him

the execution thereof, or by an affidavit of a witness of such execution duly-sworn to before such notary public or other officer. The ownership of any 2008 Certificates and the amount, Certificate Payment Date, number and date of holding the same may be proved by the registration books relating to the 2008 Certificates at the corporate trust office of the Trustee.

Any declaration, request or other instrument or writing of the Owner of any 2008 Certificate shall bind all future Owners of such Certificate with respect to anything done or suffered to be done by the Authority or the Trustee in good faith and in accordance therewith.

Section 11.04. Waiver of Personal Liability. No member, officer or employee of the Authority shall be individually or personally liable for the payment of the interest or principal or prepayment premiums, if any, evidenced and represented by the 2008 Certificates by reason of their issuance, but nothing herein contained shall relieve any such member, officer or employee from the performance of any official duty provided by applicable provisions of law or hereby.

Section 11.05. Content of Certificates of the Authority. Every Certificate of the Authority with respect to compliance with any agreement, condition, covenant or provision provided herein shall include (a) a statement that the person or persons making or giving such certificate have read such agreement, condition, covenant or provision and the definitions herein relating thereto; (b) a brief statement as to the nature and scope of the examination or investigation upon which the statements contained in such certificate are based; (c) a statement that, in the opinion of the signers, they have made or caused to be made such examination or investigation as is necessary to enable them to express an informed opinion as to whether or not such agreement, condition, covenant or provision has been complied with; and (d) a statement as to whether, in the opinion of the signers, such agreement, condition, covenant or provision has been complied with.

Any Certificate of the Authority may be based, insofar as it relates to legal matters, upon an Opinion of Counsel unless the person making or giving such certificate knows that the Opinion of Counsel with respect to the matters upon which his certificate may be based, as aforesaid, is erroneous, or in the exercise of reasonable care should have known that the same was erroneous. Any Opinion of Counsel may be based, insofar as it relates to factual matters or information with respect to which is in the possession of the Authority, upon a representation by an officer or officers of the Authority unless the counsel executing such Opinion of Counsel knows that the representation with respect to the matters upon which his opinion may be based, as aforesaid, is erroneous, or in the exercise of reasonable care should have known that the same was erroneous.

Section 11.06. Accounts and Funds; Business Days. The Trustee may establish such funds and accounts as it deems necessary and appropriate to perform its duties and obligations hereunder. Any account or fund required herein to be established and maintained by the Trustee may be established and maintained in the accounting records of the Trustee either as an account or a fund, and may, for the purposes of such accounting records, any audits thereof and any reports or statements with respect thereto, be treated either as an account or a fund; but all such records with respect to all such accounts and funds shall at all times be maintained in accordance with sound corporate trust industry practice and with due regard for the protection of the security of the 2008 Certificates and the rights of the Owners. Any action required to occur hereunder on

a day which is not a Business Day shall be required to occur on the next succeeding Business Day with the same effect as if made on such non-Business Day.

Section 11.07. Notices.

(a) All written notices to be given hereunder shall be given by facsimile transmission or other Electronic means or by first-class mail or hand delivery (unless such delivery method shall be otherwise specified herein) to the party entitled thereto at its address set forth below, or at such other address as such party may provide to the other parties in writing from time to time, namely:

If to the Authority:

Modesto Public Financing Authority  
c/o City of Modesto  
City Hall  
1010 Tenth Street, Suite 5200  
Modesto, CA 95353  
Attention: Auditor and Treasurer  
Telephone No.: (209) 577-5371  
Facsimile No.: (209) 571-5880

If to the City:

City of Modesto  
1010 Tenth Street, Suite 5200  
Modesto, CA 95353  
Attention: Finance Director  
Telephone No.: (209) 577-5371  
Facsimile No.: (209) 571-5880

If to the Trustee:

The Bank of New York Mellon Trust Company,  
N.A.  
100 Pine Street, Suite 3100  
San Francisco, CA 94111  
Attention: Corporate Trust  
Telephone No.: (415) 263-2432  
Facsimile No.: (415) 399-1647

If to S&P:

Attn: Muni Structured Finance  
55 Water Street, 38<sup>th</sup> Floor  
New York, New York 10041  
Telephone No.: (212) 438-2000  
Email: Pubfin\_structured@standardandpoors.com

If to Moody's:

Moody's Investors Services  
7 World Financial Center  
New York, New York 10007  
Attention: Public Finance Department  
Facsimile: (212) 553-4090

If to the 2008 Certificate Insurer: Assured Guaranty Corp.  
1325 Avenue of the Americas  
New York, New York 10019  
Attention: General Counsel  
Facsimile: (212) 581-3268

Assured Guaranty  
1325 Avenue of the Americas  
New York, New York 10019  
Attention: Risk Management Department - Public  
Finance Surveillance  
Facsimile: (212) 581-3268

If to the Bank: JPMorgan Chase Bank, N.A.  
383 Madison Avenue, Floor 8  
New York, New York 10179  
Mail Code: NY1-M076  
Attention: James G. Millard  
Telephone: (212) 270-2198  
Telecopy: (917) 456-3538

Each such notice, statement, demand, consent, approval, authorization, offer, designation, request or other communication hereunder shall be deemed delivered to the party to whom it is addressed (i) if personally served or delivered, upon delivery, (ii) if given by Electronic communication, whether by telex, telegram or telecopier, upon the sender's receipt of an appropriate answer back or other written acknowledgement or confirmation of receipt of the entire notice, approval, demand, report or other communication, (iii) if given by first class or registered or certified mail, return receipt requested, deposited the United States mail postage prepaid, 72 hours after such notice is deposited with the United States mail, (iv) if given by overnight courier, with courier charges prepaid, 24 hours after delivery to said overnight courier, or (v) if given by any other means, upon delivery at the address specified in this Section 11.07.

(b) The Trustee shall give notice to the Rating Agencies of the occurrence of any of the following with respect to the 2008 Certificates:

(i) the removal, resignation or appointment of the Trustee or Remarketing Agent;

(ii) the execution of any amendment or supplement to the Trust Agreement, the Credit Enhancement, the Liquidity Facility or the Remarketing Agreement;

(iii) the expiration, termination, extension or substitution of the Liquidity Facility or Credit Enhancement;

(iv) the redemption in whole of the Outstanding 2008 Certificates;

(v) the acceleration of all Outstanding 2008 Certificates pursuant to Article VIII of the Trust Agreement;

- (vi) the defeasance of all Outstanding 2008 Certificates; and
- (vii) any change in Mode of the 2008 Certificates.

(c) The Trustee shall give notice to the Holders of the expiration, termination, extension or substitution of the Liquidity Facility or Credit Enhancement;

Section 11.08. CUSIP Numbers. Neither the Authority nor the Trustee shall be liable for any defect or inaccuracy in the CUSIP number that appears on any 2008 Certificate or in any prepayment notice relating thereto. The Trustee may, in its discretion, include in any prepayment notice relating to any of the 2008 Certificates a statement to the effect that the CUSIP numbers on the 2008 Certificates have been assigned by an independent service and are included in such notice solely for the convenience of the Owners and that neither the Authority nor the Trustee shall be liable for any defects or inaccuracies in such numbers.

Section 11.09. Article and Section Headings and References. The headings or titles of the several articles and sections hereof and the table of contents appended hereto shall be solely for convenience of reference and shall not affect the meaning, construction or effect hereof. All references herein to "articles," "sections" and other subdivisions or clauses are to the corresponding articles, sections, subdivisions or clauses hereof; and the words "hereby," "herein," "hereof," "hereto," "herewith," "hereunder" and other words of similar import refer to this Trust Agreement as a whole and not to any particular article, section, subdivision or clause hereof.

Section 11.10. Partial Invalidity. If any one or more of the agreements or covenants Trustee shall be contrary to law, then such agreement or agreements, such covenant or covenants or such portions thereof shall be null and void and shall be deemed separable from the remaining agreements and covenants or portions thereof and shall in no way affect the validity hereof or of the 2008 Certificates, and the Owners shall retain all the benefit, protection and security afforded to them under any applicable provisions of law. The Authority and the Trustee hereby declare that they would have executed and delivered this Trust Agreement and each and every other article, section, paragraph, subdivision, sentence, clause and phrase hereof and would have authorized the execution and delivery of the 2008 Certificates pursuant hereto irrespective of the fact that any one or more articles, sections, paragraphs, subdivisions, sentences, clauses or phrases hereof or the application thereof to any person or circumstance may be held to be unconstitutional, unenforceable or invalid.

Section 11.11. Execution in Several Counterparts. This Trust Agreement may be executed in any number of counterparts and each of such counterparts shall for all purposes be deemed to be an original; and all such counterparts, or as many of them as the Authority and the Trustee shall preserve undestroyed, shall together constitute but one and the same instrument.

Section 11.12. California Law. This Trust Agreement shall be construed and governed in accordance with the laws of the State of California.

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IN WITNESS WHEREOF, the Modesto Public Financing Authority has caused this Trust Agreement to be signed in its name by its Auditor and Treasurer and The Bank of New York Mellon Trust Company, N.A., in token of its acceptance of the trusts created hereunder, has caused this Trust Agreement to be signed by one of the officers thereunder duly authorized, all as of the day and year first above written.

MODESTO PUBLIC FINANCING  
AUTHORITY

By: *Monette Brink*  
Auditor and Treasurer

THE BANK OF NEW YORK MELLON  
TRUST COMPANY, N.A.,  
as Trustee

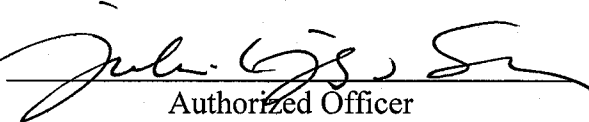
By: \_\_\_\_\_  
Authorized Officer

IN WITNESS WHEREOF, the Modesto Public Financing Authority has caused this Trust Agreement to be signed in its name by its Auditor and Treasurer and The Bank of New York Mellon Trust Company, N.A., in token of its acceptance of the trusts created hereunder, has caused this Trust Agreement to be signed by one of the officers thereunder duly authorized, all as of the day and year first above written.

MODESTO PUBLIC FINANCING  
AUTHORITY

By: \_\_\_\_\_  
Auditor and Treasurer

THE BANK OF NEW YORK MELLON  
TRUST COMPANY, N.A.,  
as Trustee

By:  \_\_\_\_\_  
Authorized Officer

**EXHIBIT A**

**[FORM OF CERTIFICATE OF PARTICIPATION]**

**WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A**

**Evidencing and Representing a Proportionate Interest of the Owner Hereof  
in 2008 Payments to be made by the  
City of Modesto  
to the  
Modesto Public Financing Authority**

Unless this certificate is presented by an authorized representative of The Depository Trust Company a New York corporation ("DTC"), to the Trustee or its agent for registration of transfer, exchange, or payment, and any certificate issued is registered in the name of Cede & Co. or in such other name as is requested by an authorized representative of DTC (and any payment is made to Cede & Co. or to such other entity as is requested by an authorized representative of DTC), ANY TRANSFER, PLEDGE, OR OTHER USE HEREOF FOR VALUE OR OTHERWISE BY OR TO ANY PERSON IS WRONGFUL inasmuch as the registered owner hereof, Cede & Co., has an interest herein.

No. R-1

\$47,625,000

<u>Interest Rate</u>	<u>Certificate Payment Date</u>	<u>Dated Date</u>	<u>CUSIP</u>	<u>Substitution Date</u>
Variable	October 1, 2036	May 30, 2008	607804 AC5	July 14, 2011

REGISTERED OWNER: CEDE & CO.

PRINCIPAL SUM: FORTY SEVEN MILLION SIX HUNDRED TWENTY FIVE  
THOUSAND DOLLARS

THIS IS TO CERTIFY that the registered owner set forth above of this Water Refunding Revenue Certificate of Participation, 2008 Series A (this "Certificate"), is the owner of a proportionate interest in the 2008 Payments (as that term is defined in the Trust Agreement hereinafter mentioned) made under and pursuant to that certain Master Installment Purchase Contract executed and entered into as of November 1, 1997, as heretofore supplemented and as supplemented by that certain 2008 Supplemental Installment Purchase Contract, dated as of May 1, 2008, each by and between the City of Modesto, a charter city and municipal corporation organized and existing under and by virtue of the Constitution and laws of the State of California (the "City") and the Modesto Public Financing Authority, a joint exercise of powers agency duly organized and existing under and by virtue of the laws of the State of California (the "Authority") (which Master Installment Purchase Contract as so supplemented is referred to herein as the "Contract"), all of which rights in the 2008 Payments have been assigned by the

Authority to The Bank of New York Mellon Trust Company, N.A., a national banking association duly organized and existing under and by virtue of the laws of the United States of America, or any other bank or trust company which may at any time be substituted in place of the original trustee as provided in the Trust Agreement hereinafter mentioned (the "Trustee"). Capitalized terms used in this Certificate but not otherwise defined shall have the meanings assigned to them in the Trust Agreement.

The registered owner of this Certificate is entitled to receive, subject to the terms of the Contract and any right of prepayment prior thereto hereinafter provided for, on the Certificate Payment Date set forth above, upon surrender of this Certificate on such Certificate Payment Date or on the date of prepayment prior thereto at the corporate trust office of the Trustee, the principal sum set forth above, representing the registered owner's proportionate share of the 2008 Payments constituting principal installments with respect to Certificates becoming due and payable on such Certificate Payment Date or on the date of prepayment prior thereto, and to receive an interest installment on such principal installment on each Interest Payment Date to the respective Certificate Payment Date or date of prepayment prior thereto. While this Certificate is in a Daily Mode or a Weekly Mode, the Interest Payment Date shall be the first Business Day of the month. Payment of interest evidenced by this Certificate shall be made to the person appearing on the registration books of the Trustee as the Owner thereof as of the close of business on the applicable Record Date, such interest to be payable on each Interest Payment Date by the Trustee (i) by check mailed on such Interest Payment Date to such Owner's address as it appears on the registration books of the Trustee at the close of business on the Record Date or (ii) by wire transfer to any Owner of at least \$1,000,000 aggregate principal amount of Certificates according to the written instructions provided by such Owner on or prior to the applicable Record Date to the Trustee, which written instructions shall remain in effect until revised by such Owner by an instrument in writing delivered to the Trustee. Interest evidenced by this Certificate shall accrue from and including the Interest Accrual Date immediately preceding the date of authentication hereof, or, if such date of authentication shall be an Interest Accrual Date, from such Interest Accrual Date or, if such date of authentication shall be prior to the second Interest Accrual Date, from the Delivery Date.

This Certificate is one of the duly authorized certificates of participation aggregating \$47,625,000, which have been executed by the Trustee under and pursuant to the provisions of a Trust Agreement, dated as of May 1, 2008, as amended and restated by an Amended and Restated Trust Agreement, dated July 14, 2011 (the "Trust Agreement"), between the Authority and the Trustee. Copies of the Trust Agreement are on file at the corporate trust office of the Trustee in San Francisco, California and reference is hereby made to the Trust Agreement and to any and all amendments thereof and supplements thereto for a description of the covenants and pledges securing the 2008 Payments and the Certificates, for the nature, extent and manner of enforcement of such covenants and pledges, for the rights and remedies of the registered owners of the Certificates with respect thereto and for the other conditions and terms upon which the Certificates are executed and delivered thereunder.

To the extent and in the manner permitted by the terms of the Trust Agreement, the provisions of the Trust Agreement may be amended by the parties thereto, but no such amendment shall (1) extend the Certificate Payment Date of this Certificate, or change the payment dates of, or reduce the rate of interest or principal or prepayment premium, if any,

evidenced and represented hereby, without the express written consent of the registered owner hereof, or (2) reduce the percentage of Certificates required for the written consent to any amendment, or (3) modify any rights or obligations of the Trustee without its prior written assent thereto.

The Certificates are delivered as fully registered Certificates in Authorized Denominations. This Certificate is being issued initially in a Weekly Mode and so long as this Certificate shall remain in a Weekly Mode, this Certificate shall bear interest at a Weekly Rate determined by the provisions of the Trust Agreement.

As provided in and subject to the terms and conditions of the Trust Agreement, the Certificates may, from time to time, be changed from a Weekly Mode to a Daily Mode, a Flexible Mode, a Term Rate Mode or a Fixed Rate Mode.

Except in the event of serialization of the Certificates in accordance with the provisions of the Trust Agreement, the Certificates are subject to mandatory prepayment from Sinking Fund Payments prior to their Maturity Date, in part by lot, on October 1 of each year on and after October 1, 2008, in accordance with the schedule set forth below upon notice as provided in the Trust Agreement, from and in the amount of the principal installment of the 2008 Payments due and payable on such dates, at a prepayment price equal to the sum of the principal amount evidenced and represented thereby plus accrued and unpaid interest evidenced and represented thereby to the Prepayment Date, without a prepayment premium.

Sinking Fund Payments

Mandatory Sinking Fund Payment Date (October 1)	Sinking Fund Payment	Mandatory Sinking Fund Payment Date (October 1)	Sinking Fund Payment
2008	\$290,000	2023	\$2,300,000
2009	285,000	2024	2,410,000
2010	285,000	2025	2,515,000
2011	285,000	2026	2,595,000
2012	310,000	2027	2,705,000
2013	310,000	2028	2,810,000
2014	340,000	2029	2,945,000
2015	340,000	2030	3,055,000
2016	365,000	2031	3,185,000
2017	365,000	2032	3,295,000
2018	395,000	2033	3,430,000
2019	395,000	2034	3,570,000
2020	395,000	2035	3,705,000
2021	425,000	2036	3,870,000
2022	450,000		

Additionally, if any portion of this Certificate has been optionally prepaid as described in the succeeding paragraph, the amounts of such Sinking Fund Payments shall be reduced as

directed by the Authority, or if not so directed, proportionately in increments of Authorized Denominations by the principal amount evidenced and represented by all such Certificates so optionally prepaid.

Each Certificate in a Daily Mode or a Weekly Mode shall be subject to prepayment at the option of the Authority, in whole or in part, in Authorized Denominations on any Business Day, at a prepayment price equal to 100% of the principal amount thereof, plus, accrued interest, if any, to the Prepayment Date, without premium.

Notice of prepayment of any Certificate selected for prepayment shall be given by first-class mail not less than 30 days nor more than 60 days before the prepayment date to the registered owner hereof, subject to and in accordance with provisions of the Trust Agreement with respect thereto. If notice of prepayment has been duly given and money for the payment of the prepayment price is held by the Trustee, then this Certificate shall, on the prepayment date designated in such notice, become due and payable, and from and after the date so designated interest evidenced and represented by this Certificate shall cease to accrue, and the registered owner of this Certificate shall have no rights with respect hereto except to receive payment of the prepayment price hereof.

This Certificate is transferable on the books to be kept for that purpose at the above-mentioned office of the Trustee by the registered owner hereof in person or by his duly authorized attorney upon payment of the charges provided in the Trust Agreement and upon surrender of this Certificate for cancellation accompanied by delivery of a duly executed written instrument of transfer in a form acceptable to the Trustee, and thereupon a new Certificate or Certificates of the same Certificate Payment Date evidencing and representing a like aggregate principal amount in Authorized Denominations will be delivered to the transferee. This Certificate may be exchanged at the above-mentioned office of the Trustee upon payment of the charges provided in the Trust Agreement for a like aggregate principal amount of Certificates of the same Certificate Payment Date of other Authorized Denominations. The Trustee may deem and treat the registered owner hereof as the absolute owner hereof for the purpose of receiving payment of the interest and principal evidenced and represented hereby and for all other purposes, whether this Certificate shall be overdue or not, and the Trustee shall not be affected by any notice or knowledge to the contrary; and payment of the interest and principal and prepayment premium, if any, evidenced and represented by this Certificate shall be made only to such registered owner, which payments shall be valid and effectual to satisfy and discharge liability on this Certificate to the extent of the sum or sums so paid.

The Certificates each evidence and represent a proportionate interest in the 2008 Payments in an amount equal to the aggregate principal amount of Certificates originally executed and delivered by the Trustee pursuant to the Trust Agreement and enjoy the benefits of a security interest in the moneys held in the funds established pursuant to the Trust Agreement, subject to the provisions of the Trust Agreement permitting the disbursement thereof for or to the purposes and on the conditions and terms set forth therein. The obligation of the City to make the 2008 Payments is a special obligation of the City payable solely from the Gross Revenues of the Water Utility System as provided in the Contract, and does not constitute a debt of the City or of the State of California or of any political subdivision thereof in contravention of any

constitutional or statutory debt limitation or restriction. The City may incur other obligations payable on parity with the 2008 Payments in accordance with the Contract.

The Trustee has no obligation or liability to the Certificate owners for the payment of the interest or principal or the prepayment premiums, if any, evidenced and represented by the Certificates; but rather the Trustee's sole obligations are to administer, for the benefit of the City and the Certificate owners, the various funds established under the Trust Agreement.

No member, officer or employee of the Authority shall be individually or personally liable for the payment of the interest or principal or prepayment premiums, if any, evidenced and represented by the Certificates by reason of their delivery, but nothing herein contained shall relieve any such member, officer or employee from the performance of any official duty provided by applicable provisions of law or hereby.

The Trust Agreement prescribes the manner in which it may be discharged and after which the Certificates shall no longer be secured by or entitled to the benefits of the Trust Agreement.

IN WITNESS WHEREOF, this Certificate has been executed by the manual signature of an authorized signatory of the Trustee as of the date set forth above.

THE BANK OF NEW YORK MELLON TRUST  
COMPANY, N.A.,  
as Trustee

By: \_\_\_\_\_  
Authorized Officer

ASSIGNMENT

For value received the undersigned hereby sells, assigns and transfers unto \_\_\_\_\_ (Taxpayer Identification Number: \_\_\_\_\_) the within Certificate and all rights thereunder, and hereby irrevocably constitutes and appoints \_\_\_\_\_ attorney to transfer the within Certificate on the books kept for registration thereof, with full power of substitution in the premises.

Dated: \_\_\_\_\_

Note: The signature to this Assignment must correspond with the name as written on the face of the Certificate in every particular, without alteration or enlargement or any change whatever.

Signature Guaranteed: \_\_\_\_\_

Notice: Signature must be guaranteed by an eligible guarantor institution.

## STATEMENT OF INSURANCE

Assured Guaranty Corp. ("Assured Guaranty"), a Maryland-domiciled insurance company, has delivered its financial guaranty insurance policy (the "Policy") with respect to the scheduled payments of principal of and interest on this Certificate to The Bank of New York Trust Company, N.A., as paying agent on behalf of the holders of the Certificates (the "Paying Agent"). Such Policy is on file and available for inspection at the principal office of the Paying Agent and a copy thereof may be obtained from Assured Guaranty or the Paying Agent. All payments required to be made under the Policy shall be made in accordance with the provisions thereof. The owner of this Certificate acknowledges and consents to the subrogation rights of Assured Guaranty as more fully set forth in the Policy.

FIRST AMENDMENT TO THE  
REIMBURSEMENT AGREEMENT

This First Amendment to the Reimbursement Agreement (this “Amendment”) is made and entered into as of June 5, 2014 between the CITY OF MODESTO, a charter city and municipal corporation organized under the Constitution and laws of the State of California (the “Applicant”), and JPMORGAN CHASE BANK, NATIONAL ASSOCIATION, a national banking association (the “Bank”).

W I T N E S S E T H

WHEREAS, the Applicant and the Bank are parties to the Reimbursement Agreement, dated as of July 1, 2011 (the “Agreement,” unless otherwise defined herein, capitalized terms used herein and defined in the Agreement shall have the same meaning herein as therein defined);

WHEREAS, the Applicant desires to extend the Stated Expiration Date of Letter of Credit No. CPCS-923992 (the “Letter of Credit”) as stated herein below;

WHEREAS, the Bank is willing to extend the Stated Expiration Date of the Letter of Credit upon the terms and conditions set forth in this Amendment.

NOW, THEREFORE, in consideration of the foregoing, the premises and mutual covenants contained herein and for other valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto hereby agree as follows:

1. Effectiveness of this Amendment. This Amendment shall become effective as provided herein at the time (the “Amendment Effective Time”) on the first date (the “Amendment Effective Date”) on which each of the following conditions shall be satisfied or waived by the Bank:

(a) Execution of this Amendment. The Applicant and the Bank shall have executed a copy of this Amendment (whether the same or different copies) and the Applicant shall have delivered the same to the Bank.

(b) No Default; Representations and Warranties. The Bank shall be satisfied that, immediately prior to the Amendment Effective Time and after giving effect to this Amendment, (i) there shall exist no Default or Event of Default under the Agreement and (ii) the representations and warranties of the Applicant contained in this Amendment are true and correct in all material respects as of the Amendment Effective Time with the same effect as though such representations and warranties had been made at the Amendment Effective Time.

(c) Payments. The Bank shall have received all amounts, if any, owing under the Agreement and the Fee Letter from the Applicant through and including the Amendment Effective Date.

(d) Amended and Restated Fee Letter. The Applicant and the Bank shall have executed (whether the same or different copies) a letter agreement amending and restating the Fee Letter (the “Amended and Restated Fee Letter”) and the Applicant shall have delivered the same to the Bank.

(e) Authority. The Bank shall have received evidence satisfactory to it that the Applicant has the authority to enter into this Amendment and the Amended and Restated Fee Letter.

2. Amendment to Agreement. At the Amendment Effective Time:

(a) Section 1.1 of the Agreement shall be amended by adding the following defined terms in alphabetical order:

“Anti-Corruption Laws” means all laws, rules, and regulations of any jurisdiction applicable to the Applicant from time to time concerning or relating to bribery or corruption.

“Sanctions” means economic or financial sanctions or trade embargoes imposed, administered or enforced from time to time by the U.S. government, including those administered by the Office of Foreign Assets Control of the U.S. Department of the Treasury or the U.S. Department of State.

“Sanctioned Country” means, at any time, a country or territory which is the subject or target of any Sanctions.

“Sanctioned Person” means, at any time, (a) any Person listed in any Sanctions-related list of designated Persons maintained by the Office of Foreign Assets Control of the U.S. Department of the Treasury, the U.S. Department of State or by the United Nations Security Council, (b) any Person operating, organized or resident in a Sanctioned Country or (c) any Person controlled by any such Person.

(b) Article 4 of the Agreement shall be amended by adding the following Section after Section 4.19:

Section 4.20 Anti-Corruption Laws and Sanctions. The Applicant and its officers and employees, and, to the knowledge of the Applicant, its council members and agents, are in compliance with Anti-Corruption Laws and applicable Sanctions in all material respects. Neither the issuance nor the maintenance of the Letter of Credit or other transactions contemplated by this Agreement will violate Anti-Corruption Laws or applicable Sanctions.

(c) Section 5.8 of the Agreement shall be amended by adding the following sentence to the end of said Section:

The Applicant will maintain in effect and enforce policies and procedures designed to ensure compliance by the Applicant and its officers, employees and agents with Anti-Corruption Laws and applicable Sanctions.

(d) Section 5.10 of the Agreement shall be amended by adding the following sentence to the end of said Section:

The Applicant shall not use, and shall procure that its officers, employees and agents shall not use, the proceeds of the Letter of Credit (i) in violation of any Anti-Corruption Laws or (ii) in any manner that would result in the violation of any Sanctions applicable to any party hereto.

(e) Section 7.1(b) of the Agreement shall be amended and restated in its entirety to read as follows:

(b) If a Change of Law shall:

(i) limit the deductibility of interest with respect to funds obtained by the Bank to pay any of its liabilities or subject the Bank to any tax, duty, charge, deduction or withholding on or with respect to payments relating to the Certificates of Participation, the Bank Documents, or any amount paid or to be paid by the Bank as the issuer of the Letter of Credit (other than any tax measured by or based upon the overall net income of the Bank imposed by any jurisdiction having control over the Bank);

(ii) impose, modify, require, make or deem applicable to the Bank any reserve requirement, capital requirement, special deposit requirement, insurance assessment or similar requirement against any assets held by, deposits with or for the account of, or loans, letters of credit or commitments by, an office of the Bank;

(iii) change the basis of taxation of payments due the Bank under the Bank Documents or the Certificates of Participation (other than by a change in taxation of the overall net income of the Bank);

(iv) cause or deem letters of credit to be assets held by the Bank and/or as deposits on its books; or

(v) impose upon the Bank any other condition with respect to any amount paid or payable to or by the Bank or with respect to any Related Documents;

and the result of any of the foregoing shall be to increase the cost to the Bank of making any payment under or maintaining the Letter of Credit, the commitment to make Liquidity Advances or making any Liquidity Advance, or to reduce the amount of any sum received or receivable by the Bank hereunder (whether of principal, interest or otherwise) or under the Fee Letter, then the Applicant will pay to the Bank such

additional amount or amounts as will compensate the Bank for such additional costs incurred or reduction suffered.

If the Bank determines that any Change of Law regarding capital or liquidity requirements has or would have the effect of reducing the rate of return on the Bank's capital or on the capital of the Banks holding company, if any, as a consequence of this Agreement, the Letter of Credit or Liquidity Advances made by the Bank to a level below that which the Bank or the Bank's holding company could have achieved but for such Change of Law (taking into consideration the Bank's policies and the policies of the Bank's holding company with respect to capital adequacy and liquidity), then from time to time the Applicant will pay to the Bank such additional amount or amounts as will compensate the Bank or the Bank's holding company for any such reduction suffered.

A certificate of the Bank setting forth the amount or amounts reasonably determined by the Bank in good faith to be necessary to compensate the Bank or its holding company, as the case may be, as specified above shall be delivered to the Applicant by the Bank together with a reasonably detailed description of the way in which such amount has been calculated, and shall be conclusive absent fraud or manifest error. The Applicant shall pay the Bank the amount shown as due on any such certificate within 10 days after receipt thereof.

The protection of this Section 7.1(b) shall be available to the Bank regardless of any possible contention of invalidity or inapplicability of the law, regulation or condition which has been imposed; *provided, however*, that if it shall be later determined by the Bank that any amount so paid by the Applicant pursuant to this Section 7.1(b) is in excess of the amount payable under the provisions hereof, the Bank shall refund such excess amount to the Applicant.

3. Representations and Warranties. The Applicant hereby makes, as of the Amendment Effective Date, each of the representations and warranties set forth in Article 4 of the Agreement (including those amended by this Amendment), and such representations and warranties are, by this reference, incorporated herein as if set forth herein in their entirety, provided that references to "Agreement" shall, for purposes of this paragraph, be deemed to include this Amendment.

4. Extension of Expiration Date. At the Amendment Effective Time, the Bank shall execute and deliver to the Trustee an extension to Letter of Credit in the form of Annex H to the Letter of Credit extending the Stated Expiration Date thereof to July 14, 2017.

5. Miscellaneous.

(a) Except as expressly modified by this Amendment, the Agreement shall continue to be and remain in full force and effect in accordance with their respective terms.

(b) This Amendment may be executed in any number of counterparts and by facsimile or electronic means, each of which shall constitute an original, but all of which when taken together shall constitute but one instrument.

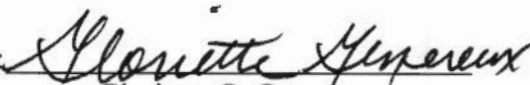
(c) PURSUANT TO SECTION 5-1401 OF THE NEW YORK GENERAL OBLIGATIONS LAW (OR ANY SUCCESSOR STATUTE THERETO), THIS AMENDMENT SHALL BE DEEMED TO BE A CONTRACT UNDER, AND SHALL BE GOVERNED BY, AND CONSTRUED AND INTERPRETED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF NEW YORK WITHOUT REGARD TO CHOICE OF LAW RULES; PROVIDED, HOWEVER, THAT THE LAWS OF THE STATE OF CALIFORNIA SHALL GOVERN THE INTERPRETATION OF THIS AMENDMENT AS IT RELATES TO THE CAPACITY, POWER AND AUTHORITY OF THE APPLICANT TO ENTER INTO AND PERFORM ITS OBLIGATIONS UNDER THIS AMENDMENT.

(d) This Amendment may be executed by facsimile signature and each such signature shall be treated in all respects as having the same effect as an original signature.

*[Remainder of page intentionally left blank.]*

IN WITNESS WHEREOF, each of the City and the Bank has caused this Amendment to be signed in its name by one or more officers, all as of the day and year first above written.

CITY OF MODESTO

By:   
Name: Gloriette G. Genereux  
Title: Finance Director

JPMORGAN CHASE BANK, N.A.

By: James G. Millard  
Name: James G. Millard  
Title: Executive Director

# J.P.Morgan

June 5, 2014

City of Modesto  
1010 Tenth Street, Suite 5200  
Modesto, CA 95353  
Attention: Finance Director

Ladies and Gentlemen:

Reference is made to (i) the Reimbursement Agreement, dated as of July 1, 2011 (the “**Existing Agreement**”), and the First Amendment to the Reimbursement Agreement, dated as of June 5, 2014 (the “**First Amendment**”; together with the Existing Agreement, the “**Agreement**”), in each case between City of Modesto (the “**City**”) and JPMorgan Chase Bank, N.A. (the “**Bank**”) and (ii) the letter agreement regarding fees and expenses dated as of July 14, 2011, from the Bank to the City (the “**Existing Fee Letter**”). Any capitalized term below that is defined in the Agreement shall have the same meaning when used herein. This letter agreement (this “**Fee Letter**”) amends and restates the Existing Fee Letter in its entirety. This letter is the Fee Letter described in the Agreement.

In order to induce the Bank to enter into the First Amendment and to extend the stated expiration date of the Letter of Credit, the City agrees to make the following payments at the following times:

(1) A facility fee (the “**Facility Fee**”) for each day on the Available Amount as of the close of business of the Bank on such day, at the Facility Fee Rate (as defined below), payable quarterly in arrears on the first Business Day of each January, April, July and October (commencing on October 1, 2011, for the period from and including July 14, 2011 to and including September 30, 2011) until the Termination Date and on the Termination Date. As used herein, “**Facility Fee Rate**” means the rate per annum set forth in the grid below opposite Level 1; provided, however, if any Rating Agency downgrades its rating of the unenhanced long-term debt (including certificates of participation) of the Applicant secured by Gross Revenues (each, a “**Rating**”) to a level less than Level 1, the applicable “**Facility Fee Rate**” shall be the rate per annum set forth in the grid below opposite the level that corresponds to (i) the level that contains both Ratings in the event the Ratings fall within a single level or (ii) the level that contains the lowest rating in the event that the Ratings fall within different levels (it being understood that Level 1 is the highest level and Level 7 is the lowest level):

LEVEL	MOODY'S RATING	S&P RATING	FACILITY FEE RATE PRIOR TO JULY 14, 2014	FACILITY FEE RATE FROM AND AFTER JULY 14, 2014
LEVEL 1	Aa3 or better	AA- or better	1.20%	0.875%
LEVEL 2	A1	A+	1.30%	1.075%
LEVEL 3	A2	A	1.50%	1.275%
LEVEL 4	A3	A-	1.70%	1.475%

LEVEL 5	Baa1	BBB+	1.90%	1.775%
LEVEL 6	Baa2	BBB	2.10%	2.075%
LEVEL 7	Baa3 or below	BBB- or below	2.30%	2.375%

Notwithstanding the foregoing, (A) the Facility Fee Rate shall be increased by 1.00% per annum from the Facility Fee Rate in effect immediately prior thereto in the event that, and for so long as, any Rating is withdrawn or suspended by any Rating Agency and (B) the Facility Fee Rate shall be increased by 1.00% per annum from the Facility Fee Rate in effect immediately prior thereto upon the occurrence and during the continuance of an Event of Default. Any change in the Facility Fee Rate resulting from a change in a Rating shall be and become effective as of and on the date of the announcement of the change in such Rating.

(2) In the event the Letter of Credit is terminated or the Available Amount is permanently reduced (other than as a result of the payment of or scheduled prepayment of the Bonds) prior to the Stated Expiration Date, the City shall pay the Bank a fee (the "**Termination Fee**") on the date of termination or permanent reduction equal to the Facility Fee that would have been payable to the Bank pursuant to preceding paragraph (1) but for the termination or permanent reduction for the period from and including the date on which the Letter of Credit is terminated or the Available Amount is permanently reduced to and including the Stated Expiration Date assuming (A) a Facility Fee Rate equal to the Facility Fee Rate in effect immediately prior to the date on which the Letter of Credit is terminated or the Available Amount is permanently reduced; and (B) the Available Amount is fully reinstated (*i.e.*, at its maximum amount) immediately prior to the date on which Letter of Credit is terminated or the Available Amount is permanently reduced; provided, however, that the Termination Fee shall not be payable if (i) the short-term ratings of the Bank fall below a level of "P1" by Moody's or "A-1" by S&P or (ii) the COPS are paid, prepaid or defeased in full or in part, whether by refunding or otherwise, with the proceeds of Indebtedness of the City that is not (a) secured or supported by a letter of credit, liquidity facility, credit agreement or other agreement issued or executed by a financial institution or (b) in the form of notes or certificates that are purchased by a financial institution (e.g., floating rate notes).

(3) A draw fee of \$300 for each drawing presented under the Letter of Credit, payable on each Business Day on which the Bank pays the amount requested in a drawing. For the avoidance of doubt, the draw fee shall only be payable if the Bank advances funds pursuant to a drawing.

(4) At the time of any transfer of the Letter of Credit, a fee of \$3,000 plus reasonable attorneys' fees and expenses.

(5) At the time the City requests an amendment, or seeks the Bank's consent to any amendment, of any Related Document, a fee of \$3,000 plus reasonable attorneys' fees and expenses, which fee shall be earned and payable whether or not any such amendment is executed or consent granted.

(6) At the time the City requests a waiver, or seeks the Bank's consent to a waiver, of any provision of any Related Document, such fee as the Bank may determine in its sole discretion, plus reasonable attorneys' fees and expenses, which fee shall be earned and payable whether or not any such waiver is executed or consent granted.

(7) On the Amendment Effective Date, the fees and expenses of McGuireWoods LLP, counsel to the Bank, in an amount not to exceed \$12,500.

All amounts paid pursuant to this Fee Letter shall be non-refundable. Computations of the Facility Fee and the Termination Fee shall be made on the basis of a 360 day year and actual days elapsed.

All payments to be made by the City to the Bank pursuant to this Fee Letter shall be in the manner and at the times set forth in the Agreement.

This Fee Letter may not be amended or waived except by an instrument in writing signed by the Bank and the City. This Fee Letter may be executed in any number of counterpart, each of which shall be an original, and all of which, when taken together, shall constitute one agreement. Delivery of an executed signature page of this Fee Letter by electronic transmission shall be effective as delivery of a manually executed counterpart hereof.

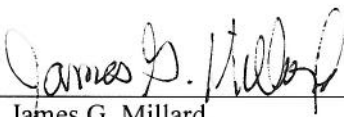
This Fee Letter is delivered to the City on the understanding that neither this Fee Letter nor any of its terms shall be disclosed, directly or indirectly, to any other person except (a) the City's council members, officers, employees, accountants, attorneys, agents and advisors who are directly involved in the consideration of this matter on a confidential and need-to-know basis and for whom the City shall be responsible for any breach by any of them of this confidentiality undertaking; (b) under compulsion of law (whether by interrogatory, subpoena, civil investigative demand or otherwise) or by order of any court or governmental or regulatory body; or (c) to any person requesting a copy of this Fee Letter as a public record, provided that, in the case of clauses (b) and (c), the City shall (to the extent permitted) give the Bank reasonable prior notice of such disclosure and an opportunity to restrain such disclosure.

*[Remainder of page intentionally left blank.]*

Please confirm that the foregoing is our mutual understanding by signing and returning to the Bank an executed counterpart of this Fee Letter. This Fee Letter shall become effective as of the date first above referenced upon our receipt of an executed counterpart of this Fee Letter from the City.

Very truly yours,

JPMORGAN CHASE BANK, NATIONAL  
ASSOCIATION

By:   
Name: James G. Millard  
Title: Executive Director

Accepted and agreed to  
as of the date first  
written above by:

CITY OF MODESTO

By: *Gloriette Genereux*  
Name: Gloriette G. Genereux  
Title: Finance Director

**JPMorgan Chase Bank, N.A.**

Global Trade Services

131 South Dearborn

5<sup>th</sup> Floor, Mail Code IL-0236

Chicago, IL 60603-5506

Tel: (800) 634-1969 Fax: (312) 954-6163

SWIFT: CHASUS33

NOTICE OF EXTENSION AMENDMENT

June 6, 2014

CUSIP No. 607804AC5

The Bank of New York Mellon Trust Company, N.A.  
100 Pine Street, Suite 3100  
San Francisco, California 94111

Attention: Corporate Trust Department, Sheila Bowman


Ladies and Gentlemen:

Reference is hereby made to that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "*Letter of Credit*"), established by us in your favor as Beneficiary related to the Authority's \$46,765,000 Water Revenue Refunding Certificates of Participation 2008 Series A (the "*Certificates*"). We hereby notify you that, in accordance with the terms of the Letter of Credit and that certain Reimbursement Agreement dated as of July 1, 2011, between the City of Modesto and us, the Stated Expiration Date (as defined in the Letter of Credit) has been extended to July 14, 2017.

The Trustee's name is corrected as herein above stated.

This letter shall be attached to the Letter of Credit and made a part thereof.

JPMORGAN CHASE BANK, N.A.

By:   
Name: KATHERINE M. MOSES  
Title: ASSOCIATE



Shipment Receipt

Transaction Date: 06 Jun 2014

Tracking Number:

1ZR7A9220199319366

<b>1</b> Address Information		
<b>Ship To:</b> THE BANK OF NEW YORK MELLON TRUST ATTN: SHEILA BOWMAN 100 PINE STREET, SUITE 3100 CORPORATE TRUST DEPARTMENT COMPANY, N.A. SAN FRANCISCO CA 941115217	<b>Ship From:</b> JPMorgan Chase Bank NA Patricia A Williams 131 S. Dearborn St - 5/F Chicago IL 606035506 Telephone:312 385-7233	<b>Return Address:</b> JPMorgan Chase Bank NA Patricia A Williams 131 S. Dearborn St - 5/F Chicago IL 606035506 Telephone:312 385-7233

<b>2</b> Package Information			
Weight	Dimensions / Packaging	Declared Value	Reference Numbers
1. Letter (Letter billable)	UPS Letter		Reference 1: - 487400 Letter of Credit Reference - CPCS-923992 Cost Center: -

<b>3</b> UPS Shipping Service and Shipping Options	
<b>Service:</b> <b>Guaranteed By:</b>	UPS Next Day Air 10:30 AM Monday, Jun 9, 2014 <b>Additional Shipping Options</b> <b>Quantum View Notify E-mail Notifications:</b> 1 patricia.g.williams@jpmchase.com: Ship

<b>4</b> Payment Information	
<b>Bill Shipping Charges to:</b>	Shipper's Account R7A922
You are not authorized to view rates information.All Shipping Charges in USD	

**Note:** Your invoice may vary from the displayed reference rates.

\* For delivery and guarantee information, see the UPS Service Guide. To speak to a customer service representative, call 1-800-PICK-UPS for domestic services and 1-800-782-7892 for international services.

**OFFICIAL STATEMENT SUPPLEMENT NO. 2, DATED JUNE 6, 2014**

**NOT A NEW ISSUE**

**\$47,625,000\***  
**CITY OF MODESTO, CALIFORNIA**  
**WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION**  
**2008 SERIES A**

**Dated: Date of Original Delivery**      **Price: 100%**      **CUSIP<sup>†</sup> 607804AC5**      **Due: October 1, 2036**  
**(May 30, 2008)**

This Official Statement Supplement No. 2 (this “Supplement”) sets forth certain information supplementary to that information contained in the Official Statement dated May 29, 2008 as supplemented by the Official Statement Supplement No. 1, dated July 5, 2011, and as amended by Amendment to Official Statement Supplement No. 1, dated July 5, 2011 (collectively, the “Original Official Statement”), relating to the City of Modesto, California Water Refunding Revenue Certificates of Participation 2008 Series A (the “2008 Certificates”). The 2008 Certificates were executed and delivered pursuant to a Trust Agreement, dated as of May 1, 2008, by and between the Modesto Public Financing Authority (the “Authority”) and The Bank of New York Trust Company, N.A., as trustee (the “Trustee”) , as amended and restated by an Amended and Restated Trust Agreement, dated as of May 1, 2008, as amended and restated on July 14, 2011, by and between the Authority and the Trustee, for the principal purpose of refinancing certain improvements to the Water Utility System of the City of Modesto (the “City”).

The 2008 Certificates are currently in a Weekly Mode. Payment of the purchase price of the 2008 Certificates upon optional or mandatory tender for purchase are currently supported by an irrevocable direct pay letter of credit (the “JPMorgan Letter of Credit”) issued by JPMorgan Chase Bank, National Association, (“JPMorgan”). *On or about June 6, 2014, the expiration date of the JPMorgan Letter of Credit will be extended from July 14, 2014 to July 14, 2017.* For additional information relating to JPMorgan, see APPENDIX A – “INFORMATION CONCERNING JPMORGAN CHASE BANK, NATIONAL ASSOCIATION,” which additional information has been provided by JPMorgan, and no representation is made by the Authority or the City as to the accuracy or completeness or the adequacy of such information.

Information with respect to the 2008 Certificates is contained in the Original Official Statement, as supplemented by this Supplement. This Supplement should be read together with the Original Official Statement. To the extent that the information in this Supplement conflicts with the information in the Original Official Statement, this Supplement shall govern. No attempt has been made to update the Original Official Statement except as specifically set forth in this Supplement. For more recent information relating to the Water Utility System of the City, see the most recent Comprehensive Annual Financial Report, available on the City’s website at <http://www.modestogov.com>. The City’s website is not incorporated herein by reference. Unless otherwise defined in this Supplement, all terms used herein shall have the same meanings as those terms in the Original Official Statement.

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\* Original principal amount. As of the date of this Supplement the Certificates are outstanding in the principle amount of \$45,860,000.

† Copyright 2014, American Bankers Association. CUSIP® is a registered trademark of the American Bankers Association. The CUSIP data herein is provided by the CUSIP Service Bureau, managed on behalf of the American Bankers Association by Standard & Poor’s. The CUSIP numbers are not intended to create a database and do not serve in any way as a substitute for CUSIP service. CUSIP numbers have been assigned by an independent company not affiliated with the City and are provided solely for convenience and reference. None of the Authority, the City or the Remarketing Agent takes any responsibility for the accuracy of such numbers.

**MISCELLANEOUS**

This Supplement is not to be construed as a contract or agreement between the Authority or the City and the purchasers or holders of any of the 2008 Certificates. Any statements made in this Supplement involving matters of opinion, whether or not expressly so stated, are intended merely as an opinion and not as representations of fact. The information and expressions of opinion herein are subject to change without notice and neither the delivery of this Supplement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the Authority, the City, the Water Utility System or JPMorgan since the date hereof.

This Supplement has been duly approved, executed and delivered by the City and the Authority.

**CITY OF MODESTO, CALIFORNIA**

By: /s/ James N. Holgersson  
James N. Holgersson  
City Manager

**MODESTO PUBLIC FINANCING AUTHORITY**

By: /s/ Gloriette Genereux  
Gloriette Genereux  
Auditor and Treasurer

## **APPENDIX A**

### **INFORMATION CONCERNING JPMORGAN CHASE BANK, NATIONAL ASSOCIATION**

JPMorgan Chase Bank, National Association (the “Bank”) is a wholly owned subsidiary of JPMorgan Chase & Co., a Delaware corporation whose principal office is located in New York, New York. The Bank offers a wide range of banking services to its customers, both domestically and internationally. It is chartered and its business is subject to examination and regulation by the Office of the Comptroller of the Currency.

As of March 31st, 2014, the Bank had total assets of \$1,970.5 billion, total net loans of \$617.5 billion, total deposits of \$1,335.1 billion, and total stockholder’s equity of \$173.9 billion. These figures are extracted from the Bank’s unaudited Consolidated Reports of Condition and Income (the “Call Report”) as of March 31st, 2014, prepared in accordance with regulatory instructions that do not in all cases follow U.S. generally accepted accounting principles. The Call Report including any update to the above quarterly figures is filed with the Federal Deposit Insurance Corporation and can be found at [www.fdic.gov](http://www.fdic.gov).

Additional information, including the most recent annual report on Form 10-K for the year ended December 31, 2013, of JPMorgan Chase & Co., the 2013 Annual Report of JPMorgan Chase & Co., and additional annual, quarterly and current reports filed with or furnished to the Securities and Exchange Commission (the “SEC”) by JPMorgan Chase & Co., as they become available, may be obtained without charge by each person to whom this Official Statement is delivered upon the written request of any such person to the Office of the Secretary, JPMorgan Chase & Co., 270 Park Avenue, New York, New York 10017 or at the SEC’s website at [www.sec.gov](http://www.sec.gov).

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The information contained in this Appendix relates to and has been obtained from the Bank. The delivery of the Supplement shall not create any implication that there has been no change in the affairs of the Bank since the date hereof, or that the information contained or referred to in this Appendix is correct as of any time subsequent to its date.

**AMENDMENT TO OFFICIAL STATEMENT SUPPLEMENT NO. 1, DATED JULY 5, 2011**

**\$47,625,000**

**CITY OF MODESTO, CALIFORNIA  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A**

This Amendment, dated July 12, 2011 (this "Amendment"), to the Official Statement Supplement No. 1, dated July 5, 2011 ("Official Statement Supplement"), relating to the City of Modesto, California Water Refunding Revenue Certificates of Participation 2008 Series A, is intended to be read in conjunction with the Official Statement Supplement. This Amendment constitutes an integral part of the Official Statement Supplement and recipients are requested to attach this Amendment to the Official Statement Supplement.

**PLEASE BE ADVISED that the Official Statement Supplement has been amended to add the following information:**

• *The section below contained in APPENDIX D-DEFINITIONS AND SUMMARY OF THE AMENDED AND RESTATED TRUST AGREEMENT commencing on page D-23 of the Official Statement Supplement and ending on page D-24 of the Official Statement Supplement is hereby deleted in its entirety and replaced with the following:*

Control of Remedies by Credit Facility Provider or Liquidity Facility Provider. As long as no Control Event has occurred, notwithstanding anything in the Trust Agreement to the contrary, the 2008 Certificate Insurer will have the right to direct all remedies upon the occurrence of an Event of Default. If a Control Event has occurred and the Bank's Credit Enhancement is in effect, notwithstanding anything in the Trust Agreement to the contrary, the Bank will have the right to direct all remedies upon the occurrence of an Event of Default. If a Control Event has occurred and the Bank's Credit Enhancement is no longer in effect, notwithstanding anything in the Trust Agreement to the contrary, the Liquidity Facility Provider will have the right to direct all remedies upon the occurrence of an Event of Default.

Notwithstanding the foregoing, if a Liquidity Facility is in effect, and the Provider thereof has failed to honor its payment obligations under the Liquidity Facility in respect of the purchase price of Certificates upon tender thereof, fifty-one percent (51%) of the Certificate holders of the Certificates enhanced by such Liquidity Facility (excluding Certificates owned by the City and Bank Certificates), will have the right at any time, by an instrument or instruments in writing executed and delivered to the Trustee, to direct the method and place of conducting all proceedings to be taken in connection with the enforcement of such payment obligations; provided that such direction will be in accordance with applicable law.

The delivery of this Amendment to the Official Statement Supplement has been duly authorized by the City of Modesto and the Modesto Public Financing Authority.

Amendment Dated: July 12, 2011

CITY OF MODESTO, CALIFORNIA

By: /s/ Gloriette G. Beck  
Finance Director/Treasurer

MODESTO PUBLIC FINANCING AUTHORITY

By: /s/ Gloriette G. Beck  
Auditor and Treasurer

**NOT A NEW ISSUE**

**RATINGS:**

See “RATINGS” herein

**\$47,625,000**  
**CITY OF MODESTO, CALIFORNIA**  
**WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION**  
**2008 SERIES A**

**Dated: Date of Original Delivery**  
**(May 30, 2008)**

**Price: 100%**

**CUSIP<sup>†</sup> 607804AC5**

**Due: October 1, 2036**

This Official Statement Supplement No. 1 (this “Supplement”) sets forth certain information supplementary to that information contained in the Official Statement dated May 29, 2008 (the “Original Official Statement”), relating to the City of Modesto, California Water Refunding Revenue Certificates of Participation 2008 Series A (the “2008 Certificates”). The 2008 Certificates were executed and delivered pursuant to a Trust Agreement, dated as of May 1, 2008, by and between the Modesto Public Financing Authority (the “Authority”) and The Bank of New York Trust Company, N.A., as trustee, for the principal purpose of refinancing certain improvements to the Water Utility System of the City of Modesto (the “City”).

Information with respect to the 2008 Certificates is contained in the Original Official Statement, as supplemented by this Supplement. This Supplement should be read together with the Original Official Statement (a copy of which is attached hereto as Appendix A and incorporated herein by reference). To the extent that the information in this Supplement conflicts with the information in the Original Official Statement, this Supplement shall govern. No attempt has been made to update the Original Official Statement except as specifically set forth in this Supplement. Unless otherwise defined in this Supplement, all terms used herein shall have the same meanings as those terms in the Original Official Statement.

The 2008 Certificates are currently in a Weekly Mode. Interest with respect to the 2008 Certificates accruing at the Daily Rate, Weekly Rate or Flexible Rate will be computed upon the basis of a 365 or 366-day year, as applicable, for the actual number of days elapsed.

Funds for the payment of the purchase price of the 2008 Certificates upon optional or mandatory tender for purchase are currently available (subject to certain conditions precedent and automatic termination events) under a Standby Certificate Purchase Agreement, dated as of May 1, 2008 (the “Standby Purchase Agreement”), between the Authority and Bank of America, N.A., as the liquidity facility provider. On July 14, 2011 (the “Substitution Date”), the Standby Purchase Agreement will be replaced by an irrevocable direct pay letter of credit (the “JPMorgan Letter of Credit”) issued by JPMorgan Chase Bank, National Association, (“JPMorgan”) which will expire on July 14, 2014, as described herein. The 2008 Certificates will be subject to mandatory tender on the Substitution Date. After the Substitution Date, the Trustee will be required to draw on the JPMorgan Letter of Credit to pay the interest and scheduled principal (on sinking fund payments) on the 2008 Certificates, as well as the purchase price of the 2008 Certificates upon any optional or mandatory tender if remarketing proceeds are insufficient therefor. J. P. Morgan Securities LLC will serve as remarketing agent for the 2008 Certificates (the “Remarketing Agent”).

**J.P.Morgan**

The scheduled payment of principal of and interest on the 2008 Certificates when due will, to the extent that JPMorgan fails to honor a properly presented and conforming draw under the JPMorgan Letter of Credit, continue to be guaranteed under financial guaranty insurance policy previously issued by Assured Guaranty Corp. for the 2008 Certificates.



*Certain legal matters in connection with the delivery of the JPMorgan Letter of Credit will be passed upon for the City by Sidley Austin LLP, San Francisco, California, Special Counsel. Certain legal matters will be passed upon for the City and the Authority by the City Attorney of the City and for JPMorgan by White & Case, LLP, Los Angeles, California.*

**J.P. MORGAN**

<sup>†</sup> Copyright 2008, American Bankers Association. CUSIP data is provided by Standard & Poor’s CUSIP Service Bureau, a Division of the McGraw-Hill Companies, Inc., and is set forth herein for convenience of reference only. None of the Authority, the City or the Remarketing Agent takes any responsibility for the accuracy of such numbers.

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**OFFICIAL STATEMENT SUPPLEMENT NO. 1, DATED JULY 5, 2011 RELATING TO**

**\$47,625,000**

**CITY OF MODESTO, CALIFORNIA  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A**

**INTRODUCTION**

The purpose of this Official Statement Supplement No. 1 (this “Supplement”) is to supplement the Official Statement dated May 29, 2008 (the “Original Official Statement”), relating to the \$47,625,000 City of Modesto, California Water Refunding Revenue Certificates of Participation 2008 Series A (the “2008 Certificates”). The 2008 Certificates are currently outstanding in the aggregate principal amount of \$46,765,000. This Supplement provides information concerning the substitution, as of July 14, 2011 (the “Substitution Date”), of an irrevocable direct pay letter of credit (the “JPMorgan Letter of Credit”) issued by JPMorgan Chase Bank, National Association (“JPMorgan”) to provide for the payment of principal, purchase price and optional and mandatory sinking fund prepayment price of and interest represented by the 2008 Certificates. The JPMorgan Letter of Credit will expire on July 14, 2014.

The 2008 Certificates were executed and delivered pursuant to a Trust Agreement, dated as of May 1, 2008, (the “Original Trust Agreement”) by and between the Modesto Public Financing Authority (the “Authority”) and The Bank of New York Trust Company, N.A., as trustee, for the principal purpose of refinancing certain improvements to the Water Utility System of the City of Modesto (the “City”). In connection with the replacement of the Standby Purchase Agreement (defined below) by the JPMorgan Letter of Credit, the Original Trust Agreement will be amended and restated pursuant to an Amended and Restated Trust Agreement (the Original Trust Agreement as so amended and restated, the “Amended Trust Agreement”). The provisions of the Amended Trust Agreement will become effective on the Substitution Date. The amendments to the Original Trust Agreement reflected in the Amended Trust Agreement consist solely of revisions required to accommodate a direct pay letter of credit as security for the Series 2008 Certificates. Definitions of certain terms used in this Supplement are set forth in APPENDIX D – “DEFINITIONS AND SUMMARY OF THE AMENDED AND RESTATED TRUST AGREEMENT.”

Funds for the payment of the purchase price of the 2008 Certificates that are subject to optional or mandatory tender for purchase are currently available (subject to certain conditions precedent and automatic termination events) under a Standby Certificate Purchase Agreement, dated as of May 1, 2008 (the “Standby Purchase Agreement”), between the Authority and Bank of America, N.A., as the liquidity facility provider. On the Substitution Date, the Standby Purchase Agreement will be replaced by the JPMorgan Letter of Credit. The 2008 Certificates will be subject to mandatory tender on the Substitution Date. The City has not obligated itself to purchase the 2008 Certificates in the event of a mandatory or optional tender.

The 2008 Certificates are currently in a Weekly Mode, and will remain in the Weekly Mode following the Substitution Date, until changed in accordance with the provisions of the Amended Trust Agreement. Interest with respect to the 2008 Certificates accruing at the Daily Rate, Weekly Rate or Flexible Rate will be computed upon the basis of a 365 or 366-day year, as applicable, for the actual number of days elapsed.

This Supplement also provides information about JPMorgan and Assured Guaranty Corp. (“AGC” or the “2008 Insurer”) which has been provided by JPMorgan and by the 2008 Insurer,

respectively. See “INFORMATION CONCERNING JPMORGAN” and “INFORMATION CONCERNING ASSURED GUARANTY CORP.” below.

Information with respect to the 2008 Certificates is contained in the Original Official Statement, as supplemented by this Supplement. This Supplement should be read together with the Original Official Statement (a copy of which is attached hereto as Appendix A and incorporated herein by reference). To the extent that the information in this Supplement conflicts with the information in the Original Official Statement, this Supplement shall govern. No attempt has been made to update the Original Official Statement except as specifically set forth in this Supplement. See “THE WATER UTILITY SYSTEM.” Unless otherwise defined in this Supplement, all terms used herein shall have the same meanings as those terms in the Original Official Statement.

## **THE JPMORGAN LETTER OF CREDIT AND THE REIMBURSEMENT AGREEMENT**

**POTENTIAL PURCHASERS OF THE 2008 CERTIFICATES SHOULD MAKE ANY DECISION WITH RESPECT TO THE PURCHASE, HOLDING OR TENDER OF SUCH 2008 CERTIFICATES BASED SOLELY UPON THE CREDIT OF JPMORGAN AND NOT THE CITY OR THE WATER UTILITY SYSTEM. THE CITY HAS NOT OBLIGATED ITSELF TO PURCHASE THE 2008 CERTIFICATES IN THE EVENT OF A MANDATORY OR OPTIONAL TENDER. CERTAIN INFORMATION INCLUDED IN THIS SUPPLEMENT WITH RESPECT TO THE CITY OR THE WATER UTILITY SYSTEM IS FOR INFORMATIONAL PURPOSES ONLY.**

### **The JPMorgan Letter of Credit**

The JPMorgan Letter of Credit will be effective on the Substitution Date, and will expire on July 14, 2014 unless extended by JPMorgan in its sole discretion upon the request of the City. The JPMorgan Letter of Credit will be issued in an amount equal to the aggregate principal amount of the outstanding 2008 Certificates, plus 56 days’ interest at a rate of 12% per annum calculated on the basis of the 365 day year and actual days elapsed. The Trustee will be required to draw on the JPMorgan Letter of Credit to pay the interest and scheduled principal (on sinking fund payments) on the 2008 Certificates, as well as the purchase price of the 2008 Certificates upon any optional or mandatory tender if remarketing proceeds are insufficient therefor. See APPENDIX E – “FORM OF LETTER OF CREDIT.”

### **The Reimbursement Agreement**

#### *General.*

The following summarizes certain provisions of the Reimbursement Agreement, dated as of July 1, 2011 (the “Reimbursement Agreement”), by and between the City and JPMorgan. Reference is made to the Reimbursement Agreement in its entirety for the detailed provisions thereof, copies of which are available for inspection from the Trustee.

The Reimbursement Agreement, which among other things, sets forth the terms and conditions whereby the City is required to repay to JPMorgan any amounts drawn by the Trustee under the JPMorgan Letter of Credit.

Under the Reimbursement Agreement, the City agrees to comply with various covenants, including but not limited to, covenants to: maintain its existence; maintain the Water Utility System; comply with applicable laws; maintain insurance; provide financial statements and other operating reports to JPMorgan; and maintain the tax-exempt status of the 2008 Certificates.

*Events of Default.*

Each of the following constitutes an “Event of Default” under the Reimbursement Agreement:

(a) (i) any representation or warranty made by the City in the Reimbursement Agreement (or incorporated therein by reference) or in any of the other Related Documents (defined to mean the Reimbursement Agreement, the agreement among the City, JPMorgan and JPMorgan of New York Trust Company, N.A., as custodian for JPMorgan in respect of 2008 Certificates purchased by JPMorgan from the proceeds of drawings made under the Letter of Credit (the “Custodian Agreement”), the letter agreement between the City and JPMorgan regarding fees and expenses (the “Fee Letter”), the Letter of Credit, the agreement among the 2008 Insurer, the City, the Trustee and JPMorgan regarding the circumstances and procedures under which the Policy can be cancelled (the “Cancellation Agreement”), the Trust Agreement, the Master Installment Purchase Contract between the City and the Authority (as amended and supplemented, the “Purchase Contract”), the Remarketing Agreement, the Policy, this Reoffering Circular and the 2008 Certificates and any other agreement or instrument relating thereto) or in any certificate, document, instrument, opinion or financial or other statement contemplated by or made or delivered pursuant to or in connection with the Reimbursement Agreement or with any of the other Related Documents that is not qualified by “materiality” or similar qualifier, shall prove to have been incorrect, incomplete or misleading in any material respect; or (ii) any representation or warranty made by the City in the Reimbursement Agreement (or incorporated therein by reference) or in any of the other Related Documents or in any certificate, document, instrument, opinion or financial or other statement contemplated by or made or delivered pursuant to or in connection with the Reimbursement Agreement or with any of the other Related Documents that is qualified by “materiality” or similar qualifier, shall prove to have been incorrect, incomplete or misleading in any respect; or

(b) any “event of default” shall have occurred under any of the Related Documents (as defined respectively therein) other than the Reimbursement Agreement; or

(c) failure to pay to JPMorgan any Obligations (defined to mean (i) any and all obligations of the City to reimburse JPMorgan for any drawings under the Letter of Credit and all obligations to repay JPMorgan for any liquidity advance made under the Reimbursement Agreement, (ii) the obligation of the City to pay to JPMorgan all fees and expenses under the Fee Letter and (c) the obligation of the City to pay to JPMorgan any other amounts set forth in the Related Documents (other than those described in clauses (i) and (ii) immediately above) when and as due hereunder; or

(d) default in the due observance or performance by the City of certain covenants set forth in the Reimbursement Agreement; or

(e) default in the due observance or performance by the City of any other covenant set forth in the Reimbursement Agreement and the continuance of such default for 30 days after the occurrence thereof; or

(f) any material provision of the Reimbursement Agreement or any of the other Related Documents shall cease to be valid and binding, or the City or a senior officer of the City shall contest any such provision, or the City or a senior officer of the City or any agent or trustee on behalf of the City shall deny that it has any or further liability under the Reimbursement Agreement or any of the other Related Documents; or

(g) the City shall (i) have entered involuntarily against it an order for relief under the United States Bankruptcy Code, as amended, (ii) not pay, or admit in writing its inability to pay, its debts generally as they become due, (iii) make an assignment for the benefit of creditors, (iv) apply for, seek, consent to, or acquiesce in, the appointment of a receiver, custodian, trustee, examiner, liquidator or similar official for it or any substantial part of its property, (v) institute any proceeding seeking to have entered against it an order for relief under the United States Bankruptcy Code, as amended, to adjudicate it insolvent, or seeking dissolution, winding up, liquidation, reorganization, arrangement, marshalling of assets, adjustment or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors or fail to file an answer or other pleading denying the material allegations of any such proceeding filed against it, (vi) take any action in furtherance of any matter described in parts (i) through (v) above, or (vii) fail to contest in good faith any appointment or proceeding described in paragraph (h) below; or

(h) a custodian, receiver, trustee, examiner, liquidator or similar official shall be appointed for the City or any substantial part of its property, or a proceeding described in paragraph (g)(v) above shall be instituted against the City and such appointment continues undischarged or any such proceeding continues undismissed or unstayed for a period of 60 or more days; or

(i) dissolution or termination of the existence of the City; or

(j) a default shall occur under any evidence of indebtedness issued, assumed, or guaranteed by the City or under any indenture, agreement or other instrument under which the same may be issued, and such default shall continue for a period of time sufficient to permit the acceleration of the maturity of any such indebtedness (whether or not such maturity is in fact accelerated) or any such Indebtedness shall not be paid when and as due (whether by lapse of time, acceleration or otherwise); or

(k) any judgment or judgments, writ or writs or warrant or warrants of attachment, or any similar process or processes in an aggregate amount in excess of \$5,000,000 shall be entered or filed against the City or against any of its property that is payable from “gross revenues” (as defined in the Purchase Agreement) and remain undismissed, unvacated, unbonded or unstayed for a period of 30 days; or

(l) there shall be appointed or designated with respect to the City an entity such as an organization, board, commission, authority, agency or body to monitor or declare a financial emergency or similar state of financial distress with respect to the City, or there shall be declared by the City or by any legislative or regulatory body with competent jurisdiction over the City, the existence of a state of financial emergency or similar state of financial distress in respect of the City; or

(m) the Trustee shall cease to have an effective security interest to the extent and priority created or purported to be created by the Trust Agreement; or

(n) certain tax events shall have occurred.

#### *Insurer Default.*

Each of the following constitutes an “Insurer Default” under the Reimbursement Agreement:

(a) any principal of or interest with respect to any 2008 Certificate (including 2008 Certificates purchased by JPMorgan) is not paid by the City when due and such principal or interest is not paid by the Insurer when, as and in the amounts required to be paid pursuant to the terms of the Policy; or

(b) the 2008 Insurer shall fail to make any payment related to principal and interest when due under any insurance policy (other than the Policy) or surety bond issued by it insuring or supporting the payment of municipal obligations rated by any rating agency, and such failure shall continue for a period of thirty (30) days (it being understood by JPMorgan that default for purposes of this clause (b) shall not mean a situation whereby the 2008 Insurer contests in good faith its liability under any such policy or policies in light of the claims made thereunder); or

(c) a proceeding is instituted in a court having jurisdiction in the premises seeking an order for relief, rehabilitation, reorganization, conservation, liquidation or dissolution in respect of the 2008 Insurer or for any substantial part of its property under any applicable bankruptcy, insolvency or other similar law now or hereafter in effect, or for the appointment of a receiver, liquidator, assignee, custodian, trustee or sequestrator (or other similar official) and such proceeding shall not have been dismissed within 60 days or such court enters an order granting the relief sought in such proceeding; or the New York Department of Insurance shall declare a moratorium on the payment of the 2008 Insurer's debts, or the 2008 Insurer shall commence a voluntary case under any applicable bankruptcy, insolvency or other similar law now or hereafter in effect, shall consent to the entry of an order for relief in an involuntary case under any such law or shall consent to the appointment of or taking possession by a receiver, liquidator, assignee, trustee, custodian or sequestrator (or other similar official) of the 2008 Insurer or for any substantial part of its property, or shall make a general assignment for the benefit of creditors, or shall fail generally to pay its debts (provided for purposes of this definition, "debts" shall not include any obligation of the 2008 Insurer under any insurance policy or surety bond) as they become due, or an order for rehabilitation, liquidation or dissolution of the 2008 Insurer shall be issued; or

(d) (i) any material provision of the Policy relating to the obligation of the 2008 Insurer to make payments of principal and interest thereunder at any time for any reason ceases to be valid and binding on the 2008 Insurer in accordance with the terms of the Policy or the New York Department of Insurance, or a court or other Governmental Authority of appropriate jurisdiction shall find or rule or shall enter an order, judgment or decree that the Policy is not valid and binding on the 2008 Insurer or (ii) the 2008 Insurer shall (A) claim in writing that the Policy is not valid and binding on the 2008 Insurer, (B) repudiate the 2008 Insurer's obligations under the Policy or (C) initiate legal proceedings seeking an adjudication that the Policy, or any material provision thereof regarding the payment of principal or interest on the 2008 Certificates is not valid and binding on the 2008 Insurer.

#### *Insurer Downgrade Event.*

An "Insurer Downgrade Event" shall occur if Moody's or S&P shall (a) assign a financial strength rating or claims paying ability rating to the 2008 Insurer that is less than "A1", in the case of Moody's and less than "A+" in the case of S&P or (b) withdraw or suspend the financial strength rating or claims paying ability rating of the 2008 Insurer for credit related reasons; provided, however, that for purposes of this definition, a withdrawal or a suspension of a rating by either rating agency at the direction of the 2008 Insurer as a result of a reduction or potential reduction of the financial strength or claims-paying ability rating of the Insurer will be deemed to have occurred for credit related reasons.

#### *Mandatory Tender Event.*

A "Mandatory Tender Event" shall occur if (a) either S&P or Moody's shall have (i) assigned a rating to the long-term unenhanced indebtedness (including certificates of participation) of the City secured by Gross Revenues (as defined in the Purchase Agreement) below "A", in the case of S&P, or "A3", in the case of Moody's, or (ii) withdrawn (for reasons other than defeasance or redemption) or suspended any such rating or (b) a change of law shall occur which could reasonably be expected to result in a material adverse effect on the ability of the City to pay any Obligation when due.

*Remedies of JPMorgan Upon Occurrence of Event of Default or Mandatory Event Prior to the Policy Cancellation Date.*

If an Event of Default or a Mandatory Tender Event shall have occurred and be continuing prior to the cancellation date of the Policy (the "Cancellation Date"), JPMorgan may exercise any one or more of the following rights and remedies in addition to any other remedies in the Reimbursement Agreement or by law provided:

(a) give written notice of the occurrence of such Event of Default or such Mandatory Tender Event to the Trustee and direct the Trustee to cause a mandatory tender of the 2008 Certificates pursuant to the Trust Agreement, thereby causing the Letter of Credit to terminate fifteen (15) days thereafter in accordance with its terms, in which case JPMorgan shall, in accordance with the provisions of the Trust Agreement, direct that the Policy be terminated and the Authority, the City, the Trustee and JPMorgan shall take such action as shall be necessary to effect such termination in accordance with the terms of the Cancellation Agreement; provided, however, that if an Insurer Default shall have occurred and be continuing, JPMorgan may give notice of an Event of Default or Mandatory Tender Event to the Trustee and direct the Trustee to cause a mandatory tender of the 2008 Certificates without directing the Authority, the City and the Trustee to take such action as shall be necessary to effect a termination of the Policy in accordance with the terms of the Cancellation Agreement;

(b) pursue any rights and remedies it may have under the Related Documents subject to the terms thereof, including, instituting suit, actions or proceedings to enforce its rights under the Trust Agreement; or

(c) pursue any other action available at law or in equity either for specific performance of any covenant or agreement contained in the Reimbursement Agreement or in aid of execution of any power granted in the Reimbursement Agreement or for the enforcement of any proper legal remedy;

provided, however, that in the case of the foregoing clauses (b) and (c), except in certain limited circumstances, JPMorgan shall not exercise any such rights and remedies or pursue such other actions, including directions or remedies under the Trust Agreement, without the consent of the 2008 Insurer.

*Remedies of JPMorgan Upon Insurer Default or Insurer Downgrade Event.*

(a) If an Insurer Default or an Insurer Downgrade Event shall have occurred, JPMorgan may give written notice to the Trustee of the occurrence of such Insurer Default or Insurer Downgrade Event, as applicable, and direct that the Insurance Policy be terminated within fifteen (15) days of such direction, whereupon, in accordance with the Trust Agreement, the 2008 Certificates shall be subject to mandatory tender. Upon any such direction, the Authority, the City, the Trustee and JPMorgan shall take such action as shall be necessary to effect such termination pursuant to the terms of the Cancellation Agreement.

(b) If (i) the City fails to pay JPMorgan any Letter of Credit facility fee or (ii) an Insurer Default or an Insurer Downgrade Event shall have occurred and be continuing, in each case, during the occurrence and continuation of an Event of Default, JPMorgan may give written notice to the Trustee of the occurrence thereof, and direct the Trustee to cause a mandatory tender of the 2008 Certificates in accordance with the Trust Agreement, thereby causing the Letter of Credit to terminate fifteen (15) days thereafter.

*Remedies of JPMorgan Upon Occurrence of Event of Default or Mandatory Event On or After the Policy Cancellation Date.*

If the Insurance Policy Cancellation Date has occurred, upon the occurrence and continuance of an Event of Default or a Mandatory Tender Event, JPMorgan may exercise any one or more of the following rights and remedies:

(a) by notice to the City, declare all Obligations to be, and such amounts shall thereupon become, immediately due and payable without presentment, demand, protest or other notice of any kind, all of which are hereby waived by the City, provided that upon the occurrence of an Event of Default under of the type described in paragraph (g) or (h) of the definition thereof such acceleration shall automatically occur (unless such automatic acceleration is waived by JPMorgan in writing);

(b) give notice of the occurrence of an Event of Default to the Trustee, directing the Trustee to cause a mandatory purchase the 2008 Certificates, thereby causing the Letter of Credit to expire fifteen (15) days thereafter;

(c) pursue any rights and remedies it may have under the Related Documents; or

(d) pursue any other action available at law or in equity.

#### **INFORMATION CONCERNING JPMORGAN**

*The information under this caption has been furnished by JPMorgan and no representation is made by the Authority or the City as to the accuracy or completeness or the adequacy of such information. Further, no representation is made by the Authority or the City or JPMorgan as to the absence of material adverse changes in such information subsequent to the date hereof, or that the information given below or incorporated herein by reference is correct as of any time subsequent to its date.*

#### **JPMorgan Chase Bank, National Association**

JPMorgan Chase Bank, National Association (“JPMorgan”) is a wholly owned bank subsidiary of JPMorgan Chase & Co., a Delaware corporation whose principal office is located in New York, New York. JPMorgan offers a wide range of banking services to its customers, both domestically and internationally. It is chartered and its business is subject to examination and regulation by the Office of the Comptroller of the Currency.

As of March 31, 2011, JPMorgan Chase Bank, National Association, had total assets of \$1,723.5 billion, total net loans of \$537.6 billion, total deposits of \$1,093.0 billion, and total stockholder’s equity of \$123.8 billion. These figures are extracted from JPMorgan’s unaudited Consolidated Reports of Condition and Income (the “Call Report”) as of March 31, 2011, prepared in accordance with regulatory instructions that do not in all cases follow U.S. generally accepted accounting principles, which are filed with the Federal Deposit Insurance Corporation. The Call Report, including any update to the above quarterly figures, can be found at [www.fdic.gov](http://www.fdic.gov).

Additional information, including the most recent annual report on Form 10-K for the year ended December 31, 2010, of JPMorgan Chase & Co., the 2010 Annual Report of JPMorgan Chase & Co., and additional annual, quarterly and current reports filed with or furnished to the Securities and Exchange Commission (the “SEC”) by JPMorgan Chase & Co., as they become available, may be obtained without charge by each person to whom this Supplement is delivered upon the written request of any such person

to the Office of the Secretary, JPMorgan Chase & Co., 270 Park Avenue, New York, New York 10017 or at the SEC's website at [www.sec.gov](http://www.sec.gov).

## **INFORMATION CONCERNING ASSURED GUARANTY CORP.**

*The following information has been provided by Assured Guaranty Corp. It has not been verified by the Authority or the City, and neither the Authority nor the City guarantees its accuracy or completeness.*

### **Financial Guaranty Insurance Policy**

The scheduled payment of, principal of, and interest on the 2008 Certificates when due will, to the extent that JPMorgan fails to honor a properly presented and conforming draw under the JPMorgan Letter of Credit, continue to be guaranteed under the financial guaranty insurance policy (the "Policy") previously issued by the 2008 Insurer for the 2008 Certificates.

The Policy is not covered by any insurance security or guaranty fund established under New York, California, Connecticut or Florida insurance law.

### **Assured Guaranty Corp.**

AGC is a Maryland-domiciled insurance company regulated by the Maryland Insurance Administration and licensed to conduct financial guaranty insurance business in all fifty states of the United States, the District of Columbia and Puerto Rico. AGC commenced operations in 1988. AGC is a wholly owned, indirect subsidiary of Assured Guaranty Ltd. ("AGL"), a Bermuda-based holding company whose shares are publicly traded and are listed on the New York Stock Exchange under the symbol "AGO." AGL, through its operating subsidiaries, provides credit enhancement products to the U.S. and global public finance, infrastructure and structured finance markets. Neither AGL nor any of its shareholders is obligated to pay any debts of AGC or any claims under any insurance policy issued by AGC.

AGC's financial strength is rated "AA+" (stable outlook) by Standard & Poor's Ratings Services, a Standard & Poor's Financial Services LLC business ("S&P") and "Aa3" (negative outlook) by Moody's Investors Service, Inc. ("Moody's"). Each rating of AGC should be evaluated independently. An explanation of the significance of the above ratings may be obtained from the applicable rating agency. The above ratings are not recommendations to buy, sell or hold any security, and such ratings are subject to revision or withdrawal at any time by the rating agencies, including withdrawal initiated at the request of AGC in its sole discretion. Any downward revision or withdrawal of any of the above ratings may have an adverse effect on the market price of any security guaranteed by AGC. AGC does not guarantee the market price of the securities it insures, nor does it guarantee that the ratings on such securities will not be revised or withdrawn.

### *Current Financial Strength Ratings*

On June 13, 2011, S&P issued a release stating that it had affirmed the "AA+" financial strength rating of AGC, with a stable outlook. Reference is made to the release, a copy of which is available at [www.standardandpoors.com](http://www.standardandpoors.com), for the complete text of S&P's comments.

On January 24, 2011, S&P published a Request for Comment: Bond Insurance Criteria (the "Bond Insurance RFC") in which it requested comments on its proposed changes to its bond insurance ratings criteria. In the Bond Insurance RFC, S&P notes that it could lower its financial strength ratings on

existing investment-grade bond insurers (including AGC) by one or more rating categories if the proposed bond insurance ratings criteria are adopted, unless those bond insurers (including AGC) raise additional capital or reduce risk. Reference is made to the Bond Insurance RFC, a copy of which is available at [www.standardandpoors.com](http://www.standardandpoors.com), for the complete text of S&P's comments.

In a press release dated December 18, 2009, Moody's announced that it had confirmed its "Aa3" insurance financial strength rating of AGC, with a negative outlook. Reference is made to the press release, a copy of which is available at [www.moody.com](http://www.moody.com), for the complete text of Moody's comments.

There can be no assurance as to any further ratings action that Moody's or S&P may take with respect to AGC.

For more information regarding AGC's financial strength ratings and the risks relating thereto, see AGL's Annual Report on Form 10-K for the fiscal year ended December 31, 2010, which was filed by AGL with the Securities and Exchange Commission ("SEC") on March 1, 2011, and AGL's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2011, which was filed by AGL with the SEC on May 10, 2011.

#### *Capitalization of Assured Guaranty Corp.*

As of March 31, 2011, AGC had total admitted assets of \$2,975,338,938 (unaudited), total liabilities of \$2,109,748,930 (unaudited), total surplus of \$865,590,009 (unaudited) and total statutory capital (surplus plus contingency reserves) of \$1,604,567,578 (unaudited), in each case, determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities.

#### *Incorporation of Certain Documents by Reference*

The portions of the following document filed by AGL with the SEC relating to AGC are hereby incorporated by reference into this Official Statement and shall be deemed to be a part hereof:

- (i) the Annual Report on Form 10-K for the fiscal year ended December 31, 2010 (which was filed by AGL with the SEC on March 1, 2011); and
- (ii) the Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2011 (which was filed by AGL with the SEC on May 10, 2011).

All consolidated financial statements of AGC and all other information relating to AGC included in documents filed by AGL with the SEC pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, after the filing of the last document referred to above and prior to the termination of the offering of the 2008 Certificates shall be deemed to be incorporated by reference into this Supplement and to be a part hereof from the respective dates of filing such documents.

Any statement contained in a document incorporated herein by reference or contained herein under the heading "INFORMATION CONCERNING ASSURED GUARANTY CORP. — Assured Guaranty Corp." shall be modified or superseded for purposes of this Supplement to the extent that a statement contained herein or in any subsequently filed document which is incorporated by reference herein also modifies or supersedes such statement. Any statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Supplement.

Copies of the consolidated financial statements of AGC incorporated by reference herein and of the statutory financial statements filed by AGC with the Maryland Insurance Administration are available upon request by contacting AGC at 31 West 52<sup>nd</sup> Street, New York, New York 10019 or by calling AGC at (212) 974-0100. In addition, the information regarding AGC that is incorporated by reference in this Supplement that has been filed by AGL with the SEC is available to the public over the Internet at the SEC's web site at <http://www.sec.gov> and at AGL's web site at <http://www.assuredguaranty.com>, from the SEC's Public Reference Room at 450 Fifth Street, N.W., Room 1024, Washington D.C. 20549, and at the office of the New York Stock Exchange at 20 Broad Street, New York, New York 10005.

AGC makes no representation regarding the 2008 Certificates or the advisability of investing in the 2008 Certificates. In addition, AGC has not independently verified, makes no representation regarding, and does not accept any responsibility for the accuracy or completeness of this Supplement or any information or disclosure contained herein, or omitted herefrom, other than with respect to the accuracy of the information regarding AGC supplied by AGC and presented under the heading "INFORMATION CONCERNING ASSURED GUARANTY CORP."

## **TENDER AND PURCHASE OF THE 2008 CERTIFICATES**

The 2008 Certificates are subject to optional and mandatory tender for purchase as described in the 2008 Official Statement.

### **Alternate Liquidity Facility**

While the 2008 Certificates are in the Weekly Mode, the Authority is required to provide a Liquidity Facility. On or prior to the expiration of the JPMorgan Letter of Credit, the Authority may provide for an Alternate Liquidity Facility upon such terms and conditions as described in the 2008 Official Statement. If any condition precedent to the substitution of an Alternate Liquidity Facility is not satisfied, the substitution shall not occur, but the affected 2008 Certificates shall remain subject to mandatory purchase on the proposed Substitution Date.

## **THE WATER UTILITY SYSTEM**

### **The Water Utility System**

The City is located in California's Central Valley, approximately 88 miles from the City and County of San Francisco and has a population of 201,165 according to the U.S. Census released in April 2011.

In general terms, the City's total water service area consists of one large contiguous area and several outlying, non-contiguous service areas. The contiguous water area includes all of the property currently within the corporate boundaries of the City (approximately 37.04 square miles) as well as the property located within its sphere of influence and properties located within the communities of Ceres, Empire and Salida. There are five outlying non-contiguous water service areas. They are the communities of Del Rio, Grayson, Hickman and Waterford, as well as portions of the City of Turlock.

See APPENDIX F – "ANNUAL REPORT FILING FOR FISCAL YEAR ENDED JUNE 30, 2010" for certain updated information on the City's Water Utility System.

## **Existing Facilities**

The principal facilities of the existing Water Utility System consist of 125 domestic wells (111 of which are currently active), over 900 miles of mains, seven storage tanks, a Water Treatment Plant owned by Modesto Irrigation District (“MID”) and financed by the City and a terminal storage area serving surface water and/or groundwater to its customers through nearly 77,000 water connections.

MID surface water is treated at the Water Treatment Plant and conveyed to the City via transmission mains for direct use in the contiguous portion of the City’s water service area. The City’s facilities are designed to deliver both surface water and groundwater. The Water Treatment Plant does not provide surface water to the outlying portions of the City’s water service areas including those portions that are outside of MID’s authorized service boundaries, which are served through groundwater wells.

Groundwater is pumped directly from the wells into the distribution system, which consists of 900 miles of water mains and pipelines. Most of the larger water mains are 10- and 12-inch diameter pipelines which have been installed by the City. The installation of smaller pipelines in subdivisions is typically the responsibility of the subdivider. Seven ground level tanks and booster pump stations provide storage capacities ranging from 500,000 to 1,300,000 gallons each.

## **Water Treatment Plant Expansion**

The expansion of the Modesto Irrigation District’s Modesto Regional Water Treatment Plant (MRWTP) has not been completed as of this date. The original plant is still on line and is fully operational and is capable of producing up to 42 mgd. The project expansion has experienced construction issues which have delayed its completion. MID has hired several firms to help them get the project back on track and is working through issues with the contractor. It is MID’s position that any additional costs for completing the project will be borne by the engineer and the contractor and will not be passed on to the City’s water customers. Also, based on the City’s agreement with MID, it is the City’s position that should there be additional costs beyond those borne by the engineer and contractor, those costs would be borne by MID and not the City’s water customers. At this point there is no official projected completion date but progress is being made in many areas. However, due to the complexity of the remaining issues it would be reasonable to assume that full completion of the project expansion is at least 18 months out. Until the expansion project is online, the City projects that it will be able to meet projected water demands with current treatment plant production and groundwater.

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## Historical Operating Results

The following table summarizes operating revenues, operating expenses and net income of the Water Utility System for the five fiscal years 2005-06 through 2009-10. The information for each of the fiscal years shown was prepared by the City on the basis of its audited financial statements. See APPENDIX C- "EXCERPTS FROM THE CITY'S FINANCIAL STATEMENTS FOR FISCAL YEAR ENDING 2010."

### WATER UTILITY SYSTEM Historical Debt Service Coverage<sup>(1)</sup>

	<i>Fiscal Year 2006</i>	<i>Fiscal Year 2007</i>	<i>Fiscal Year 2008</i>	<i>Fiscal Year 2009</i>	<i>Fiscal Year 2010</i>
Charges for services	\$42,500,107	\$49,258,673	\$52,927,134	\$52,990,138	\$51,572,801
Connection charges	1,873,465	2,289,994	1,943,456	1,113,082	647,579
Refunds, Damages & Recoveries	40,765	566,307	232,570	29,033	428,083
Interest and rental income	149,145	735,396	1,984,517	2,055,531	1,006,611
Draw from (Deposit to) rate stabilization fund	(153,200)	—	—	—	—
Service Credits <sup>(2)</sup>	403,717	314,930	604,082	501,671	2,170,367
Miscellaneous			13,190	32,586	25,782
<b>Total Gross Operating Revenues</b>	<b>\$44,813,999</b>	<b>\$53,165,300</b>	<b>\$57,704,949</b>	<b>\$56,722,041</b>	<b>\$55,851,223</b>
Total operating expenses <sup>(3)</sup>	\$20,596,957	\$23,983,380	\$23,664,217	\$28,359,392	\$30,219,002
Operating transfers <sup>(4)(5)</sup>	95,385	65,000	65,000	482,503	765,000
CIP expenses moved to operating <sup>(6)</sup>	496,547	2,023,261	2,156,833	3,054,407	1,127,185
<b>Total Operating Expenses<sup>(7)</sup></b>	<b>\$21,188,889</b>	<b>\$26,071,641</b>	<b>\$25,886,050</b>	<b>\$31,896,302</b>	<b>\$32,111,187</b>
<b>Net Operating Revenues</b>	<b>\$23,625,110</b>	<b>\$27,093,659</b>	<b>\$31,818,899</b>	<b>\$24,825,739</b>	<b>\$23,740,036</b>
Total Debt Service:					
1997 Refunding Certificate of Participation	\$1,790,658	\$1,794,120	\$1,791,930	\$1,792,258	\$1,794,688
2006 Revenue Certificates of Participation	—	1,082,432	1,982,256	—	—
2008 Revenue Certificates of Participation	—	—	—	2,262,117	2,145,966
MID Treatment & Delivery Agreement	6,690,994	6,687,444	6,681,894	6,672,406	7,455,918
CDWR Loan	264,653	264,719	264,719	263,079	264,719
<b>Total Debt Service</b>	<b>\$8,746,305</b>	<b>\$9,828,715</b>	<b>\$10,720,799</b>	<b>\$10,989,860</b>	<b>\$11,661,291</b>
<b>Debt Service Coverage</b>	<b>2.70</b>	<b>2.76</b>	<b>2.97</b>	<b>2.26</b>	<b>2.04</b>

<sup>(1)</sup> Calculated in conformity with the Contract and Trust Agreement.

<sup>(2)</sup> Service Credits are reimbursements from other City funds of costs associated with employee time worked on other projects. In Fiscal Year 2010 Cashiering, Utilities, and Collections division was moved into the Water Fund. This caused a structural change and in return an increase in service credits.

<sup>(3)</sup> Beginning in Fiscal Year 2009 total operating expenses increased as a result of the initiation of a meter program and increases in costs associated with supplies, maintenance, water treatment litigation and administration.

<sup>(4)</sup> Operating transfers in Fiscal Year 2009 increased due to an administrative oversight and funds were returned to the correct fund.

<sup>(5)</sup> Includes operating transfers for building rental fee of \$65,000 annually and commencing in Fiscal Year 2010 \$700,000 annual transfer to the Storm Drain Fund to actively protect the groundwater supply source from contamination.

<sup>(6)</sup> In Fiscal Year 2010, the City made a prior period adjustment to reclassify certain operating costs previously recorded as capital improvements. This prior period adjustment has been reflected in this table in the years costs were incurred.

<sup>(7)</sup> Total operating expenses excludes depreciation and amortization, as well as the debt service component under the Treatment and Delivery Agreement.

Source: City of Modesto

## Projected Operating Results

The City has prepared the following table of projections of operating results of the Water Utility System for the five fiscal years 2010-11 through 2015-16. The projected amounts set forth below are based on certain assumptions made by the City. To the extent that actual future conditions vary from those assumed in preparing the projections, the actual results will vary.

### WATER UTILITY SYSTEM Projected Operating Results <sup>(1)</sup>

	<i>Fiscal Year 2011<sup>(2)</sup></i>	<i>Fiscal Year 2012</i>	<i>Fiscal Year 2013</i>	<i>Fiscal Year 2014</i>	<i>Fiscal Year 2015</i>
Charges for services <sup>(3)</sup>	\$52,322,246	\$53,601,395	\$55,209,437	\$58,571,692	\$61,837,064
Connection charges	308,237	338,423	338,423	338,423	338,423
Refunds, Damages & Recoveries	—	—	—	—	—
Interest and rental income	259,498	207,319	224,385	178,346	213,524
Draw from (Deposit to) rate stabilization	—	—	—	—	—
Service Credits	2,106,146	2,645,803	3,252,788	3,300,643	3,349,454
Miscellaneous	52,200	31,301	31,927	32,566	33,217
<b>Total Gross Operating Revenues</b>	<b>\$55,048,327</b>	<b>\$56,824,241</b>	<b>\$59,056,960</b>	<b>\$62,421,670</b>	<b>\$65,771,682</b>
Total operating expenses <sup>(4)</sup>	\$27,868,284	\$33,117,784	\$36,442,354	\$38,215,362	\$39,851,885
Operating transfers <sup>(5)</sup>	765,000	1,783,610	765,000	765,000	765,000
CIP expenses moved to operating <sup>(6)</sup>	679,000				
<b>Total Operating Expenses <sup>(7)</sup></b>	<b>\$29,312,284</b>	<b>\$34,901,394</b>	<b>\$37,207,354</b>	<b>\$38,980,362</b>	<b>\$40,616,885</b>
<b>Net Operating Revenues</b>	<b>\$25,736,043</b>	<b>\$21,922,847</b>	<b>\$21,849,606</b>	<b>\$23,441,308</b>	<b>\$25,154,797</b>
Total Debt Service:					
1997 Refunding Certificate of Participation <sup>(8)</sup>	\$1,794,013	—	—	—	—
2008 Revenue Certificates of Participation	2,271,034	2,655,850	2,632,225	2,619,139	2,992,291
MID Treatment & Delivery Agreement <sup>(9)</sup>	10,794,051	10,794,041	10,789,791	10,778,307	10,778,701
CDWR Loan	264,719	264,719	264,719	264,719	264,719
0340 ARRA Funding CDPH				36,614	36,614
<b>Total Debt Service</b>	<b>\$15,123,817</b>	<b>\$13,714,610</b>	<b>\$13,686,735</b>	<b>\$13,698,779</b>	<b>\$14,072,325</b>
Debt Service Coverage	1.70	1.60	1.60	1.71	1.79

<sup>(1)</sup> Calculated in conformity with the Contract and Trust Agreement.

<sup>(2)</sup> Actuals through May 2011. Projected through June 30, 2011.

<sup>(3)</sup> Assumes projected increase in rates of 6% (not yet approved) on each January 1, 2013-15.

<sup>(4)</sup> Assumes an inflationary rate of 4%.

<sup>(5)</sup> Includes operating transfers for building rental fee of \$65,000 annually and \$700,000 annual transfer to the Storm Drain Fund to actively protect the groundwater supply source from contamination. Transfers also include a one time transfer to Parks for a \$350,000 loan in Fiscal Year 2012 for Agriculture Wells in Parks and a one time payment of \$668,000 in Fiscal Year 2012 to Information Technology for a new financial system.

<sup>(6)</sup> In Fiscal Year 2010, the City made a prior period adjustment to reclassify certain operating costs previously recorded as capital improvements in Fiscal Years 2005-2006 through 2010-2011.

<sup>(7)</sup> Excludes depreciation and amortization and the debt service component under the Treatment and Delivery Agreement.

<sup>(8)</sup> 1997 COPS were prepaid in full in Fiscal Year 2011.

<sup>(9)</sup> Debt service payment increased by \$4.1 million in Fiscal Year 2011 due to the expiration of capitalized interest.

Source: City of Modesto.

## THE REMARKETING AGREEMENT

The Authority has entered into a Remarketing Agreement, dated as of July 1, 2011 (the “Remarketing Agreement”) with J.P. Morgan Securities LLC as remarketing agent (the “Remarketing Agent”), pursuant to which J.P. Morgan Securities LLC serves as the Remarketing Agent for the 2008 Certificates. Pursuant to the Remarketing Agreement, the Remarketing Agent agrees to perform its duties and obligations under the Trust Agreement and use its best efforts to remarket the 2008 Certificates tendered or deemed tendered for purchase pursuant to the Trust Agreement and has no obligation to purchase any 2008 Certificates tendered for purchase. The obligation of the Remarketing Agent to remarket 2008 Certificates will be subject to the terms and conditions of the Remarketing Agreement.

The Remarketing Agent’s responsibilities include determining the interest rate from time to time and remarketing 2008 Certificates that are tendered by the owners thereof either pursuant to an optional or mandatory tender (subject, in each case, to the terms of the Remarketing Agreement), all as further described in this Supplement. The Remarketing Agent is appointed by the Authority and is paid by the Authority for its services. As a result, the interests of the Remarketing Agent may differ from those of existing owners and potential purchasers of 2008 Certificates.

***The Remarketing Agent Routinely Purchases 2008 Certificates for its Own Account.*** The Remarketing Agent acts as remarketing agent for a variety of variable rate demand obligations and, in its sole discretion, routinely purchases such obligations for its own account. The Remarketing Agent is permitted, but not obligated, to purchase tendered 2008 Certificates for its own account and, in its sole discretion, routinely acquires such tendered 2008 Certificates in order to achieve a successful remarketing of the 2008 Certificates (i.e., because there otherwise are not enough buyers to purchase the 2008 Certificates) or for other reasons. However, the Remarketing Agent is not obligated to purchase 2008 Certificates, and may cease doing so at any time without notice. The Remarketing Agent may also make a market in the 2008 Certificates by routinely purchasing and selling 2008 Certificates other than in connection with an optional or mandatory tender and remarketing. Such purchases and sales may be at or below par. However, the Remarketing Agent is not required to make a market in the 2008 Certificates. The Remarketing Agent may also sell any 2008 Certificates it has purchased to one or more affiliated investment vehicles for collective ownership or enter into derivative arrangements with affiliates or others in order to reduce its exposure to the 2008 Certificates. The purchase of 2008 Certificates by the Remarketing Agent may cause the interest rate to be lower than it would be if the Remarketing Agent did not purchase 2008 Certificates and may create the appearance that there is greater third party demand for the 2008 Certificates in the market than is actually the case. The practices described above also may result in fewer 2008 Certificates being tendered in a remarketing.

***2008 Certificates May be Offered at Different Prices on Any Date Including a Rate Determination Date.*** Pursuant to the Remarketing Agreement, the Remarketing Agent is required to determine the applicable rate of interest that, in its judgment, is the lowest rate that would permit the sale of the 2008 Certificates bearing interest at the applicable interest rate at par plus accrued interest, if any, on and as of the applicable Rate Determination Date. The interest rate will reflect, among other factors, the level of market demand for the 2008 Certificates (including whether the Remarketing Agent is willing to purchase 2008 Certificates for its own account). The purchase of the 2008 Certificates by the Remarketing Agent may cause the interest rate to be lower than it would be if the Remarketing Agent did not purchase 2008 Certificates. There may or may not be 2008 Certificates tendered and remarketed on a rate determination date, the Remarketing Agent may or may not be able to remarket any 2008 Certificates tendered for purchase on such date at par and the Remarketing Agent may sell 2008 Certificates at varying prices to different investors on such date or any other date. The Remarketing Agent is not obligated to advise purchasers in a remarketing if it does not have third party buyers for all of the 2008 Certificates at the remarketing price. The Remarketing Agent, in its sole discretion, may offer 2008

Certificates on any date, including the Rate Determination Date, at a discount to par to some investors, if the Remarketing Agent purchases such 2008 Certificates for its own account.

***The Ability to Sell the 2008 Certificates other than Through Tender Process May Be Limited.*** The Remarketing Agent may buy and sell 2008 Certificates other than through the tender process. However, it is not obligated to do so and may cease doing so at any time without notice and may require owners that wish to tender their 2008 Certificates to do so through the Tender Agent with appropriate notice. Thus, investors who purchase the 2008 Certificates, whether in a remarketing or otherwise, should not assume that they will be able to sell their 2008 Certificates other than by tendering the 2008 Certificates in accordance with the tender process.

***Under Certain Circumstances, the Remarketing Agent May Be Removed, Resign or Cease Remarketing the 2008 Certificates, Without a Successor Being Named.*** Under certain circumstances the Remarketing Agent may be removed or have the ability to resign or cease its remarketing efforts, without a successor having been named, subject to the terms of the Remarketing Agreement. In the event there is no Remarketing Agent, the Trustee shall *ipso facto* be deemed to be the Remarketing Agent for all purposes until the appointment by the Authority of the Remarketing Agent or successor Remarketing Agent.

See “TENDER AND PURCHASE OF THE 2008 CERTIFICATES” above for information regarding the sources of payment for the 2008 Certificates tendered or deemed tendered for purchase pursuant to the Trust Agreement.

## **RISK FACTORS**

*If for any reason JPMorgan fails to honor a drawing under the JPMorgan Letter of Credit, the City cannot provide any assurance that it will have sufficient funds on hand and available to make such payment of principal of and/or interest on the 2008 Certificates supported by the JPMorgan Letter of Credit or to make such payments in a timely manner. Prospective investors therefore should base their investment decision solely on the credit standing of JPMorgan, rather than on that of the City.*

*The purchase of the 2008 Certificates involves certain investment risks. Accordingly, each prospective purchaser of the 2008 Certificates should make an independent evaluation of all of the information presented in this Supplement in order to make an informed investment decision. Certain of these risks are described below.*

### **Factors Relating to the JPMorgan Letter of Credit**

The availability of money to pay the principal, purchase price and optional and mandatory sinking fund prepayment price of and interest represented by the 2008 Certificates depends solely on JPMorgan performing its obligations under the JPMorgan Letter of Credit. JPMorgan could be precluded from performing its obligations under the JPMorgan Letter of Credit in the event of bankruptcy, insolvency or reorganization, or a moratorium or similar event. There can be no assurance that JPMorgan will maintain its present financial condition or that an adverse change in such condition will not adversely affect its ability to honor future drawings under the JPMorgan Letter of Credit.

Additionally, the rating on the 2008 Certificates could be downgraded or withdrawn if JPMorgan were to be downgraded, placed on credit watch, have its rating suspended or withdrawn or were to refuse to perform under the JPMorgan Letter of Credit. The Amended Trust Agreement permits the Authority to substitute the JPMorgan Letter of Credit with an Alternate Liquidity Facility (with approval of the 2008 Certificate Insurer) should the Authority wish to do so in connection with a downgrade of the rating of

JPMorgan. No assurance can be given, however, that the Authority would be able to obtain an Alternate Credit Facility in such an event or, if obtained, what the ratings on 2008 Certificates would be.

Performance by JPMorgan of its obligations under the JPMorgan Letter of Credit is subject to the satisfaction of certain conditions by the Trustee, as set forth in the JPMorgan Letter of Credit. Holders of the 2008 Certificates are thus dependent upon the Trustee acting to satisfy such conditions before they will receive the benefit of the JPMorgan Letter of Credit. Furthermore, the question of whether the Trustee has properly satisfied such conditions is a question of fact which, if disputed, could delay or defeat the Trustee's rights of enforcement of the JPMorgan Letter of Credit.

## **TAX MATTERS**

In connection with the original execution and delivery of the 2008 Certificates, Sidley Austin LLP delivered its opinion that, based on existing statutes, regulations, rulings and judicial decisions and assuming compliance by the City with certain covenants in the Installment Purchase Contract and with requirements of the Internal Revenue Code of 1986, as amended (the "Code"), regarding the use, expenditure and investment of 2008 Certificate proceeds and the timely payment of certain investment earnings to the United States, interest represented by the 2008 Certificates would be excludable from the gross income of the owners of the 2008 Certificates for federal income tax purposes.

Sidley Austin LLP further opined that interest represented by the 2008 Certificates would not be treated as an item of tax preference in calculating the federal alternative minimum taxable income of individuals or corporations but interest represented by the 2008 Certificates would be included as an adjustment in the calculation of federal corporate alternative minimum taxable income and would therefore affect a corporation's federal alternative minimum tax liability.

The Original Official Statement states:

"Certain requirements and procedures contained or referred to in the Installment Purchase Contract and the Trust Agreement or other relevant documents relating to the Certificates may be changed, and certain actions may be taken (including, without limitation, defeasance of the Certificates), or omitted, under the circumstances and subject to the terms and conditions set forth in such documents, upon the advice or with the approving opinion of counsel nationally recognized in the area of municipal bonds. We express no opinion as to the effect of any change to any document pertaining to the Certificates or of any action taken or not taken where such change is made or action is taken or not taken without our approval or in reliance upon the advice of counsel other than ourselves with respect to the exclusion from gross income of the interest represented by the Certificates for federal income tax purposes."

The form of the opinion of Sidley Austin LLP delivered on May 30, 2008, is included herein as Appendix C to Appendix A hereto.

On the Substitution Date, Sidley Austin LLP, Special Counsel to the City, will deliver an opinion to the effect that the substitution of the JPMorgan Letter of Credit is permitted under the Trust Agreement, and will not, in and of itself, result in the inclusion of interest represented by the 2008 Certificates in gross income for federal income tax purposes. Sidley Austin LLP has not made any investigation as to any matters affecting the exclusion from gross income of interest represented by the 2008 Certificates since the date of issuance of the 2008 Certificates, and, accordingly, Sidley Austin LLP expresses no opinion as to the exclusion from gross income of interest represented by the 2008

Certificates for federal income tax purposes. A complete copy of the proposed form of the opinion of Sidley Austin LLP is included as Appendix B hereto.

## **RATINGS**

Moody's Investors Service, Inc. ("Moody's") has assigned ratings of "Aa1/VMIG 1" and Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc. ("S&P") is expected to assign ratings of "AAA/A-1+" to the 2008 Certificates, based on the understanding that the JPMorgan Letter of Credit supporting the timely payment of principal and purchase price of and interest represented by such 2008 Certificates will be issued by JPMorgan on July 14, 2011. Moody's and S&P have assigned underlying ratings of "Aa3" and "AA-", respectively, to the 2008 Certificates. Such ratings reflect only the views of such organizations and any desired explanation of the significance of such ratings should be obtained from the rating agency furnishing the same, at the following addresses: Moody's Investors Service, Inc., 7 World Trade Center, 250 Greenwich Street, New York, New York 10007-2796; and Standard & Poor's, 55 Water Street, New York, New York 10041. Generally, a rating agency bases its rating on the information and materials furnished to it and on investigations, studies and assumptions of its own. There is no assurance such ratings will continue for any given period of time or that such ratings will not be revised downward or withdrawn entirely by the rating agencies, if in the judgment of such rating agencies, circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price of the 2008 Certificates.

**MISCELLANEOUS**

This Supplement is not to be construed as a contract or agreement between the Authority or the City and the purchasers or holders of any of the 2008 Certificates. Any statements made in this Supplement involving matters of opinion, whether or not expressly so stated, are intended merely as an opinion and not as representations of fact. The information and expressions of opinion herein are subject to change without notice and neither the delivery of this Supplement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the Authority, the City, the Water Utility System or JPMorgan since the date hereof.

This Supplement has been duly approved, executed and delivered by the City and the Authority.

CITY OF MODESTO, CALIFORNIA

By: /s/ Gloriette G. Beck  
Finance Director/Treasurer

MODESTO PUBLIC FINANCING AUTHORITY

By: /s/ Gloriette G. Beck  
Auditor and Treasurer

**APPENDIX A**

**COPY OF OFFICIAL STATEMENT, DATED MAY 29, 2008**

*In the opinion of Sidley Austin LLP, San Francisco, California, Special Counsel, based on existing statutes, regulations, rulings and judicial decisions and assuming compliance with certain covenants in the documents pertaining to the 2008 Certificates and requirements of the Internal Revenue Code of 1986, as amended (the "Code"), as described herein, interest with respect to the Certificates is not includable in the gross income of the owners of the Certificates for federal income tax purposes. In the further opinion of Special Counsel, interest with respect to the 2008 Certificates is not treated as an item of tax preference in calculating the federal alternative minimum taxable income of individuals and corporations. Interest with respect to the Certificates, however, is included as an adjustment in the calculation of federal corporate alternative minimum taxable income and may therefore affect a corporation's alternative minimum tax liability. In the further opinion of Special Counsel, interest with respect to the 2008 Certificates is exempt from personal income taxes imposed by the State of California. See "TAX MATTERS" herein.*

**\$47,625,000**  
**CITY OF MODESTO, CALIFORNIA**  
**WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION**  
**2008 SERIES A**

**Dated: Date of delivery****Price: 100%****CUSIP† 607804AB7****Due: October 1, 2036**

The 2008 Certificates are being executed and delivered pursuant to the 2008 Trust Agreement, dated as of May 1, 2008, by and between the Modesto Public Financing Authority and The Bank of New York Trust Company, N.A., as trustee, for the principal purpose of refinancing certain improvements to the Water Utility System of the City of Modesto. The 2008 Certificates are payable solely from installment payments to be made by the City to the Authority pursuant to the Master Installment Purchase Contract, dated as of November 1, 1997, as supplemented by the 2008 Supplemental Installment Purchase Contract, dated as of May 1, 2008, by and between the City and the Authority. The obligation of the City to make such installment payments is a special obligation of the City payable solely from Gross Revenues of its Water Utility System and certain funds and accounts created under the 2008 Trust Agreement. As described herein, those Gross Revenues are also pledged to the payment of certain other Parity Obligations of the City.

The 2008 Certificates will be initially executed and delivered in the Weekly Mode, and interest with respect to the 2008 Certificates in the Weekly Mode will be evidenced at the Weekly Rate. In general, the Weekly Rate is the rate of interest per annum determined by Banc of America Securities LLC, as Remarketing Agent, on and as of the applicable Rate Determination Date to be the minimum rate of interest which would result in the sale of the 2008 Certificates at a price equal to 100% of the principal amount thereof. Such interest is payable on the first Business Day of each month. The 2008 Certificates are subject to conversion to a different interest rate mode pursuant to the 2008 Trust Agreement. *This Official Statement describes the 2008 Certificates only while they are in the Weekly Mode.*

While the 2008 Certificates are in the Weekly Mode, they are subject to optional and mandatory tender for purchase under the circumstances described herein. Funds for the payment of the purchase price of the 2008 Certificates that are so subject to optional tender or mandatory tender for purchase and that are not remarketed by the Remarketing Agent will be available (subject to certain conditions precedent and automatic termination events) under a Standby Certificate Purchase Agreement, dated as of May 1, 2008, between the Authority and Bank of America, N.A., as the Liquidity Facility Provider.



The Standby Certificate Purchase Agreement does not support, secure or guaranty the payments of the principal of, premium, if any, or interest with respect to the 2008 Certificates.

The 2008 Certificates are being executed and delivered in book-entry form only and when executed and delivered will be registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York. Beneficial interests in the 2008 Certificates while the 2008 Certificates are in the Weekly Mode will be available for purchase in denominations of \$100,000 and any integral multiple of \$5,000 in excess thereof. Purchasers of such beneficial interests will not receive certificates representing their beneficial ownership in the 2008 Certificates but will receive credit balances on the books of their respective nominees. The principal of and interest evidenced by the 2008 Certificates are payable by the Trustee to Cede & Co.; and such interest and principal payments are to be disbursed to the beneficial owners of the 2008 Certificates through their nominees.

**The 2008 Certificates are subject to optional prepayment and mandatory sinking fund prepayment prior to maturity as well as optional and mandatory tender for purchase as described herein.**

The scheduled payment of principal of and interest with respect to the 2008 Certificates when due will be guaranteed under a financial guaranty insurance policy to be issued concurrently with the delivery of the 2008 Certificates by Assured Guaranty Corp.



**THE OBLIGATION OF THE CITY TO PAY INSTALLMENTS OF PRINCIPAL AND INTEREST IS A SPECIAL OBLIGATION OF THE CITY PAYABLE SOLELY FROM THE GROSS REVENUES OF ITS WATER UTILITY SYSTEM LESS MAINTENANCE AND OPERATIONS COSTS THEREOF (AS DEFINED IN THE MASTER INSTALLMENT PURCHASE CONTRACT), ALL AS FURTHER DESCRIBED HEREIN. SAID OBLIGATION DOES NOT CONSTITUTE A DEBT OF THE CITY OR THE STATE OF CALIFORNIA, OR ANY POLITICAL SUBDIVISION THEREOF, WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTION. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE CITY OR THE STATE, OR ANY POLITICAL SUBDIVISION THEREOF, IS PLEDGED TO THE PAYMENT OF THE INSTALLMENT PAYMENTS OR THE INTEREST THEREON.**

*THIS COVER PAGE CONTAINS CERTAIN INFORMATION FOR GENERAL REFERENCE ONLY. IT IS NOT A SUMMARY OF THIS ISSUE. INVESTORS ARE ADVISED TO READ THE ENTIRE OFFICIAL STATEMENT TO OBTAIN INFORMATION ESSENTIAL TO THE MAKING OF AN INFORMED INVESTMENT DECISION.*

*The 2008 Certificates are offered when, as and if delivered and received by the Underwriter, subject to the approval of legality by Sidley Austin LLP, San Francisco, California, Special Counsel, and certain other conditions. Certain legal matters will be passed upon for the City and the Authority by the City Attorney of the City and by Stradling Yocca Carlson & Rauth, a Professional Corporation, Newport Beach, California, Disclosure Counsel; for the Trustee by the Jensen Law Office, Orinda, California; for the Liquidity Facility Provider by Kathleen C. Johnson, Esq., Santa Barbara, California and for the 2008 Certificate Insurer by its General Counsel. It is anticipated that the 2008 Certificates will be available for delivery to The Depository Trust Company or its agent on or about May 30, 2008.*

## Banc of America Securities LLC

Dated: May 29, 2008

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**CITY OF MODESTO, CALIFORNIA**

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**CITY COUNCIL**

Jim Ridenour, Mayor

Garrad Marsh, Vice Mayor

Dave Lopez

Janice Keating

Will O'Bryant

Kristin Olsen

Brad Hawn

**CITY OFFICIALS**

James E. Niskanen, Interim City Manager

Susana Alcala Wood, City Attorney

Wayne Padilla, Finance Director/Treasurer

Nick Pinhey, Director of Public Works

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**SPECIAL SERVICES**

**Special Counsel**

Sidley Austin LLP

San Francisco, California

**Trustee**

The Bank of New York Trust Company, N.A.

San Francisco, California

**Financial Advisor**

Public Financial Management, Inc.

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**Disclosure Counsel**

Stradling Yocca Carlson & Rauth, a Professional Corporation

Newport Beach, California

All the information which the City of Modesto intends to present investors regarding the City, the Authority, and the 2008 Certificates is contained in this Official Statement. While the City maintains an internet website for various purposes, none of the information on that website is intended to assist investors in making any investment decision, or to provide any continuing information, with respect to the 2008 Certificates or any other obligations of the City. Moreover, none of the information on the website is incorporated herein by reference. No dealer, broker, salesperson or other person has been authorized by the City, the Authority, the 2008 Certificate Insurer or the Underwriter to give any information or to make any representations other than those contained in this Official Statement in connection with the offering made hereby and, if given or made, such other information or representations must not be relied upon as having been authorized by the City, the Authority, the 2008 Certificate Insurer or the Underwriter. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of the 2008 Certificates by a person in any jurisdiction in which it is unlawful for such person to make such an offer, solicitation or sale.

This Official Statement is not to be construed as a contract with the purchasers of the 2008 Certificates. Statements contained in this Official Statement which involve estimates, forecasts or matters of opinion, whether or not expressly so described herein, are intended solely as such and are not to be construed as a representation of facts.

The information set forth herein has been obtained from sources which are believed to be reliable, but it is not guaranteed as to accuracy or completeness. The information and expression of opinions herein are subject to change without notice and neither delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the City or the 2008 Certificate Insurer since the date hereof. All summaries of documents contained herein are made subject to the provisions of such documents and do not purport to be complete statements of any or all such provisions.

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The Underwriter has provided the following sentence for inclusion in this Official Statement:

*The Underwriter has reviewed the information in this Official Statement in accordance with, and as part of, its responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriter does not guarantee the accuracy or completeness of such information.*

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The 2008 Certificate Insurer has provided the following sentence for inclusion in this Official Statement:

Assured Guaranty makes no representation regarding the 2008 Certificates or the advisability of investing in the 2008 Certificates. In addition, Assured Guaranty makes no representation regarding, nor does it accept any responsibility for, the accuracy or completeness of this Official Statement or any information or disclosure contained herein, or omitted herefrom, other than with respect to the accuracy of the information regarding Assured Guaranty supplied by Assured Guaranty and presented under the heading "CERTIFICATE INSURANCE" and Appendix E — "SPECIMEN FINANCIAL GUARANTY INSURANCE POLICY."

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**CAUTIONARY INFORMATION REGARDING FORWARD-LOOKING STATEMENTS IN  
THIS OFFICIAL STATEMENT**

Certain statements included or incorporated by reference in this Official Statement constitute "Forward-Looking Statements" within the meaning of the United States Private Securities Litigation Reform Act of 1995, Section 21E of the United States Securities Exchange Act of 1934, as amended, and Section 27A of the United States Securities Act of 1933, as amended. Such statements are generally identifiable by the terminology used, such as "plan," "expect," "estimate," "budget" and other similar words and include, but are not limited to, statements that describe possible future connections to and revenues and expenses of the Water Utility System.

The achievement of certain results or other expectations contained in such forward-looking statements involves known and unknown risks, uncertainties and other factors which may cause actual results, performance or achievements described to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements.

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THE 2008 CERTIFICATES HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, IN RELIANCE UPON AN EXEMPTION CONTAINED IN SUCH ACT. THE 2008 CERTIFICATES HAVE NOT BEEN REGISTERED OR QUALIFIED UNDER THE SECURITIES LAWS OF ANY STATE.

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**\$47,625,000**  
**CITY OF MODESTO, CALIFORNIA**  
**WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION**  
**2008 SERIES A**

**INTRODUCTION**

**General**

This Official Statement, including the cover page and all appendices attached hereto, provides certain information concerning the City of Modesto Refunding Water Revenue Certificates of Participation, 2008 Series A (the “2008 Certificates”), evidencing and representing the proportionate interests of the Owners thereof in certain payments to be made by the City of Modesto, California (the “City”). Descriptions and summaries of various documents hereinafter set forth do not purport to be comprehensive or definitive, and reference is made to each document for complete details of all terms and conditions thereof. Capitalized terms used and not otherwise defined herein shall have the meanings ascribed to them in APPENDIX B — “DEFINITIONS AND SUMMARY OF PRINCIPAL LEGAL DOCUMENTS.”

The 2008 Certificates are being executed and delivered primarily to refinance certain improvements (collectively, the “2008 Project”) to the City’s water utility system (the “Water Utility System”) as further described under the caption “THE 2008 PROJECT” below. Proceeds derived from the sale of the 2008 Certificates, along with other funds available for such purposes, will also be used to pay the costs of executing and delivering the 2008 Certificates and to make a cash deposit into, and to pay the premium for a reserve fund financial guaranty insurance policy (the “Parity Reserve Fund Insurance Policy”) that will be credited to, the debt service reserve fund for the Parity Obligations (as hereinafter defined) (the “Parity Reserve Fund”). See “REFINANCING PLAN” and “ESTIMATED SOURCES AND USES OF FUNDS.”

**The 2008 Certificates**

The 2008 Certificates represent the proportionate undivided interests of the registered owners thereof (the “Owners”) in installment payments (the “2008 Payments”) payable by the City under the Master Installment Purchase Contract, dated as of November 1, 1997 (the “Master Contract”), by and between the City and the Modesto Public Financing Authority, a California joint exercise of powers agency (the “Authority”), as supplemented by supplemental purchase contracts including the 2008 Supplemental Installment Purchase Contract, dated as of May 1, 2008 by and between the City and the Authority (the “2008 Contract” and, collectively with the Master Contract, the “Contract”). The 2008 Certificates are being executed and delivered pursuant to the Trust Agreement, dated as of May 1, 2008 (the “2008 Trust Agreement”), by and between the Authority and The Bank of New York Trust Company, N.A., as trustee (the “Trustee”). Pursuant to the 2008 Trust Agreement, the Authority has assigned to the Trustee for the benefit of the Owners of the 2008 Certificates all its rights under the Contract, including its right to receive 2008 Payments payable under the Contract and its right to enforce payment by the City of the 2008 Payments when due.

The 2008 Certificates will be dated the date on which they are executed and delivered and will mature on October 1, 2036 (the “Maturity Date”), subject to prepayment prior thereto. See “THE 2008 CERTIFICATES — Prepayment.” The 2008 Certificates will be initially executed and

delivered in the Weekly Mode, and interest with respect to the 2008 Certificates in the Weekly Mode will be evidenced at the Weekly Rate. In general, the Weekly Rate is the rate of interest per annum determined by Banc of America Securities LLC, as Remarketing Agent (the “Remarketing Agent”), on and as of the applicable Rate Determination Date to be the minimum rate of interest which would result in the sale of the 2008 Certificates at a price equal to 100% of the principal amount thereof. Such interest is payable on the first Business Day of each month. See “THE 2008 CERTIFICATES.” The 2008 Certificates are subject to conversion to a different interest rate mode pursuant to the 2008 Trust Agreement. *This Official Statement describes the 2008 Certificates only while they are in the Weekly Mode.*

While the 2008 Certificates are in the Weekly Mode, they are subject to optional and mandatory tender for purchase under the circumstances described herein. Funds for the payment of the purchase price of the 2008 Certificates that are so subject to optional tender or mandatory tender for purchase and that are not remarketed by the Remarketing Agent will be available (subject to certain conditions precedent and automatic termination events) under a Standby Certificate Purchase Agreement, dated as of May 1, 2008 (the “Liquidity Facility”), between the Authority and Bank of America, N.A., as Liquidity Facility Provider (the “Liquidity Facility Provider”). The Liquidity Facility does not support, secure or guaranty the payments of the principal of, premium, if any, or interest with respect to the 2008 Certificates. For a description of the Standby Certificate Purchase Agreement and information concerning Bank of America, N.A., see “LIQUIDITY FACILITY.”

### **Security for the 2008 Certificates**

**General.** The 2008 Certificates represent the proportionate interests of the Owners in the 2008 Payments. The City is required to make the 2008 Payments pursuant to the provisions of the Contract. The 2008 Payments represent the purchase price of the 2008 Project, which the Authority is selling to the City.

**The Master Contract.** The Master Contract establishes the terms and conditions upon which certain obligations of the City will be incurred and secured. Pursuant to the Master Contract, all Gross Revenues (as defined in the Master Contract) of the Water Utility System are pledged to the payment of the 2008 Payments, all payments required to be made under all other Parity Obligations and Maintenance and Operations Costs; and amounts on deposit in the Parity Reserve Fund are pledged to the payment of the 1997 Payments (defined below), the 2008 Payments and any other obligations hereafter issued in connection with a Supplemental Contract. The City has previously incurred, and may in the future incur, obligations payable from Gross Revenues on a parity with the 2008 Payments (“Parity Obligations”) pursuant to the terms and conditions of the Master Contract. See “SECURITY FOR THE 2008 CERTIFICATES — Existing and Future Parity Obligations.” To provide additional security for the 2008 Certificates and Parity Obligations, the Master Contract contains a rate covenant which requires the City to fix, prescribe, and collect certain minimum rates, fees and charges for the water service, calculated in accordance with the Master Contract. See “SECURITY FOR THE 2008 CERTIFICATES — Rate Covenant.”

**The 1997 Contract.** The City has previously financed and refinanced certain improvements to its Water Utility System pursuant to a 1997 Supplemental Installment Purchase Contract, dated as of November 1, 1997, by and between the City and the Authority (the “1997 Contract”), under which the City is obligated to make certain payments (the “1997 Payments”) to the Authority as payment of the purchase price for those improvements. The 1997 Payments are payable from Gross Revenues on a parity with the 2008 Payments.

***The 2006 Contract.*** Subsequent to its execution of the 1997 Contract, in order to finance the cost of additional improvements to the Water Utility System (the “2006 Project”), the City entered into the 2006 Supplemental Installment Purchase Contract with the Authority (the “2006 Contract”), supplementing the Master Contract. Pursuant to the 2006 Contract, the City obligated itself to make certain payments (the “2006 Payments”) to the Authority; and pursuant to a related trust agreement the Authority assigned to The Bank of New York Trust Company, N.A., as trustee (the “2006 Trustee”), its right to receive the 2006 payments. The Authority and the 2006 Trustee executed and delivered certificates of participation in the 2006 Payments (the “2006 Certificates”), and proceeds from the sale of the 2006 Certificates are being used to pay the costs of constructing the 2006 Project. In connection with the 2008 Contract, the City will reconvey the 2006 Project to the Authority for sale back to the City as the 2008 Project; and proceeds from the sale of the 2008 Certificates, along with other funds available for such purpose, will be applied to prepay the 2006 Payments. As a result of the foregoing, the City’s obligations with respect to the 2006 Contract will be extinguished, and the 2006 Certificates will be defeased, concurrently with the execution and delivery of the 2008 Certificates, provided, however, that certain amendments to the Master Contract contained in the 2006 Contract will remain in full force and effect.

***The 2008 Contract.*** The 2008 Contract is a Parity Obligation executed and delivered under the provisions of the Master Contract. In consideration of the Authority’s agreement to finance the 2008 Project pursuant to the provisions of the 2008 Contract, the City agrees to pay the 2008 Payments to the Authority, solely from Gross Revenues on parity with all other Parity Obligations and Maintenance and Operation Costs, as provided in the 2008 Contract. The obligation of the City to make the 2008 Payments from Gross Revenues is absolute and unconditional; and, until such time as the 2008 Payments have been paid in full (or provision for the payment thereof shall have been made pursuant to the Master Contract), the City will not discontinue or suspend any such payments required to be made by it under the 2008 Contract when due whether or not the Water Utility System or any part thereof is operating or operable, or its use is suspended, interfered with, reduced, curtailed or terminated in whole or in part. See “SECURITY FOR THE 2008 CERTIFICATES — 2008 Payments.”

THE OBLIGATION OF THE CITY TO PAY THE 2008 PAYMENTS IS A SPECIAL OBLIGATION OF THE CITY PAYABLE SOLELY FROM GROSS REVENUES OF THE WATER UTILITY SYSTEM AND DOES NOT CONSTITUTE A DEBT OF THE CITY OR OF THE STATE OF CALIFORNIA OR ANY POLITICAL SUBDIVISION THEREOF IN CONTRAVENTION OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTION. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE CITY OR THE STATE OF CALIFORNIA, OR ANY POLITICAL SUBDIVISION, THEREOF IS PLEDGED TO THE PAYMENT OF THE 2008 PAYMENTS.

#### **Certificate Insurance / Reserve Fund Insurance Policy**

Assured Guaranty Corp. (“Assured Guaranty” or the “2008 Certificate Insurer”) has issued a commitment to issue, simultaneously with the delivery of the 2008 Certificates, a municipal bond insurance policy (the “2008 Certificate Insurance Policy”) relating to the 2008 Certificates, effective as of the date of delivery of the 2008 Certificates. By the terms of the 2008 Certificate Insurance Policy, Assured Guaranty agrees to pay the principal and interest represented by the 2008 Certificates which come due for payment but which are unpaid, to the extent that the Trustee has not received sufficient funds from the City with which to make such payment. See “CERTIFICATE

INSURANCE” and APPENDIX E — “SPECIMEN FINANCIAL GUARANTY INSURANCE POLICY.”

Assured Guaranty will also issue the Parity Reserve Fund Insurance Policy (see “CERTIFICATE INSURANCE — The Reserve Fund Insurance Policy”); and, in connection therewith, the City and the Trustee will enter into an agreement with Assured Guaranty, dated as of May 1, 2008 (the “Reimbursement Agreement”). The City’s obligations under the Reimbursement Agreement will be Parity Obligations.

### **Liquidity Facility**

While the 2008 Certificates are in the Weekly Mode, they are subject to optional tender and mandatory tender for purchase. Funds for the payment of the purchase price of 2008 Certificates that are so tendered for purchase and that are not remarketed by the Remarketing Agent will be available (subject to certain conditions precedent and automatic termination events) under the Liquidity Facility. The Liquidity Facility does not support, secure or guaranty the payments of the principal of, premium, if any, or interest with respect to the 2008 Certificates. See “LIQUIDITY FACILITY.”

### **Swap Agreement**

In connection with the execution and delivery of the 2006 Certificates, the City entered into an interest rate swap agreement in the form of an ISDA Master Agreement (Local Currency – Single Jurisdiction), the U.S. Municipal Counterparty Schedule thereto, a Credit Support Annex and a Confirmation each dated as of and entered into on September 27, 2006 (collectively, the “2006 Swap Agreement”) with Bank of America, N.A. (the “Swap Provider”). In connection with the execution and delivery of the 2008 Certificates, the City and the Swap Provider will amend the 2006 Swap Agreement in various respects, including increasing the notional amount thereof, revising schedule pursuant to which the notional amount is to be reduced and providing for certain payments thereunder to be insured by Assured Guaranty (as so amended, the “2008 Swap Agreement”). The 2008 Swap Agreement is scheduled to expire on the Maturity Date of the 2008 Certificates; and the notional amount of the 2008 Swap Agreement is scheduled to be reduced on the same dates and in the same amounts as the principal evidenced by the 2008 Certificates is scheduled to be reduced. Pursuant to the 2008 Swap Agreement, the City will be required to make periodic payments to the Swap Provider calculated on the basis of a fixed rate of interest on an initial notional amount equal to the principal amount represented by the 2008 Certificates. In return, the Swap Provider will be required to make periodic payments to the City calculated on the basis of a variable rate of interest equal to a percentage of LIBOR on the same notional amount. The amounts payable by each party pursuant to the 2008 Swap Agreement are netted against the payments to be received by such party thereunder. See “SECURITY FOR THE 2008 CERTIFICATES — 2008 Swap Agreement.”

Bank of America, N.A. (the Swap Provider and the Liquidity Facility Provider) and Banc of America Securities LLC, (the Underwriter and Remarketing Agent), are affiliates, both being subsidiaries of Bank of America Corporation.

### **The City**

The City was incorporated in 1884, is the county seat of Stanislaus County, had an estimated population of over 209,000 as of January 1, 2008, and covers approximately 36 square miles. The City operates under a council-manager form of government pursuant to a charter adopted in 1963. It

is located in Central California, approximately 93 miles east of San Francisco. See APPENDIX F — “CERTAIN INFORMATION ABOUT THE CITY.”

### **The Water Utility System**

The Water Utility System provides potable water service to residential, commercial and industrial consumers located within the incorporated area of the City and in neighboring areas of Stanislaus County. The City owns, operates and maintains the Water Utility System, which is the sole retail provider of water service in the City. See “THE WATER UTILITY SYSTEM.”

### **Tax Matters**

For description of the tax status of interest with respect to the 2008 Certificates, see “TAX MATTERS” herein and see the complete copy of the proposed form of opinion of Special Counsel set forth in APPENDIX C — “PROPOSED FORM OF OPINION OF SPECIAL COUNSEL.”

### **No Continuing Disclosure**

While in the Weekly Mode, the 2008 Certificates are exempt from the continuing disclosure requirements of Rule 15c2-12 under the Securities Exchange Act of 1934, as amended.

### **Disclosure of Identity of Purchasers**

Any person who purchases a beneficial interest in the 2008 Certificates in connection with the initial offering thereof agrees that the underwriters of the 2008 Certificates may disclose such person’s identity to the City and Authority unless such person advises his or her sales representative otherwise.

### **Changes to Preliminary Official Statement**

In addition to the usual changes associated with finalizing a preliminary official statement, this final Official Statement includes a new section titled “CERTIFICATE INSURANCE — The Reserve Fund Insurance Policy,” revisions to the discussion of events of default and remedies under the Liquidity Facility (see “LIQUIDITY FACILITY — Initial Liquidity Facility”) and revisions to the table showing the projected operating results of the Water Utility System to reflect debt service with respect to the 2008 Certificates (see “THE WATER UTILITY SYSTEM — Summary of Projected Operating Results of the Water Utility System”).

## **REFINANCING PLAN**

Proceeds from the sale of the 2008 Certificates, along with other funds available for such purpose, in an aggregate amount equal to the outstanding principal amount of the 2006 Certificates and the interest payable with respect thereto on May 30, 2008, will be deposited with the 2006 Trustee concurrently with the execution of the 2008 Certificates. The 2006 Trustee has previously given a conditional notice of full prepayment of the 2006 Certificates to the registered owners thereof. Said notice states that the 2006 Certificates will be prepaid in full on May 30, 2008, subject to receipt by the 2006 Trustee of funds sufficient to pay the prepayment price of the 2006 Certificates on said date. Thus, upon execution and delivery of the 2008 Certificates and the deposit of proceeds from the sale thereof in the amount described above with the 2006 Trustee, the 2006 Certificates will no longer be outstanding.

## THE 2008 PROJECT

The 2008 Project consists of the City's conveyance to the Authority of the improvements that comprise the 2006 Project and the Authority's reconveyance thereof to the City in order to effect the refinancing of the 2006 Project. The 2006 Project consists of improvements required to be made by the City in connection with the Modesto Irrigation District's expansion of the Modesto Regional Water Treatment Plant (the "Water Treatment Plant"), including the construction of several new downstream water facilities and various water distribution system improvements to insure the reliability of water supply to both existing and future customers. The 2006 Project includes the acquisition of land and rights of way as well as design and construction costs related to the new facilities and improvements. The facilities include the acquisition, construction and installation of three storage tanks and connecting transmission facilities, construction and improvement of transmission/distribution mains and associated pump stations, and installation of motor-operated control valves controlling the flow of treated surface water from the Water Treatment Plant to the City system. The 2006 Project facilities and improvements are intended to help replace less reliable groundwater production capacity, improve the City's ability to maintain desired system operational pressures during high-demand periods and meet other operational criteria. These facilities are also intended to improve system distribution capabilities to future customers.

The Water Treatment Plant was constructed and is owned and operated by the Modesto Irrigation District ("MID"). Pursuant to an agreement with the City (the "Treatment and Delivery Agreement"), MID has agreed to an expansion of the Water Treatment Plant, doubling its rated capacity from approximately 30 million gallons per day to approximately 60 million gallons per day. (The Water Treatment Plant has been designed to accommodate a possible further expansion subject to a future agreement between the City and MID.) On June 26, 2007, the Modesto Irrigation District Financing Authority issued bonds in a principal amount of \$93,190,000 (the "MIDFA 2007 Bonds") in order to provide financing for the Water Treatment Plant expansion described above. The ultimate source of funds expected to be used to pay debt service on the MIDFA 2007 Bonds consists of payments to be made by the City to MID pursuant to the Treatment and Delivery Agreement. See "THE WATER UTILITY SYSTEM — Treatment and Delivery Agreement."

The 2006 Project is expected to be completed in the third quarter of 2009, the expansion of the Water Treatment Plant is expected to be completed in the fourth quarter of 2009 and the expanded plant is expected to be fully operational early in 2010.

## ESTIMATED SOURCES AND USES OF FUNDS

The table below sets forth the estimated sources and uses of the proceeds of the 2008 Certificates and certain other funds:

Sources:	
Principal Amount of the 2008 Certificates	\$47,625,000.00
Funds Held for 2006 Certificates	1,957,071.79
Less: Underwriter's Discount	( <u>153,920.63</u> )
Total	<u>\$49,428,151.16</u>
Uses:	
Transfer to 2006 Trustee <sup>(1)</sup>	\$46,286,841.26
Parity Reserve Fund <sup>(2)</sup>	1,834,552.07
Costs of Issuance <sup>(3)</sup>	1,196,042.80
Capitalized Interest	<u>110,715.03</u>
Total	<u>\$49,428,151.16</u>

<sup>(1)</sup> Equal to the principal amount of the 2006 Certificates and the interest payable with respect thereto on May 30, 2008, the date designated for the prepayment of the 2006 Certificates.

<sup>(2)</sup> The Reserve Fund Requirement, which is described herein under the caption "SECURITY FOR THE 2008 CERTIFICATES — Parity Reserve Fund," will be satisfied in connection with the execution and delivery of the 2008 Certificates by (a) the retention in the Parity Reserve Fund of cash currently held therein in connection with the 2006 Certificates in the amount of \$1,834,515.50, (b) a cash deposit of \$36.57 and (c) the delivery to the Trustee of the Parity Reserve Fund Insurance Policy, with a policy limit of \$2,082,512.74. See "CERTIFICATE INSURANCE — The Reserve Fund Insurance Policy."

<sup>(3)</sup> Includes the premium for the 2008 Certificate Insurance Policy and the Parity Reserve Fund Insurance Policy, fees and expenses of Special Counsel, Disclosure Counsel, Financial Advisor, and Trustee, and printing and other miscellaneous expenses.

## THE 2008 CERTIFICATES

### General

The 2008 Certificates represent the proportionate interests of the Owners in the 2008 Payments. The 2008 Certificates will be dated the date on which they are executed and delivered and will mature on the Maturity Date, subject to prepayment prior thereto as described below under "Prepayment." The 2008 Certificates will be initially executed and delivered in the Weekly Mode, and interest with respect to the 2008 Certificates in the Weekly Mode will be evidenced at the Weekly Rate. See "Interest Rate Provisions" below.

Upon delivery, the 2008 Certificates will be registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York ("DTC"). DTC will act as securities depository for the 2008 Certificates. Ownership interests in the 2008 Certificates may be purchased in book entry form only. See "Book-Entry-Only System" below. While the 2008 Certificates are in the Weekly Mode such ownership interests may be purchased in denominations of \$100,000 and integral multiples of \$5,000 in excess thereof.

### Book-Entry-Only System

The 2008 Certificates will be executed and delivered in book-entry form only. Purchasers of the 2008 Certificates will not receive certificates representing their ownership interests in the 2008 Certificates purchased but will receive credit balances on the books of their respective nominees. All

payments with respect to the 2008 Certificates are to be made by the Trustee directly to DTC. DTC is expected to credit such payments to the respective accounts of its Direct Participants which, in turn, are expected to make payment thereof to the purchasers of the 2008 Certificates.

As long as Cede & Co. is the registered owner of the 2008 Certificates, references herein to the Owners of the 2008 Certificates shall refer to Cede & Co. and not to the beneficial owners of the 2008 Certificates (the “Beneficial Owners”). *Neither the Authority nor the City gives any assurance that DTC, its Participants or others will distribute payments with respect to the 2008 Certificates or notices concerning the 2008 Certificates to the Beneficial Owners thereof or that DTC will otherwise serve and act in the manner described in this Official Statement.* See APPENDIX D — “INFORMATION CONCERNING DTC” for a further description of DTC and its book-entry system. The information presented therein is based solely on information provided by DTC.

The Authority may decide to discontinue the use of book-entry transfers through DTC (or a successor Securities Depository). In that event, the 2008 Certificates will be printed and delivered to the Beneficial Owners and will be governed by the provisions of the 2008 Trust Agreement with respect to the payment of principal and interest and rights of exchange and transfer.

### **Interest Rate Provisions**

***Establishment of the Weekly Rate.*** The 2008 Certificates will be executed and delivered in the Weekly Mode. The interest rate for the 2008 Certificates while they are in the Weekly Mode will be the rate of interest per annum determined by the Remarketing Agent on and as of the applicable Rate Determination Date (each Wednesday or, if Wednesday is not a Business Day, then the Business Day next succeeding such Wednesday) as the minimum rate of interest which, in the opinion of the Remarketing Agent under then-existing market conditions, would result in the sale of the 2008 Certificates at a price equal to 100% of the principal amount thereof. While the 2008 Certificates are in the Weekly Mode, the Remarketing Agent is obligated to establish the Weekly Rate by 4:00 p.m. New York City time on each Rate Determination Date; and the Weekly Rate shall be in effect during the applicable Weekly Rate Period (generally, the period commencing on Thursday of each week to and including Wednesday of the following week).

***Notification of the Weekly Rate.*** The Remarketing Agent is required to make the Weekly Rate available no later than 5:00 p.m. New York City time on the Business Day following the Rate Determination Date by telephone or Electronic means to the Authority, each other Notice Party and any Beneficial Owner requesting such rate.

***Alternate Rate.*** When the 2008 Certificates are in the Weekly Mode, in the event (i) the Remarketing Agent fails or is unable to determine the interest rate for the 2008 Certificates, (ii) the method by which the Remarketing Agent determines the interest rate with respect to the 2008 Certificates shall be held to be unenforceable by a court of law of competent jurisdiction, or (iii) the Remarketing Agent suspends its remarketing effort in accordance with the provisions of the Remarketing Agreement (as hereinafter defined), then the 2008 Certificates shall evidence interest during each subsequent Interest Period for the 2008 Certificates at the Alternate Rate in effect on the first day of such Weekly Rate Period. The Alternate Rate for the 2008 Certificates in the Weekly Mode as of any Rate Determination Date is a rate per annum equal to (a) the SIFMA Municipal Swap Index (the “SIFMA Rate”) most recently available as of the date of determination, or (b) if such index is no longer available, or if the SIFMA Rate is no longer published, the S&P Weekly High Grade Index (formerly the J.J. Kenny Index), or (c) if neither the SIFMA Rate nor the S&P

Weekly High Grade Index is published, the index determined to equal the prevailing rate determined by the Remarketing Agent for tax-exempt state and local government bonds meeting criteria determined in good faith by the Remarketing Agent to be comparable under the circumstances to the criteria used by the Securities Industry and Financial Markets Association (“SIFMA”) to determine the SIFMA Rate just prior to when the SIFMA stopped publishing the SIFMA Rate. If there is no Remarketing Agent for the 2008 Certificates, if the Remarketing Agent fails to make any such determination or if the Remarketing Agent has suspended its remarketing efforts in accordance with the Remarketing Agreement, then the Trustee shall make the determinations required by this definition, or if the Trustee shall decline to make such determination, a financial advisor, investment banker or other qualified party shall make such determination at the expense of the Authority. Such provisions will continue to apply until such time as the Remarketing Agent (or the Authority, if applicable) resumes making such determinations. In the case of clause (ii) above, the Remarketing Agent (or the Authority, if applicable) shall resume making such determination at such time as there is delivered to the Remarketing Agent or the Authority, as applicable, an opinion of Special Counsel to the effect that there are no longer any legal prohibitions against the Remarketing Agent or Authority, as applicable, making such determinations.

### **Optional Tender**

Subject to the availability of sufficient funds from either the remarketing of such 2008 Certificates or the Liquidity Facility, while the 2008 Certificates are in the Weekly Mode, any 2008 Certificate or portion thereof in a principal amount equal to an Authorized Denomination is required to be purchased on any Business Day at a price equal to the Purchase Price, upon delivery of a Tender Notice to the Trustee by 5:00 p.m. New York City time on the Business Day seven days prior to the applicable Purchase Date. See, “Purchase Fund,” “Delayed Remarketing Period,” “Liquidity Facility” and “LIQUIDITY FACILITY — Initial Liquidity Facility.” A Tender Notice is a notice delivered by Electronic means or in writing that states: (i) the principal amount of the 2008 Certificates to be purchased pursuant to the optional tender provisions of the 2008 Trust Agreement; (ii) the Purchase Date on which such 2008 Certificates are to be purchased; (iii) applicable payment instructions with respect to such 2008 Certificates being tendered for purchase; and (iv) an irrevocable demand for such purchase. For so long as the 2008 Certificates are registered in the name of Cede & Co., as nominee for DTC, the tender option rights of Owners of 2008 Certificates may be exercised only by a Direct Participant of DTC acting, directly or indirectly, on behalf of a Beneficial Owner of 2008 Certificates by giving notice of its election to tender 2008 Certificates or portions thereof at the time and in the manner described above. Beneficial Owners will not have any rights to tender 2008 Certificates directly to the Trustee.

If funds sufficient to pay the Purchase Price of any Certificate are held by the Trustee on any Purchase Date, such 2008 Certificate shall be deemed to have been purchased and shall be purchased according to the terms of the Trust Agreement, for all purposes of the Trust Agreement, irrespective of whether or not such 2008 Certificate shall have been delivered to the Trustee; and neither the former Owner of such 2008 Certificate nor any other person shall have any claim thereon, under the Trust Agreement or otherwise, for any amount other than the Purchase Price thereof.

### **Mandatory Tender for Purchase Upon Change of Mode**

***Changes in Mode.*** At the option of the Authority, the 2008 Certificates in the Weekly Mode may be changed to another Mode (other than a Fixed Rate Mode) as set forth below, provided that all the 2008 Certificates shall be converted.

Unless otherwise specified in the 2008 Trust Agreement, notice of the proposed change in Mode must be given by the Trustee to the Owners of the 2008 Certificates not less than the 15th day next preceding the applicable Mode Change Date. Such notice must state the Mode to which the conversion will be made and the proposed Mode Change Date and, if applicable, shall be combined with the notice of mandatory purchase required to be delivered by the Trustee pursuant to the 2008 Trust Agreement. The new Mode shall commence on the Mode Change Date and the interest rate(s), together, in the case of a change to the Flexible Mode, with the Interest Period or Interest Period(s), as applicable, shall be determined by the Remarketing Agent (or the Authority in the case of the Interest Period for the 2008 Certificates being converted to a Term Rate Mode) in the manner provided in the 2008 Trust Agreement.

In the case of a change from the Weekly Mode, the Mode Change Date can be any Business Day. The 2008 Certificates shall be subject to mandatory tender for purchase on such Mode Change Date as described below: and, except as is otherwise described herein, the 2008 Certificates shall be purchased on the Mode Change Date at a Purchase Price equal to 100% of the principal amount thereof; provided, however, that if the 2008 Certificates are to be purchased on an Interest Payment Date other than the last Interest Payment Date applicable to the 2008 Certificates, and if the 2008 Certificates would otherwise be subject to optional prepayment on such Mode Change Date at a prepayment price of more than 100% of the principal amount thereof, then the 2008 Certificates shall be purchased at a Purchase Price equal to such prepayment price.

***Conditions Precedent.*** It is a condition precedent to a change in Mode that certain items shall have been delivered to the Authority, Trustee, the 2008 Certificate Insurer, and the Remarketing Agent on or prior to the Mode Change Date. Those items include (a) in the case of a change from the Weekly Mode to any Mode other than the Daily Mode, a Favorable Opinion of Special Counsel dated the Mode Change Date and (b) a notice from the Rating Agencies of the rating(s) to be assigned to the 2008 Certificates on such Mode Change Date. In addition, the Authority must also have obtained and delivered to the Trustee the written consent of the 2008 Certificate Insurer to the change in Mode.

***Failure to Satisfy Conditions.*** In the event that the Authority has not withdrawn any election by it to change a Mode as described below and the conditions referred to above have not been satisfied by the applicable Mode Change Date, then the New Mode shall not take effect (although any mandatory purchase shall be made on such date if notice has been sent to the Owners stating that the 2008 Certificates would be subject to mandatory purchase on such date). In the case of a failed change in Mode from the Weekly Mode, the 2008 Certificates shall remain in the Weekly Mode with interest rates established in accordance with the provisions described above under “Interest Rate Provisions” on and as of the failed Mode Change Date.

***Rescission of Election to Change Mode.*** The Authority may rescind any election by it to change a Mode prior to the Mode Change Date by giving written notice thereof to the Notice Parties prior to such Mode Change Date. If the Trustee receives notice of such rescission prior to the time the Trustee has given notice to the Owners of the 2008 Certificates, then such notice of change in Mode shall be of no force and effect. If the Trustee receives notice from the Authority of rescission of a Mode change after the Trustee has given notice thereof to the Owners of the 2008 Certificates, then if the proposed Mode Change Date would have been a Mandatory Purchase Date, such date shall continue to be a Mandatory Purchase Date. If the proposed change in Mode was from the Weekly Mode, the 2008 Certificates shall remain in the Weekly Mode with interest rates established

in accordance with the provisions described above under “Interest Rate Provisions” on and as of the proposed Mode Change Date.

***Mandatory Tender for Purchase on Change of Mode.*** A change from the Weekly Mode to any other Mode will result in the mandatory purchase of the 2008 Certificates on the Mode Change Date. The Trustee is required to give notice of each such mandatory purchase by mail to the Owners of the 2008 Certificates subject to mandatory purchase no less than 15 days prior to the applicable Mandatory Purchase Date, which is the Mode Change Date. Such notice is required to state the Mandatory Purchase Date, set forth the Purchase Price applicable on such Mandatory Purchase Date, and identify the 2008 Certificates to be purchased. Such notice must also state that interest on the 2008 Certificates subject to mandatory purchase shall cease to accrue from and after the Mandatory Purchase Date. The failure to mail such notice with respect to any 2008 Certificate shall not affect the validity of the mandatory purchase of any other 2008 Certificate with respect to which notice was so mailed. Any notice mailed will be conclusively presumed to have been given, whether or not actually received by any Owner.

### **Other Mandatory Tenders**

The 2008 Certificates are subject to mandatory tender for purchase on each Mandatory Tender Date, In addition to Mode Change Dates, Mandatory Purchase Dates applicable to 2008 Certificates in the Weekly Mode are: (i) any Substitution Date (the date on which an Alternate Liquidity Facility is substituted for the Liquidity Facility then in effect); (ii) the fifth Business Day prior to an Expiration Date (the stated expiration date of a Liquidity Facility, as it may be extended from time to time as provided in such Liquidity Facility, or any earlier date on which such Liquidity Facility shall terminate at the direction of the Authority, expire or be cancelled, other than the date on which a Liquidity Facility shall terminate as a result of an Automatic Termination Event or an event of default under the Reimbursement Agreement entered into in connection with such Liquidity Facility); (iii) the date specified by the Trustee following the occurrence of an event of default with respect to the Liquidity Facility which requires or gives the Liquidity Facility Provider the option to terminate the Liquidity Facility upon notice and requires that all Outstanding 2008 Certificates secured by such Liquidity Facility be tendered for purchase under the applicable Reimbursement Agreement, which date shall be a Business Day not less than 20 days after the Trustee’s receipt of notice of such event of default from the applicable Liquidity Facility Provider and in no event later than the Business Day preceding the termination date specified in the notice of event of default delivered to the Trustee by such Liquidity Facility Provider; and (iv) any Business Day specified by the Authority in a notice delivered to the Trustee, which Mandatory Purchase Date shall be not less than twenty (20) days after the Trustee’s receipt of such notice from the Authority.

The Trustee is required to give notice of each such mandatory purchase at the same time and in the same manner as is described above under “Mandatory Tender for Purchase upon Change of Mode - *Mandatory Tender for Purchase on Change of Mode.*”

### **Purchase Fund**

The Trust Agreement requires the Trustee to establish and maintain a separate fund to be designated as the “2008 Purchase Fund” (the “2008 Purchase Fund”) and separate accounts therein to be designated as the “Remarketing Proceeds Account,” the “Liquidity Facility Account” and the “Authority Account.” The 2008 Purchase Fund shall be held in trust solely for the benefit of the Owners of tendered 2008 Certificates.

Upon receipt of the proceeds of a remarketing of any 2008 Certificate on the date such 2008 Certificate is to be purchased, the Trustee is required to deposit such remarketing proceeds in the Remarketing Proceeds Account to be applied to the payment of the Purchase Price of such 2008 Certificate. Upon receipt of the proceeds of a draw on a Liquidity Facility, the Trustee is required to deposit such Liquidity Facility proceeds in the Liquidity Facility Account to be applied to the payment of the Purchase Price of the 2008 Certificates to the extent that the moneys on deposit in the Remarketing Proceeds Account shall not be sufficient. Any amounts deposited in a Liquidity Facility Account and not needed for the payment of the Purchase Price of the 2008 Certificates shall be immediately returned to the applicable Liquidity Facility Provider. Upon receipt of funds from the Authority provided at its sole discretion for such purpose, the Trustee is required to deposit such funds in the Authority Account to be applied to the payment of the Purchase Price of the 2008 Certificates. Any amounts deposited in an Authority Account and not needed for the payment of the Purchase Price of the 2008 Certificates shall be immediately returned to the Authority. Amounts held in the Remarketing Proceeds Account, the Liquidity Facility Account and the Authority Account are not permitted to be commingled with any other funds held by the Trustee and must be held uninvested.

Each of the Remarketing Proceeds Account and the Liquidity Facility Account shall meet the requirements of an Eligible Account.

### **Liquidity Facility**

**Requirement.** While the 2008 Certificates are in the Weekly Mode, the Authority is required to provide a Liquidity Facility. Each such Liquidity Facility (and any Alternate Liquidity Facility provided in replacement thereof) must (i) be in an amount equal to the Required Stated Amount, (ii) be provided by a Liquidity Facility Provider and (iii) provide for the purchase of the 2008 Certificates upon their optional or mandatory tender in accordance with the provisions of the Trust Agreement. The Authority is not permitted to voluntarily terminate such Liquidity Facility or any Alternate Liquidity Facility without providing at least 30 days written notice to the Trustee and each of the other Notice Parties.

**Draws.** If a Liquidity Facility is in effect with respect to the 2008 Certificates, on each date on which a 2008 Certificate is to be purchased, the Trustee, by demand given by Electronic means before 12:30 p.m. New York City time, is required to draw on the applicable Liquidity Facility in accordance with the terms thereof so as to receive thereunder by 2:30 p.m. New York City time on such date an amount, in immediately available funds, sufficient, together with the proceeds of the remarketing of such 2008 Certificates on such date, to enable the Trustee to pay the Purchase Price in connection therewith. The proceeds of such draw shall be paid to the Trustee, who shall deposit said proceeds in the Liquidity Facility Account.

**Alternate Liquidity Facility.** The Authority may provide an Alternate Liquidity Facility on any Business Day not later than the fifth Business Day prior to the Expiration Date of the Liquidity Facility then in effect for the 2008 Certificates. Any such Alternate Liquidity Facility must be approved by the 2008 Certificate Insurer. The Authority must give at least 30 days' written notice to the Trustee and each of the Notice Parties of its intent to furnish an Alternate Liquidity Facility, which notice shall specify the nature of such Liquidity Facility, the identity of the Liquidity Facility Provider and the proposed Substitution Date. The Trustee must then give notice of each Mandatory Purchase Date resulting from the proposed delivery of an Alternate Liquidity Facility in accordance with the provisions set forth in the Trust Agreement.

On or before the Substitution Date, there must be delivered to the Trustee: (i) the Alternate Liquidity Facility in substitution for the Liquidity Facility then in effect, (ii) a Favorable Opinion of Special Counsel and (iii) a written Opinion of Counsel for the provider of Alternate Liquidity Facility to the effect that such Alternate Liquidity Facility is a legal, valid, and binding obligation of the provider thereof and covering such other matters as the Authority shall require. Upon the satisfaction of such conditions, the Trustee must accept such Alternate Liquidity Facility and surrender the Liquidity Facility then in effect to the provider thereof on the Substitution Date; provided that if there are insufficient remarketing proceeds to pay the Purchase Price of all 2008 Certificates subject to mandatory purchase on such Substitution Date, the Trustee may not surrender the Liquidity Facility then in effect until the Trustee shall have drawn upon the existing Liquidity Facility to pay the Purchase Price for the 2008 Certificates subject to mandatory purchase on such Substitution Date. If any condition precedent to the substitution of an Alternate Liquidity Facility is not satisfied, the substitution shall not occur, but the affected 2008 Certificates shall remain subject to mandatory purchase on the proposed Substitution Date.

### **Delayed Remarketing Period**

If sufficient funds are not available to pay the Purchase Price of all tendered 2008 Certificates (“Tendered Certificates”) to be purchased on any Purchase Date: (i) no purchase of such Tendered Certificates shall be consummated on such Purchase Date; (ii) all such Tendered Certificates shall be returned to the Owners thereof; (iii) all remarketing proceeds shall be returned to the Remarketing Agent for return to the persons providing such moneys; and (iv) such insufficiency and the failure to pay the Purchase Price on any Payment Date shall *not* constitute an Event of Default under the Trust Agreement. All such Tendered Certificates shall evidence interest at the Maximum Rate during the period of time from and including the applicable Purchase Date to (but not including) the date that all such Tendered Certificates are successfully remarketed (the “Delayed Remarketing Period”).

The Authority may direct the conversion of such Tendered Certificates to a different Mode during a Delayed Remarketing Period in accordance with the provisions of the Trust Agreement, but the Authority is not required to comply with the notice requirements otherwise applicable to a change of Mode.

During a Delayed Remarketing Period, the Remarketing Agent shall continue to use its best efforts to remarket such Tendered Certificates. Once the Remarketing Agent has advised the Trustee that it has a good faith belief that it is able to remarket all of such Tendered Certificates, the Trustee shall give written notice by mail to the Owners of such Tendered Certificates not later than five Business Days prior to the proposed Purchase Date, which notice shall state: (i) that such Tendered Certificates will be subject to mandatory tender for purchase on the proposed Purchase Date; (ii) the proposed Purchase Date; (iii) the Mode applicable to such Tendered Certificates from and after the proposed Purchase Date; (iv) the procedures for such mandatory tender for purchase; (v) the Purchase Price applicable to such Tendered Certificates; and (vi) the consequences of a failed remarketing.

The Trustee may, upon direction of the Authority, apply amounts on deposit in the 2008 Prepayment Subaccount of the 2008 Principal Account to the prepayment of Tendered Certificates, as a whole or in part on any Business Day during such Delayed Remarketing Period, at a prepayment price equal to the principal amount thereof, together with interest accrued thereon to the date fixed for prepayment, without premium. The Trustee shall give five (5) Business Days’ notice of such prepayment to the Owners of the 2008 Certificates to be prepaid.

Interest on Tendered Certificates shall be paid to the Owners thereof (i) on the first Business Day of each calendar month occurring during a Delayed Remarketing Period and (ii) on the day after the last day of such Delayed Remarketing Period.

## Prepayment

**Optional Prepayment.** Each 2008 Certificate in the Weekly Mode is subject to prepayment at the option of the Authority, in whole or in part, in Authorized Denominations on any Business Day, at a prepayment price equal to 100% of the principal amount thereof, plus, accrued interest, if any, to the Prepayment Date, without premium.

**Mandatory Sinking Fund Prepayment.** Except in the case of 2008 Certificates that have been converted to Serial Certificates upon a change to the Fixed Rate Mode, the 2008 Certificates are subject to mandatory prepayment from Sinking Fund Payments prior to the Maturity Date, in part by lot, on October 1 of each year on and after October 1, 2008, in accordance with the schedule set forth below upon notice hereinafter described, from and in the amount of the principal installment of the 2008 Payments due and payable on such dates, at a prepayment price equal to the sum of the principal amount evidenced and represented thereby plus accrued and unpaid interest evidenced and represented thereby to the Prepayment Date, without a prepayment premium. In addition, if any 2008 Certificates have been optionally prepaid, the amounts of such Sinking Fund Payments shall be reduced as directed by the Authority, or if not so directed, proportionality in increments of Authorized Denominations, by the principal amount evidenced and represented by all such 2008 Certificates so optionally prepaid.

<i>Mandatory Sinking Fund Payment Date (October 1)</i>	<i>Sinking Fund Payment</i>	<i>Mandatory Sinking Fund Payment Date (October 1)</i>	<i>Sinking Fund Payment</i>
2008	\$290,000	2023	\$2,300,000
2009	285,000	2024	2,410,000
2010	285,000	2025	2,515,000
2011	285,000	2026	2,595,000
2012	310,000	2027	2,705,000
2013	310,000	2028	2,810,000
2014	340,000	2029	2,945,000
2015	340,000	2030	3,055,000
2016	365,000	2031	3,185,000
2017	365,000	2032	3,295,000
2018	395,000	2033	3,430,000
2019	395,000	2034	3,570,000
2020	395,000	2035	3,705,000
2021	425,000	2036 (maturity)	3,870,000
2022	450,000		

Notwithstanding the foregoing, no 2008 Certificate (other than a Liquidity Provider Certificate) shall be optionally prepaid while any Liquidity Provider Certificate is Outstanding unless all Outstanding Liquidity Provider Certificates are prepaid or purchased by the Trustee and cancelled concurrently with such prepayment or purchase.

If for any reason, the Liquidity Provider Certificates remain in book-entry but have not been assigned a separate CUSIP number, the Trustee shall apply the amounts in the 2008 Sinking Fund Subaccount set aside for prepayment to the purchase from the Liquidity Facility provider of Liquidity Provider Certificates in an aggregate principal amount not in excess of the principal amount intended to be prepaid at a purchase price equal to the prepayment price specified above. The Liquidity Provider Certificates so purchased shall be cancelled by the Trustee, and the principal amount thereof shall be credited against the principal amount of the 2008 Certificates otherwise required to be prepaid.

***Notice of Prepayment.*** When the prepayment of 2008 Certificates is authorized as described above, the Trustee is required to give notice thereof. Such notice must state the date of such notice, the prepayment price, the place of prepayment (including the name and appropriate address of the Trustee), the CUSIP number (if any) of the 2008 Certificates to be prepaid, and, if less than all of the 2008 Certificates are to be prepaid, the distinctive certificate numbers thereof to be prepaid and, in the case of 2008 Certificates to be prepaid in part only, the respective portions of the principal amount evidenced and represented thereby to be prepaid. Each such notice shall also state that on said date there will become due and payable on each of said 2008 Certificates the prepayment price thereof and, in the case of a 2008 Certificate to be prepaid in part only, the specified portion of the principal amount evidenced and represented thereby to be prepaid, together with accrued and unpaid interest evidenced and represented thereby to the prepayment date, and that from and after such prepayment date interest evidenced and represented thereby shall cease to accrue; and such notice shall require that said 2008 Certificates be then surrendered at the address of the Trustee specified in the prepayment notice.

Such notice must be mailed by the Trustee, at least 30 but not more 60 days before the prepayment date to the respective Owners of the 2008 Certificates designated for prepayment at their addresses appearing on the registration books of the Trustee. Such notice is also required to be provided to Securities Depositories and Information Services. Failure to receive such notice shall not invalidate any of the proceedings taken in connection with such prepayment.

Any prepayment may be cancelled if the notice of such prepayment has not been mailed to the respective Owners of the 2008 Certificates or if such notice expressly conditioned the prepayment upon the occurrence of one or more events. Notice of any such cancellation shall be given in the same manner as the notice of prepayment was given at least three Business Days prior to the date scheduled for prepayment.

***Effect of Prepayment.*** If notice of prepayment has been duly given as described above and money for the payment of the prepayment price of the 2008 Certificates called for prepayment together with any accrued interest to the date fixed for prepayment is held by the Trustee, then on the prepayment date designated in such notice, the 2008 Certificates so called for prepayment will become due and payable on the date fixed for prepayment at the prepayment price specified in such notice; and from and after the date so designated, interest evidenced and represented by such 2008 Certificates so called for prepayment shall cease to accrue, and the Owners of such 2008 Certificates shall have no rights in respect thereof except to receive payment of the prepayment price thereof.

### **Purchase in Lieu of Prepayment**

Subject to the provisions of the 2008 Trust Agreement, the Authority has the option to purchase any 2008 Certificate on any date on which it would be subject to optional prepayment at a

purchase price equal to the then applicable prepayment price plus accrued interest thereon to the date of purchase.

### **Parity Obligations**

The City has previously incurred obligations payable from Gross Revenues of its Water Utility System on a parity with the 2008 Payments; and, under the terms of the Master Contract, the City may incur additional such obligations in the future. In addition to the 1997 Payments and its obligation to make the scheduled payments required pursuant to the 2008 Swap Agreement, its obligation to make termination payments under the 2008 Swap Agreement (but only if such payments are insured under the Swap Policy) and its obligations under the Reimbursement Agreement and the Liquidity Facility, the City currently has outstanding unpaid Parity Obligations with MID and the State of California Department of Water Resources (“CDWR”). See “SECURITY FOR THE 2008 CERTIFICATES — Existing and Future Parity Obligations.”

## **SECURITY FOR THE 2008 CERTIFICATES**

### **General**

Each 2008 Certificate represents a proportionate interest in the 2008 Payments to be made by the City under the 2008 Contract. Pursuant to the 2008 Trust Agreement, the Authority will assign substantially all of its right, title and interest in the 2008 Contract to the Trustee for the benefit of the Owners of the 2008 Certificates. The rights so assigned include the Authority’s right to receive the 2008 Payments and its right to exercise any remedies provided in the 2008 Contract in the event of a default by the City thereunder.

Pursuant to the 2008 Contract, the City will purchase the 2008 Project from the Authority at the purchase price specified in the 2008 Contract, which is equal to the aggregate principal amount evidenced by the 2008 Certificates. The City is obligated to make such purchase by paying the 2008 Payments specified in the 2008 Contract including the interest on such payments.

### **2008 Payments**

Pursuant to the 2008 Trust Agreement, the Authority will transfer, assign and set over to the Trustee all of the 2008 Payments and any and all rights and privileges it has under the 2008 Contract with respect to the 2008 Certificates, including, without limitation, the right to collect and receive directly all of the 2008 Payments and the right to hold and enforce any security interest.

The 2008 Payments under the 2008 Contract represent the purchase price of the 2008 Project, which the Authority is selling to the City pursuant to the 2008 Contract for the purpose of refinancing the 2006 Project. The obligation of the City to pay the 2008 Payments from Gross Revenues is absolute and unconditional; and, until such time as the 2008 Payments shall have been paid in full (or provision for the payment thereof shall have been made pursuant to the Master Contract), the City will not discontinue or suspend any 2008 Payments required to be paid by it under the 2008 Contract when due, whether or not the Water Utility System or any part thereof (including the 2008 Project) is operating or operable, or its use is suspended, interfered with, reduced, curtailed or terminated in whole or in part; and such payments are not subject to reduction whether by offset, abatement or otherwise and are not conditional upon the performance or nonperformance by any party to any agreement for any cause whatsoever. Notwithstanding anything contained in the Contract, however,

the City is not required to advance any moneys derived from any source of income other than the Gross Revenues for the payment of the 2008 Payments or for the performance of any agreements or covenants required to be performed by it contained in the Contract.

As more fully described below, under the Contract, Gross Revenues of the Water Utility System are pledged as security for the payment of the 1997 Payments, the 2008 Payments, any other Parity Obligations and the Maintenance and Operation Costs, as defined below.

“Water Utility System” is defined under the Master Contract to mean (i) all property rights, contractual rights and facilities of the City relating to water, including all facilities, properties, structures or works for the treatment, conservation, storage, transmission and distribution of water now owned by the City and (ii) all additions, betterments, extensions or improvements to such facilities, properties, structures or works or any part thereof hereafter acquired and constructed.

“Gross Revenues” is defined under the Master Contract to mean all gross income and revenue received or receivable by the City from the ownership or operation of the Water Utility System, determined in accordance with Generally Accepted Accounting Principles, including all rates, fees and charges (including all Connection Fees, contributions in aid of construction, and charges and standby water availability charges legally available for debt service) received by the City for the Water Service and the other services and facilities of the Water Utility System and all net proceeds of insurance covering business interruption loss relating to the Water Utility System and all other income and revenue howsoever derived by the City from the ownership or operation of the Water Utility System or arising from the Water Utility System, and including all Payment Agreement Receipts, and including all income from the deposit or investment of any money in the Revenue Fund or, to the extent deposited in the Revenue Fund, in the Parity Reserve Fund, but excluding in all cases any proceeds of taxes and any refundable deposits made to establish credit and advances.

“Maintenance and Operation Costs” is defined under the Master Contract to mean the costs paid or incurred by the City for maintaining and operating the Water Utility System, determined in accordance with Generally Accepted Accounting Principles, including, but not limited to, (a) all reasonable expenses of management and repair and other expenses necessary to maintain and preserve the Water Utility System in good repair and working order, (b) all costs of water purchased by the City including all costs under the Treatment and Delivery Agreement by and among the City, the Del Este Water Company and MID (which has since been amended and restated) which do not constitute debt service thereunder, (c) all administrative costs of the City that are charged directly or apportioned to the operation of the Water Utility System, such as salaries and wages of employees, overhead, taxes (if any) and insurance premiums, payments into pension funds, and (d) all other reasonable and necessary costs of the City or charges required to be paid by it to comply with the terms of the Master Contract or of any resolution authorizing the execution of any Parity Obligation or of such Parity Obligation, such as compensation, reimbursement and indemnification of the trustee or remarketing agent for any such Parity Obligation, letter of credit fees for any such Parity Obligations, and fees and expenses of Independent Certified Public Accountants and Independent Consultants, but excluding in all cases (1) depreciation, replacement and obsolescence charges or reserves therefor and amortization of intangibles, premiums and discounts, (2) interest expense, (3) amounts paid from funds of the City other than Gross Revenues, and (4) in-lieu transfers or recoupment of contributed capital to the City’s general fund.

## **Pledge of Gross Revenues**

Pursuant to the Contract, all Gross Revenues of the Water Utility System are irrevocably pledged to the payment of the 1997 Payments, the 2008 Payments, any other Parity Obligations and the Maintenance and Operation Costs; and the Gross Revenues of the Water Utility System may not be used for any other purpose while any of the 1997 Payments or the 2008 Payments remain unpaid; provided, however, that out of Gross Revenues there may be apportioned such sums for such purposes as are expressly permitted by the Contract. Such pledge constitutes a first pledge of and charge and lien upon the Gross Revenues of the Water Utility System for the payment of the amounts due with respect to the Contract, other Parity Obligations and the Maintenance and Operation Costs in accordance with the terms of the Contract.

## **Rate Covenant**

Pursuant to the Master Contract, the City covenants that it will at all times fix, prescribe and collect rates, fees and charges for the Water Service during each Fiscal Year which are reasonably fair and nondiscriminatory and which will be at least sufficient to yield Adjusted Annual Net Revenues for such Fiscal Year equal to at least 125% of Annual Debt Service to be paid during such Fiscal Year (the “Rate Covenant”).

“Adjusted Annual Net Revenues” is defined under the Master Contract to mean, for any Fiscal Year or any designated 12-month period in question, the Adjusted Annual Gross Revenues during such Fiscal Year or 12-month period less the Maintenance and Operation Costs during such Fiscal Year or 12-month period.

“Adjusted Annual Gross Revenues” is defined under the Master Contract to mean, for any Fiscal Year or any designated 12-month period in question, the Gross Revenues during such Fiscal Year or 12-month period, plus deposits to the City of Modesto Water Utility System Revenue Fund (the “Revenue Fund”) from amounts on deposit in the Rate Stabilization Fund, but only as and to the extent specified in the Master Contract, minus (y) amounts transferred from the Revenue Fund to the Rate Stabilization Fund in accordance with the Master Contract and, (z) for purposes of determining compliance with the rate covenant described above only, earnings from the investments in the Parity Reserve Fund that are deposited in the Revenue Fund in such Fiscal Year or 12-month period.

“Adjusted Annual Debt Service” is defined under the Master Contract to mean, for any Fiscal Year or any designated 12-month period in question, the Annual Debt Service for such Fiscal Year or 12-month period minus the sum of (i) for purposes of the rate covenant described above only, the earnings from the investments in the Parity Reserve Fund that are deposited in the Revenue Fund in such Fiscal Year or 12-month period, and (ii) the amount of the Annual Debt Service paid from the proceeds of Parity Obligations or interest earned thereon (other from the Parity Reserve Fund), all as set forth in a Certificate of the City.

“Annual Debt Service” is generally defined under the Master Contract to mean, for any Fiscal Year or any designated 12-month period in question, the payments required to be made with respect to all Outstanding Parity Obligations in such Fiscal Year or 12-month period; provided, that for purposes of determining compliance with the rate covenant described above, the Reserve Fund Requirement and conditions for the execution of Parity Obligations, certain additional provisions are applicable as described in APPENDIX B — “DEFINITIONS AND SUMMARY OF PRINCIPAL LEGAL DOCUMENTS.”

The City's ability to comply with the Rate Covenant may be limited by provisions of the California Constitution. See "THE WATER UTILITY SYSTEM — Impact of Proposition 218 on Water Utility System Fees and Charges." The opinion of Sidley Austin LLP, Special Counsel, with respect to the 2008 Certificates will state that the enforceability of the Contract is subject to the limitations on the imposition by the City of certain fees and charges relating to the Water Utility System under Articles XIII C and XIII D of the California Constitution. See APPENDIX C — "PROPOSED FORM OF OPINION OF SPECIAL COUNSEL." The City's ability to comply with the Rate Covenant may also be adversely affected by other factors. See "RISK FACTORS."

### **Parity Reserve Fund**

The Parity Reserve Fund was initially established pursuant to a trust agreement, dated as of November 1, 1997 (the "1997 Trust Agreement"), which provided for the execution and delivery of the City's Refunding Revenue Certificates of Participation (1997 Water Utility System Refinancing Project) (the "1997 Certificates"). The 1997 Certificates represent the proportionate, undivided interests in the 1997 Payments pursuant to the 1997 Contract. All amounts on deposit in the Parity Reserve Fund are available to be transferred to pay principal and interest evidenced and represented by both the 1997 Certificates and the 2008 Certificates and any other obligations in connection with a future supplement to the Contract (collectively, the "Parity Certificates") as described in greater detail below.

In connection with the execution and delivery of the 1997 Certificates, the City caused to be delivered to the then Trustee to be held in the Parity Reserve Fund in satisfaction of the Reserve Fund Requirement a municipal bond debt service reserve fund policy (the "1997 Certificate Reserve Policy") issued by Financial Guaranty Insurance Company, doing business in California as FGIC Insurance Company ("FGIC"). However, as a result of recent reductions in the ratings assigned to obligations insured by FGIC, the 1997 Certificate Reserve Policy must be replaced with cash or a Reserve Funding Instrument (as defined below). Concurrently with the execution and delivery of the 2008 Certificates, the Trustee will credit the Parity Reserve Fund Insurance Policy to the Parity Reserve Fund; and, as a result of the foregoing, the balance then on deposit in the Parity Reserve Fund will be equal to the Reserve Fund Requirement. See "CERTIFICATE INSURANCE — The Reserve Fund Insurance Policy" for a description of the Parity Reserve Fund Insurance Policy.

"Reserve Fund Requirement" is defined under the Master Contract to mean, as of any date of determination and excluding any Parity Obligations which are not Supplemental Contracts and the debt service thereon, the least of (a) 10% of the initial offering price to the public of the Parity Obligations as determined under the Code, or (b) the Maximum Annual Debt Service, or (c) 125% of the Average Annual Debt Service, all as computed and determined by the City and specified in writing to the Trustee; provided, that such requirement (or any portion thereof) may be provided by one or more policies of municipal bond insurance or surety bonds issued by a municipal bond insurer or by a letter of credit issued by a bank or other institution if the obligations insured by such insurer or issued by such bank or other institution, as the case may be, have ratings at the time of issuance of such policy or surety bond or letter of credit equal to "Aa" or higher assigned by Moody's (if Moody's is then rating any of the Parity Obligations) and "AA" or higher assigned by S&P (if S&P is then rating any of the Parity Obligations) and that maintain at all times ratings at least equal to the lowest ratings (without giving effect to municipal bond insurance or other credit enhancement) on any of the Parity Obligations provided by Moody's (if Moody's is then rating any of the Parity Obligations) and by S&P (if S&P is then rating any of the Parity Obligations) (all such instruments collectively, "Reserve Funding Instruments"). If at any time, obligations insured by any such

municipal bond insurer issuing a policy of municipal bond insurance or surety bond or a bank or other institution issuing a letter of credit as permitted by the definition of Reserve Fund Requirement shall no longer maintain such ratings as required in accordance with the immediately preceding sentence, the City shall provide or cause to be provided cash or a substitute municipal bond insurance policy or surety bond or a letter of credit meeting such requirements.

Pursuant to the 2008 Trust Agreement, the Trustee is to (i) withdraw and use all cash, if any, on deposit in the Parity Reserve Fund prior to using and withdrawing any amounts derived from payments under any Reserve Funding Instruments and (ii) draw on all Reserve Funding Instruments on a pro rata basis, based on the draw limit of each Reserve Funding Instrument. Amounts received by the Trustee from the City pursuant to the Master Contract as a replenishment of amounts withdrawn from the Parity Reserve Fund shall be applied first on a pro rata basis to reimburse draws on Reserve Funding Instruments and then to replenish cash withdrawn from the Parity Reserve Fund.

Moneys on deposit in the Parity Reserve Fund will be transferred by the Trustee to the debt service fund established pursuant to the 1997 Trust Agreement and/or to the 2008 Debt Service Fund established pursuant to the 2008 Trust Agreement to pay principal and interest evidenced and represented by the 1997 Certificates and by the 2008 Certificates, respectively, on any date on which interest is payable with respect thereto in the event amounts on deposit in the applicable debt service fund are insufficient for such purposes. The Trustee will also, from such amounts on deposit in the Parity Reserve Fund, transfer or cause to be transferred to any applicable debt service fund established under any other trust agreement under which any obligations are issued in connection with a Supplemental Contract, without preference or priority between transfers made pursuant to this sentence and the preceding sentence, and in the event of any insufficiency of such moneys ratably without discrimination or preference, that sum or sums, if any, equal to the amount required to be deposited therein pursuant to such trust agreement under which any obligations are issued in connection with a Supplemental Contract. Following the valuation of investments in the Parity Reserve Fund on or before each October 1, all moneys on deposit in the Parity Reserve Fund in excess of the Reserve Fund Requirement will be transferred by the Trustee to the City for deposit in the Revenue Fund.

## **Flow of Funds**

***Contract Provisions.*** The City agrees and covenants in the Contract that all Gross Revenues it receives will be deposited when and as received in the Revenue Fund, which the City established under the Master Contract and which the City agrees and covenants to maintain separate and apart from other moneys of the City so long as any Parity Obligations remain unpaid, and all money on deposit in the Revenue Fund is to be applied and used as follows. The City will pay at the following times in the following order of priority:

(1) *Payment of Maintenance and Operation Costs and Parity Obligation Payment Fund Deposits.* The City will, from the money in the Revenue Fund, without preference or priority, and in the event of any insufficiency of such moneys, ratably, without preference or priority (i) pay charges for Maintenance and Operation Costs of the Water Utility System (including amounts reasonably required to be set aside in contingency reserves for Maintenance and Operation Costs the payment of which is not then immediately required) as such charges are due and payable, and (ii) deposit in the City of Modesto Water Utility System Parity Obligation Payment Fund established under the Master Contract, on the last Business Day of each month (1) an amount equal to the interest which has accrued or will

accrue under all Parity Obligations during the next succeeding month calculated as if such interest has accrued or will accrue on a daily basis during such period, and (2) an amount equal to the principal which has accrued or will accrue (as a result of maturity, mandatory sinking fund payments or mandatory prepayment or otherwise) under all Parity Obligations during the next succeeding month calculated as if such principal has accrued or will accrue on a daily basis during such period, plus (3) the net payments due or which will be due on all Parity Payment Agreements calculated as if such net payments accrued or will accrue on a daily basis during such period, except that no such deposit need be made if the City then holds money in the Parity Obligation Payment Fund at least equal to the amount of interest and principal due or becoming due and payable under all Parity Obligations on the next succeeding date on which interest or principal becomes due and payable under any Parity Obligation plus the net payments due on all Parity Payment Agreements on such next succeeding due date therefor. Moneys on deposit in the Parity Obligation Payment Fund will be transferred by the City to make and satisfy the payments due on the next applicable date on which interest or principal becomes due and payable under any Parity Obligation or any net payment becomes due and payable by the City under any Parity Payment Agreement at least one Business Day prior to such next applicable due date.

(2) *Parity Reserve Fund Deposits.* On or before the last Business Day of each month, the City will, from the remaining money on deposit in the Revenue Fund after deposits and transfers pursuant to paragraph (1) above, transfer to the Trustee for deposit in the Parity Reserve Fund that sum, if any, necessary to restore the Parity Reserve Fund to an amount equal to the Reserve Fund Requirement. The City will also, from such remaining moneys in the Revenue Fund, transfer or cause to be transferred to the applicable reserve fund or account for any Parity Obligations for which a separate reserve has been funded, without preference or priority between transfers made in accordance with this sentence and the preceding sentence, and in the event of any insufficiency of such moneys ratably without any discrimination or preference, the sum or sums, if any, equal to the amount required to be deposited therein pursuant to such Parity Obligations.

After making the foregoing deposits and transfers, the City may apply any remaining money in the Revenue Fund for any lawful purpose of the City, including for the payment of any Subordinate Obligations in accordance with the instruments authorizing such Subordinate Obligations.

Pursuant to the Master Contract, the City has established the Rate Stabilization Fund, which has a balance of \$3,000,000 on deposit therein. The City may deposit in the Rate Stabilization Fund any Gross Revenues, after providing for the payment of Parity Obligations and Maintenance and Operation Costs, and any other money received and available to be used therefor, provided that deposits from such Gross Revenues for each Fiscal Year may be made until (but not after) 180 days after the end of such Fiscal Year. The City may withdraw amounts from the Rate Stabilization Fund only for inclusion in Adjusted Annual Net Revenues, such withdrawal to be made until (but not after) 180 days after the end of such Fiscal Year. All interest or other earnings upon deposits in the Rate Stabilization Fund will be accounted for as Gross Revenues. Notwithstanding the foregoing, no Gross Revenues will be deposited in the Rate Stabilization Fund to the extent that such amount was included by the City in Adjusted Annual Net Revenues for purposes of determining compliance with the rate covenant set forth in the Master Contract or the conditions for the execution of Parity Obligations contained in the Master Contract and deduction of the amounts to be deposited in the Rate Stabilization Fund would have caused noncompliance with such rate covenant or conditions.

The City's ability to set rates, fees and charges for the Water Service at levels which would permit the City to make deposits into the Rate Stabilization Fund may be limited by amendments to the California Constitution. See "THE WATER UTILITY SYSTEM — Impact of Proposition 218 on Water Utility System Fees and Charges." See also "THE WATER UTILITY SYSTEM — Summary of Projected Operating Results of the Water Utility System" for currently anticipated deposits into and withdrawals from the Rate Stabilization Fund.

The 2008 Contract establishes within the Parity Obligation Payment Fund the 2008 Supplemental Contract Payment Account. On or before the third Business Day immediately preceding each 2008 Payment Date or the date on which any net scheduled payment or insured termination payment is due under the 2008 Swap Agreement, the City shall, from the money in the Parity Obligation Payment Fund, deposit in the 2008 Supplemental Contract Payment Account (i) a sum equal to the amount of the interest and principal components of the 2008 Payments becoming due and payable under the 2008 Supplemental Contract on the next succeeding 2008 Payment Date and (ii) the net scheduled payments and any insured termination payment, if applicable, due under the 2008 Swap Agreement, except that no such deposit need be made if the amount then on deposit in the 2008 Supplemental Contract Payment Account is at least equal to the amount of the interest and principal components of the 2008 Payments becoming due and payable under the 2008 Contract on the next succeeding 2008 Payment Date plus the net scheduled payments and any insured termination payment, if applicable, due under the 2008 Swap Agreement on such next succeeding due date therefor. Moneys on deposit in the 2008 Supplemental Contract Payment Account shall (i) be transferred by the City to the Trustee on the Business Day immediately preceding each 2008 Payment Date to make and satisfy the 2008 Payment due on such 2008 Payment Date and (ii) be transferred by the City to the Trustee on the due date therefor to satisfy any net scheduled payment and any insured termination payment, if applicable, due under the 2008 Swap Agreement, all in accordance with the Master Contract and the 2008 Trust Agreement.

***2008 Trust Agreement Provisions.*** Pursuant to the 2008 Trust Agreement, the Trustee is required to deposit the 2008 Payments in a separate fund established by it and designated as the 2008 Debt Service Fund. The 2008 Debt Service Fund will contain two accounts: the 2008 Interest Account and the 2008 Principal Account (with a 2008 Prepayment Subaccount and a 2008 Sinking Fund Subaccount therein).

On the Business Day immediately preceding each Interest Payment Date commencing May 30, 2008, the Trustee is required to set aside from the 2008 Debt Service Fund and deposit in the 2008 Interest Account an amount equal to the amount of interest evidenced and represented by the 2008 Certificates becoming due and payable on each such Interest Payment Date. No deposit is required to be made in the 2008 Interest Account if the amount contained therein (exclusive of amounts transferred for the payment of amounts due under the 2008 Swap Agreement) is at least equal to the aggregate amount of interest evidenced and represented by the 2008 Certificates becoming due and payable on the applicable Interest Payment Date. The Trustee is also required to deposit in the 2008 Interest Account any receipts relating to the 2008 Swap Agreement which the City has directed under the 2008 Swap Agreement to be transferred to the Trustee for deposit in the 2008 Interest Account and any amounts transferred to Trustee pursuant to the 2008 Contract for the payment of payments due under the 2008 Swap Agreement.

Except as otherwise provided in the 2008 Trust Agreement, all money in the 2008 Interest Account is required to be used and withdrawn by the Trustee solely for the purpose of paying the interest with respect to the 2008 Certificates as it shall become due and payable (including accrued

interest evidenced and represented by any 2008 Certificates purchased or prepaid prior to their respective Certificate Payment Date) and the net scheduled payments due to the Swap Provider under the 2008 Swap Agreement. The Trustee shall be under no obligation to calculate the amount of Payment Agreement Payments due under the 2008 Interest Rate Swap Agreement and shall be entitled to rely conclusively on the information received by it with respect to the amount of the Payment Agreement Payments due and owing by the City. On the Business Day immediately preceding each October 1, commencing on October 1, 2008, the Trustee is required to set aside from the 2008 Debt Service Fund and deposit in the 2008 Principal Subaccount (i) an amount equal to the principal amount evidenced and represented by the Outstanding Serial Certificates with a Certificate Payment Date of such October 1 (at the time of the execution and delivery of the 2008 Certificates, none of the 2008 Certificates will be Serial Certificates) and (ii) in the 2008 Sinking Fund Subaccount the amount of all Sinking Fund Payments required to be made on such October 1. Amounts to be applied to the optional prepayment of the principal component of the 2008 Certificates are to be deposited in the 2008 Prepayment Subaccount. No deposit need be made in the 2008 Principal Account if the amount contained therein is at least equal to the aggregate amount of the principal evidenced and represented by the Outstanding Serial Certificates with a Certificate Payment Date of such October 1 and the amount contained in the 2008 Sinking Fund Subaccount is at least equal to the aggregate amount of all Sinking Fund Payments required to be made on such October 1.

All money in the 2008 Principal Account is required to be used and withdrawn by the Trustee solely for the purpose of paying the principal evidenced and represented by the Serial Certificates as they shall become due and payable, whether at their respective Certificate Payment Dates or on prior prepayment, and all money in the 2008 Sinking Fund Subaccount is required to be used and withdrawn by the Trustee only to purchase or to prepay or pay Term Certificates, and with respect to the 2008 Sinking Fund Subaccount, on each Sinking Fund Payment Date, the Trustee is required to apply the Sinking Fund Payment required on that date to the prepayment (or payment at the Certificate Payment Date, as the case may be) of the Term Certificates upon the notice and in the manner provided in the 2008 Trust Agreement, provided that at any time prior to giving notice of such prepayment, the Trustee may, upon the Written Request of the Authority and receipt of sufficient moneys therefor, purchase for cancellation Term Certificates in accordance with the 2008 Trust Agreement.

### **Existing and Future Parity Obligations**

Upon the execution and delivery of the 2008 Certificates, the obligation of the City to pay the 2008 Payments will be secured on a parity lien basis with certain existing Parity Obligations. In the Master Contract (as clarified in the 2008 Contract), "Parity Obligations" is specifically defined as the payment obligations under the Treatment and Delivery Agreement which constitute debt service, the payment obligations under the CDWR Loan Agreement, and all Supplemental Contracts and all other obligations hereafter incurred by the City the payment of which constitutes a charge and lien on the Gross Revenues equal to and on a parity with the charge and lien upon the Gross Revenues for the payment of the Payments, other than (i) such portion of the payment obligations (including certain payments due upon an early termination thereof) under any Parity Payment Agreement to the extent such obligations are expressly subordinate to Parity Obligations pursuant to the terms of such Parity Payment Agreement and (ii) Parity Bank Agreements; provided that no amounts have been drawn under any such Parity Bank Agreements which have not been reimbursed by the City. Under the Master Contract "CDWR Loan" means the loan to the City from the State of California Department of Water Resources in the principal amount of \$3,607,343.72 which \$1,754,299 was outstanding as

of April 1, 2008; and “Treatment and Delivery Agreement” means the Treatment and Delivery Agreement by and among the City of Modesto, the Del Este Water Company and MID. The Treatment and Delivery Agreement has since been amended and restated and is now called “Amended and Restated Treatment and Delivery Agreement Between Modesto Irrigation District and City of Modesto.” Under the Treatment and Delivery Agreement, the City has agreed to pay all debt service on bonds issued by MID for the construction of the Water Treatment Plant (including, but not limited to, the 2007 MID Bonds), a raw water charge, project operation, administrative services and maintenance costs, insurance on the plant and the cost of electrical energy provided to the plant. The outstanding principal amount of bonds issued for the Water Treatment Plant as of April 1, 2008 was \$163,880,000. See “THE WATER UTILITY SYSTEM — Treatment and Delivery Agreement” for a description of the Treatment and Delivery Agreement and “THE WATER UTILITY SYSTEM — Summary of Projected Operating Results of the Water Utility System” for additional information concerning existing Parity Obligations. See also Appendix B — “DEFINITIONS AND SUMMARY OF PRINCIPAL DOCUMENTS.” In addition to the Parity Obligations specifically defined as such in the Master Contract, the 2008 Swap Agreement (to the extent described above) and the 1997 Contract constitute Parity Obligations. The principal amount of the 1997 Payments currently outstanding is \$18,855,000. The Reimbursement Agreement and the Liquidity Facility constitute Parity Bank Agreements under the Contract; and Parity Bank Agreements are Parity Obligations if any amounts have been drawn thereunder which have not been reimbursed by the City.

In addition to the existing Parity Obligations, the City may at any time execute additional Parity Obligations, but subject to the specific conditions set forth in the Master Contract, including the conditions that there be on file with the Trustee either:

(1) A Certificate of the City demonstrating that during any 12 consecutive calendar months out of the immediately preceding 18 calendar month period, the Adjusted Annual Net Revenues were at least equal to 125% of the Maximum Annual Debt Service for all existing Parity Obligations plus the Parity Obligations proposed to be executed; provided, that for the purpose of providing such Certificate, the City may adjust the foregoing Adjusted Annual Net Revenues to reflect:

(i) An allowance for Gross Revenues that would have been derived from each new connection to the Water Utility System that was made prior to the execution of such Parity Obligations but which, during all or any part of said 12 month period, was not in existence, in an amount equal to the estimated additional Gross Revenues that would have been derived from each such connection if it had been made prior to the beginning of said 12 month period, and

(ii) An allowance for Gross Revenues that would have been derived from any increase in the rates, fees and charges fixed and prescribed for Water Service which became effective prior to the execution of such Parity Obligations but which, during all or any part of said 12 month period, was not in effect, in an amount equal to the estimated additional Gross Revenues that would have been derived from such increase in rates, fees and charges if it had been in effect prior to the beginning of said 12 month period; or

(2) A Consultant’s Report showing that the Adjusted Annual Net Revenues for the Fiscal Year next following the end of the period during which interest on the Parity Obligations proposed to be executed is to be capitalized or, if no interest is capitalized, the

Fiscal Year in which the Parity Obligations proposed to be executed are executed, will be at least equal to 125% of the Maximum Annual Debt Service; provided, that for the purpose of providing the Consultant's Report, the Independent Consultant may adjust the foregoing Adjusted Annual Net Revenues to reflect:

(i) An allowance for Gross Revenues that would have been derived from any increase in the rates, fees and charges prescribed for Water Service in effect and being charged, or rates, fees and charges for Water Service that are expected to be charged in accordance with a program of specific rates, fees, charges, rate levels or increases in overall Gross Revenue approved by a resolution of the City Council; and

(ii) An allowance for Gross Revenues from customers of the Water Utility System anticipated to be served by the facilities or improvements financed in substantial part by the Parity Obligations proposed to be executed together with any additional Parity Obligations expected to be executed prior to the Fiscal Year of determination.

Notwithstanding the foregoing, the Master Contract specifies that there shall be no limitations on the ability of the City to execute any Parity Obligation at any time to refund any outstanding Parity Obligation.

### **2008 Swap Agreement**

In connection with the execution and delivery of the 2006 Certificates, the City entered into an interest rate swap agreement in the form of an ISDA Master Agreement (Local Currency – Single Jurisdiction), the U.S. Municipal Counterparty Schedule thereto, a Credit Support Annex and a Confirmation each dated as of and entered into on September 27, 2006 (collectively, the “2006 Swap Agreement”) with Bank of America, N.A. (the “Swap Provider”). In connection with the execution and delivery of the 2008 Certificates, the City and the Swap Provider will amend and restate the 2006 Swap Agreement (as so amended and restated, the “2008 Swap Agreement”). The 2008 Swap Agreement is scheduled to expire on the Maturity Date of the 2008 Certificates; and the notional amount of the 2008 Swap Agreement is scheduled to be reduced on the same dates and in the same amounts as the principal evidenced by the 2008 Certificates is scheduled to be reduced. Pursuant to the 2008 Swap Agreement, the City will be required to make periodic payments to the Swap Provider calculated on the basis of a fixed rate of interest on an initial notional amount equal to the principal amount represented by the 2008 Certificates. In return, the Swap Provider will be required to make periodic payments to the City calculated on the basis of a variable rate of interest equal to a percentage of LIBOR on the same notional amount. The amounts payable by each party pursuant to the 2008 Swap Agreement are netted against the payments to be received by such party thereunder.

Certain of the amounts that may be payable by the City to the Swap Provider will be insured pursuant to a policy of interest rate swap insurance to be issued by Assured Guaranty (the “Swap Policy”).

The City's obligations under the 2008 Swap Agreement to make scheduled payments and certain termination payments (but only if such termination payments are insured pursuant to the Swap Policy) are Parity Obligations. No arrangements made in respect of the 2008 Swap Agreement will alter the City's obligation to make the 2008 Payments.

Both the City and the Swap Provider have the right to terminate the 2008 Swap Agreement prior to its stated termination date under certain conditions. Any such termination could result in an obligation on the part of the City or the Swap Provider to make termination payments to the other party, and the amount of such termination payments could be substantial. Any obligation on the part of the City to make such a termination payment (other than a termination payment that is insured under the terms of the Swap Policy) will not be a Parity Obligation and will be subordinate to the City's liabilities with respect to Parity Obligations.

Neither the Trustee nor the Owners will have any rights under the 2008 Swap Agreement or against the Swap Provider.

## **CERTIFICATE INSURANCE**

*The following information has been provided by Assured Guaranty Corp. It has not been verified by the Authority or the City. The following information is not complete, and reference is made to Appendix E for a specimen of the financial guaranty insurance policy (the "Policy") of Assured Guaranty Corp. ("Assured Guaranty" or the "Insurer").*

### **Certificate Insurance Policy**

Assured Guaranty has made a commitment to issue the Policy relating to the 2008 Certificates, effective as of the date of issuance of such 2008 Certificates. Under the terms of the Policy, Assured Guaranty will unconditionally and irrevocably guarantee to pay that portion of principal of and interest with respect to the 2008 Certificates that becomes Due for Payment but shall be unpaid by reason of Nonpayment (the "Insured Payments"). Insured Payments shall not include any additional amounts owing by the Issuer solely as a result of the failure by the Trustee or the Paying Agent to pay such amount when due and payable, including without limitation any such additional amounts as may be attributable to penalties or to interest accruing at a default rate, to amounts payable in respect of indemnification, or to any other additional amounts payable by the Trustee or the Paying Agent by reason of such failure. The Policy is non-cancelable for any reason, including without limitation the non-payment of premium.

"Due for Payment" means, when referring to the principal of the 2008 Certificates, the stated maturity date thereof, or the date on which such 2008 Certificates shall have been duly called for mandatory sinking fund redemption, and does not refer to any earlier date on which payment is due by reason of a call for redemption (other than by mandatory sinking fund redemption), acceleration or other advancement of maturity (unless Assured Guaranty in its sole discretion elects to make any principal payment, in whole or in part, on such earlier date) and, when referring to interest on such 2008 Certificates, means the stated dates for payment of interest.

"Nonpayment" means the failure of the Issuer to have provided sufficient funds to the Trustee or the Paying Agent for payment in full of all principal and interest Due for Payment on the 2008 Certificates. It is further understood that the term Nonpayment in respect of a 2008 Certificate also includes any amount previously distributed to the Holder (as such term is defined in the Policy) of such 2008 Certificate in respect of any Insured Payment by or on behalf of the Issuer, which amount has been recovered from such Holder pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court having competent jurisdiction that such payment constitutes an avoidable preference with respect to such Holder. Nonpayment does not

include nonpayment of principal or interest caused by the failure of the Trustee or the Paying Agent to pay such amount when due and payable.

Assured Guaranty will pay each portion of an Insured Payment that is Due for Payment and unpaid by reason of Nonpayment, on the later to occur of (i) the date such principal or interest becomes Due for Payment, or (ii) the business day next following the day on which Assured Guaranty shall have received a completed notice of Nonpayment therefor in accordance with the terms of the Policy.

Assured Guaranty shall be fully subrogated to the rights of the Holders of the Bonds to receive payments in respect of the Insured Payments to the extent of any payment by Assured Guaranty under the Policy.

The Policy is not covered by any insurance or guaranty fund established under New York, California, Connecticut or Florida insurance law.

### **The Reserve Fund Insurance Policy**

Assured Guaranty has made a commitment to issue a financial guaranty insurance policy for the reserve fund with respect to the 2008 Certificates (the “Reserve Fund Insurance Policy”), effective as of the date of issuance of such 2008 Certificates. Under the terms of the Reserve Fund Insurance, Assured Guaranty will unconditionally and irrevocably guarantee to pay that portion of the scheduled principal and interest on the 2008 Certificates that becomes due for payment but shall be unpaid by reason of nonpayment by the Issuer (the “Insured Payments”).

Assured Guaranty will pay each portion of an Insured Payment that is due for payment and unpaid by reason of nonpayment by the Issuer to the Trustee or Paying Agent, as beneficiary of the Reserve Fund Insurance Policy on behalf of the holders of the 2008 Certificates on the later to occur of (i) the date such scheduled principal or interest becomes due for payment or (ii) the business day next following the day on which Assured Guaranty receives a demand for payment therefor in accordance with the terms of the Reserve Fund Insurance Policy.

No payment shall be made under the Reserve Fund Insurance Policy in excess of \$2,082,512.74 (the “Reserve Fund Insurance Policy Limit”). Pursuant to the terms of the Reserve Fund Insurance Policy, the amount available at any particular time to be paid to the Trustee or Paying Agent shall automatically be reduced to the extent of any payment made by Assured Guaranty under the Reserve Fund Insurance Policy, provided, that, to the extent of the reimbursement of such payment to Assured Guaranty, the amount available under the Reserve Fund Insurance Policy shall be reinstated in full or in part, in an amount not to exceed the Reserve Fund Insurance Policy Limit.

The Reserve Fund Insurance Policy does not insure against nonpayment caused by the insolvency or negligence of the Trustee or Paying Agent.

The Reserve Fund Insurance Policy is not covered by any insurance or guaranty fund established under New York, California, Connecticut or Florida insurance law.

### **Assured Guaranty Corp.**

Assured Guaranty Corp. (“Assured Guaranty”) is a Maryland-domiciled insurance company regulated by the Maryland Insurance Administration and licensed to conduct financial guaranty

insurance business in all fifty states of the United States, the District of Columbia and Puerto Rico. Assured Guaranty commenced operations in 1988. Assured Guaranty is a wholly owned, indirect subsidiary of Assured Guaranty Ltd. (“AGL”), a Bermuda-based holding company whose shares are publicly traded and are listed on the New York Stock Exchange under the symbol “AGO.” AGL, through its operating subsidiaries, provides credit enhancement products to the U.S. and global public finance, structured finance and mortgage markets. Neither AGL nor any of its shareholders is obligated to pay any debts of Assured Guaranty or any claims under any insurance policy issued by Assured Guaranty.

Assured Guaranty is subject to insurance laws and regulations in Maryland and in New York (and in other jurisdictions in which it is licensed) that, among other things, (i) limit Assured Guaranty’s business to financial guaranty insurance and related lines, (ii) prescribe minimum solvency requirements, including capital and surplus requirements, (iii) limit classes and concentrations of investments, (iv) regulate the amount of both the aggregate and individual risks that may be insured, (v) limit the payment of dividends by Assured Guaranty, (vi) require the maintenance of contingency reserves, and (vii) govern changes in control and transactions among affiliates. Certain state laws to which Assured Guaranty is subject also require the approval of policy rates and forms.

Assured Guaranty’s financial strength is rated “AAA” by Standard Poor’s, a division of The McGraw-Hill Companies, Inc. (“S&P”), “AAA” by Fitch, Inc. (“Fitch”) and “Aaa” by Moody’s Investors Service, Inc. (“Moody’s”). Each rating of Assured Guaranty should be evaluated independently. An explanation of the significance of the above ratings may be obtained from the applicable rating agency. The above ratings are not recommendations to buy, sell or hold any security, and such ratings are subject to revision or withdrawal at any time by the rating agencies. Any downward revision or withdrawal of any of the above ratings may have an adverse effect on the market price of any security guaranteed by Assured Guaranty. Assured Guaranty does not guaranty the market price of the securities it guarantees, nor does it guaranty that the ratings on such securities will not be revised or withdrawn.

***Capitalization of Assured Guaranty Corp.*** As of March 31, 2008, Assured Guaranty had total admitted assets of \$1,518,398,730 (unaudited), total liabilities of \$1,138,285,708 (unaudited), total surplus of \$380,113,022 (unaudited) and total statutory capital (surplus plus contingency reserves) of \$1,001,533,924 (unaudited) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities. As of December 31, 2007, Assured Guaranty had total admitted assets of \$1,361,538,502 (unaudited), total liabilities of \$961,967,238 (unaudited), total surplus of \$399,571,264 (unaudited) and total statutory capital (surplus plus contingency reserves) of \$982,045,695 (unaudited) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities. As of December 31, 2006, Assured Guaranty had total admitted assets of \$1,248,270,663 (audited), total liabilities of \$962,316,898 (audited), total surplus of \$285,953,765 (audited) and total statutory capital (surplus plus contingency reserves) of \$916,827,559 (audited) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities. The Maryland Insurance Administration recognizes only statutory accounting practices for determining and reporting the financial condition and results of operations of an insurance company, for determining its solvency under the Maryland Insurance Code, and for determining whether its financial condition warrants the payment of a dividend to its stockholders. No consideration is given by the Maryland Insurance Administration to financial statements prepared in accordance with

accounting principles generally accepted in the United States (“GAAP”) in making such determinations.

***Incorporation of Certain Documents by Reference.*** The portions of the following documents relating to Assured Guaranty are hereby incorporated by reference into this Official Statement and shall be deemed to be a part hereof:

- The Annual Report on Form 10-K of AGL for the fiscal year ended December 31, 2007 (which was filed by AGL with the Securities and Exchange Commission (the “SEC”) on February 29, 2008);
- The Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2008 (which was filed by AGL with the SEC on May 9, 2008); and
- The Current Reports on Form 8-K filed by AGL with the SEC, as they relate to Assured Guaranty.

All consolidated financial statements of Assured Guaranty and all other information relating to Assured Guaranty included in documents filed by AGL with the SEC pursuant to Section 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934, as amended, subsequent to the date of this Official Statement and prior to the termination of the offering of the 2008 Certificates shall be deemed to be incorporated by reference into this Official Statement and to be a part hereof from the respective dates of filing such consolidated financial statements.

Any statement contained in a document incorporated herein by reference or contained herein under the heading “CERTIFICATE INSURANCE — Assured Guaranty Corp.” shall be modified or superseded for purposes of this Official Statement to the extent that a statement contained herein or in any subsequently filed document which is incorporated by reference herein also modifies or supersedes such statement. Any statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Official Statement.

Copies of the consolidated financial statements of Assured Guaranty incorporated by reference herein and of the statutory financial statements filed by Assured Guaranty with the Maryland Insurance Administration are available upon request by contacting Assured Guaranty at 1325 Avenue of the Americas, New York, New York 10019 or by calling Assured Guaranty at (212) 974-0100. In addition, the information regarding Assured Guaranty that is incorporated by reference in this Official Statement that has been filed by AGL with the SEC is available to the public over the Internet at the SEC’s web site at <http://www.sec.gov> and at AGL’s web site at <http://www.assuredguaranty.com>, from the SEC’s Public Reference Room at 450 Fifth Street, N.W., Room 1024, Washington, D.C. 20549, and at the office of the New York Stock Exchange at 20 Broad Street, New York, New York 10005.

Assured Guaranty makes no representation regarding the 2008 Certificates or the advisability of investing in the 2008 Certificates. In addition, Assured Guaranty has not independently verified, makes no representation regarding, and does not accept any responsibility for the accuracy or completeness of this Official Statement or any information or disclosure contained herein, or omitted herefrom, other than with respect to the accuracy of the information regarding Assured Guaranty supplied by Assured Guaranty and presented under the heading “CERTIFICATE INSURANCE.”

## LIQUIDITY FACILITY

*The following information has been provided by Bank of America, N.A. It has not been verified by the Authority or the City, and neither the Authority nor the City guarantees its accuracy or completeness.*

### **Initial Liquidity Facility**

**General.** The purchase price of 2008 Certificates tendered or deemed tendered for purchase and not remarketed is payable from amounts made available under a Standby Certificate Purchase Agreement, dated as of May 1, 2008 (the “Liquidity Facility”), by and among the Authority, the District and the Liquidity Facility Provider. Certain provisions of the Liquidity Facility are summarized below, but such summary is qualified in its entirety by reference to the Liquidity Facility.

Subject to the terms and conditions of the Liquidity Facility, the Liquidity Facility Provider is to provide funds for the payment of the purchase price on each purchase of 2008 Certificates up to \$47,625,000 in principal amount (the “Available Principal Commitment”) and \$548,014 (an amount equal to 35 days’ interest on the Available Principal Commitment at an assumed rate of 12% computed on the basis of a 365-day year for the actual number of days elapsed) accrued interest on 2008 Certificates subject to the Weekly Rate tendered or deemed tendered for purchase in the event that remarketing proceeds are not sufficient to pay the Purchase Price (as defined in the Liquidity Facility) of such 2008 Certificates. *The Liquidity Facility will not provide for the payment of principal of and interest on any 2008 Certificates other than with respect to the purchase price of the 2008 Certificates tendered or deemed tendered and not remarketed.*

The Liquidity Facility will expire on its Stated Expiration Date, which will be May 29, 2011 unless otherwise extended or terminated earlier pursuant to its terms. **Under certain circumstances as described below, the obligations of the Liquidity Facility Provider to purchase 2008 Certificates will be automatically suspended or terminated without prior notice or demand; and the Trustee will be unable to require the purchase of 2008 Certificates under the Liquidity Facility.**

**Events of Default.** The following events are defined as “Events of Default” under the Liquidity Facility:

(a) any principal or interest due on the 2008 Certificates is not paid by the Authority when due and such principal or interest is not paid by the Certificate Insurer when, as and in the amounts required to be paid pursuant to the terms of the Certificate Insurance Policy; or

(b) a Certificate Insurer Event of Insolvency shall have occurred and the rating of the City’s Water Enterprise Fund by any two of the three rating agencies is withdrawn or drops below (i) in the case of Fitch, a rating of “AAA” (or its equivalent); (ii) in the case of Moody’s, a rating of “Aaa” (or its equivalent); and (iii) in the case of S&P, a rating of “AAA” (or its equivalent) (such event is referred to herein as a “City Rating Event”); or

(c) (i) any material provision of the Certificate Insurance Policy at any time for any reason ceases to be valid and binding on the Certificate Insurer in accordance with the terms of the Certificate Insurance Policy or is declared, announced or ruled to be null and void by a court or other governmental agency of appropriate jurisdiction; or (ii) a senior authorized officer of the Certificate Insurer denies that it has any or further liability or obligation under the Certificate Insurance Policy and in either case, a City Rating Event has occurred and is continuing; or

(d) the Certificate Insurer shall default in any payment or payments of amounts payable by it under any insurance policy or policies (other than the Certificate Insurance Policy) when due and such default shall continue for a period of thirty (30) days; (it being understood by the Liquidity Facility Provider that default, for the purposes of this paragraph, shall not mean a situation whereby the Certificate Insurer contests in good faith its liability under any such policy or policies in light of the claim or claims made thereunder), and in any case a City Rating Event has occurred and is continuing; or

(e) any material representation or warranty made by the Authority or the City under or in connection with the Liquidity Facility shall prove to be untrue in any material respect on the date as of which it was made; or

(f) any Other Event of Insolvency shall have occurred; or

(g) nonpayment of any fees due to the Liquidity Facility Provider under the Liquidity Facility, if such failure to pay when due shall continue for ten (10) Business Days after the City, the Authority and the Certificate Insurer has received written notice thereof from the Liquidity Facility Provider; or

(h) the breach by the Authority or the City of certain terms or provisions of provisions of the Liquidity; or

(i) the Authority shall default in the performance or observance of any other material covenant or agreement contained (or incorporated by reference) in the Liquidity Facility such default shall continue unremedied for a period of thirty (30) days after the Authority has received written notice thereof from the Liquidity Facility Provider; or

(j) the City shall default in the performance or observance of any other material covenant or agreement contained (or incorporated by reference) in the Liquidity Facility and such default shall continue unremedied for a period of thirty (30) days after the City has received written notice thereof from the Liquidity Facility Provider; or

(k) the Trust Agreement or the 2008 Contract shall terminate or cease to be of full force and effect, other than as a result of any prepayment in full of the 2008 Certificates or provision for such prepayment in full in accordance with the Trust Agreement and discharge of all payment obligations under the 2008 Contract; or

(l) the occurrence of any “event of default” as defined in the Trust Agreement which is not otherwise described in this list of “Events of Default,” other than the failure of the Liquidity Facility Provider to provide funds for the purchase of 2008 Certificates when required by the terms and conditions of the Liquidity Facility; or

(m) the Trustee ceases to have an effective security interest in the Trust Estate prior to any lien, pledge, assignment or security interest of any creditors of the City or the Authority; or

(n) for an uninterrupted period of ninety (90) days there is not in effect both of the following in respect of the 2008 Certificates: (i) in the case of Moody’s, a rating of “Baa3” (or its equivalent) or higher; and (ii) in the case of S&P, a rating of “BBB-” (or its equivalent) or higher; or

(o) the City shall default in any payment of principal of or premium, if any, or interest on any of its Debts in excess of \$5,000,000 and such default shall continue beyond the expiration of the applicable grace period, if any, or the City shall fail to perform any other agreement, term or condition contained in any agreement under which any obligation for the payment of \$5,000,000 or more is created or secured, which shall permit or result in the declaring due and payable of such obligation prior to the date on which it would otherwise have become due and payable; or

(p) a final judgment or order for the payment of money for an uninsured claim in excess of \$5,000,000 shall have been rendered against the City and such judgment or order shall not have been satisfied, stayed or bonded pending appeal within a period of thirty (30) days from the date on which it was first so rendered; or

(q) any amendment, replacement or other modification of the Certificate Insurance Policy or substitution of the Certificate Insurer occurs without the prior written consent of the Liquidity Facility Provider.

***Remedies.*** In the case of an Event of Default described in paragraphs (a), (b) or (c)(i) above (each, a “Termination Event”), the Available Commitment and **the obligation of the Liquidity Facility Provider to purchase 2008 Certificates shall immediately terminate without notice or demand, and thereafter the Liquidity Facility Provider shall be under no obligation to purchase 2008 Certificates.**

Upon the occurrence and during the continuance of an Event of Default described in clauses (g) or (n) hereof, the Liquidity Facility Provider may terminate the Available Commitment by giving written notice (a “Notice of Termination”) to the City, the Trustee, the Remarketing Agent and the Certificate Insurer, specifying the date on which at 3:00 p.m. California time the Available Commitment shall terminate (the “Termination Date”), which shall be not less than thirty (30) days from the date of receipt of such notice by the Trustee, and after the Termination Date the Liquidity Facility Provider shall be under no further obligation to purchase 2008 Certificates under the Liquidity Facility other than 2008 Certificates which are the subject of the Notice of Liquidity Facility Provider Purchase delivered by the Trustee hereof and received by the Liquidity Facility Provider on or prior to the Termination Date.

In the case of (i) the occurrence of an Event of Default of the type described in clause (ii) of paragraph (c) above or (ii) the commencement of an involuntary case or other involuntary proceeding seeking an order for relief, rehabilitation, reorganization, conservation, liquidation or dissolution with respect to the Certificate Insurer or its debts or claims under any bankruptcy, insolvency or other similar law, or seeking the appointment of a trustee, receiver, liquidator, custodian, assignee, sequestrator or other similar official for the Certificate Insurer or any substantial part of its property (an “Involuntary Insolvency Event”) together with the occurrence and continuance of a City Rating Event, **the Liquidity Facility Provider’s obligation to purchase 2008 Certificates under the Liquidity Facility shall immediately be suspended without further action on the part of any Person.** The obligation of the Liquidity Facility Provider to purchase 2008 Certificates shall be suspended until either (x) the Liquidity Facility Provider delivers a written notice to the Trustee rescinding the automatic suspension of its obligation to purchase 2008 Certificates under the Liquidity Facility (a “Rescission Notice”) or, (y) (1) in the case of a suspension event of the type described in clause (ii) of paragraph (c) above, a final non-appealable order of a court having jurisdiction in the premises shall be entered declaring that all material contested provisions of the Certificate Insurance Policy are upheld in their entirety or (2) in the case of an Involuntary Insolvency Event, a court having jurisdiction in the premises shall dismiss or stay such involuntary case, proceeding or appointment within 60 days. In the event a final non-appealable order is entered declaring any material provision of the Certificate Insurance Policy to be null and void, or declaring that the Certificate Insurer does not have any further liability or obligation under the Certificate Insurance Policy or in the event an Involuntary Insolvency Event is not dismissed or stayed within 60 days by a court having jurisdiction in the premises, then, so long as a City Rating Event is continuing, the obligation of the Liquidity Facility Provider to purchase 2008 Certificates shall immediately terminate without any further action by any Person. In the event a final non-appealable order is entered declaring that all material contested provisions of the Certificate Insurance Policy are upheld in their entirety or in the event a court having jurisdiction in the premises shall dismiss or stay any Involuntary Insolvency Event within 60 days, the obligation of the Liquidity Facility Provider to purchase 2008 Certificates shall be automatically reinstated and the terms of the Liquidity Facility will continue in full force and effect (unless the Liquidity Facility Provider Purchase Period shall have otherwise expired or terminated) as if there had been no such suspension. Notwithstanding the foregoing, if the Liquidity Facility Provider has not delivered a Rescission Notice to the Trustee and if, upon the earlier of (a) the last day of the Liquidity Facility Provider Purchase Period or (b) (i) in the case of the occurrence of an Event of Default of the type described in clause (ii) of paragraph (c) above, the date which is three years after the effective date of suspension of the obligation of the Liquidity Facility Provider to purchase 2008 Certificates, litigation is still pending and a judgment regarding the validity of the Certificate Insurance Policy has not been obtained or (ii) in the case of the occurrence of an Involuntary Insolvency Event and the continuance of a City Rating Event, the date which is 60 days after the commencement of the involuntary case, proceeding or appointment, such involuntary case, proceeding or appointment has not been dismissed or stayed, then the Available Commitment and the obligation of the Liquidity Facility Provider to purchase 2008 Certificates shall at such time terminate without notice or demand and thereafter the Liquidity Facility Provider shall be under no further obligation to purchase 2008 Certificates.

In addition to the rights and remedies described above, in the case of any Event of Default, upon the election of the Liquidity Facility Provider: (i) all amounts payable under the Liquidity Facility (other than payments of principal and interest on Liquidity Facility Provider Certificates) shall upon notice to the City become immediately due and payable without presentment, demand, protest or further notice of any kind and (ii) the Liquidity Facility Provider shall have all the rights and remedies available to it under the Liquidity Facility, the Related Documents or otherwise

pursuant to law or equity other than acceleration of the 2008 Certificates or termination of its obligation to purchase 2008 Certificates.

### **Bank of America, N.A.**

Bank of America, N.A. (the “Bank”) is a national banking association organized under the laws of the United States, with its principal executive offices located in Charlotte, North Carolina. The Bank is a wholly-owned indirect subsidiary of Bank of America Corporation (the “Corporation”) and is engaged in a general consumer banking, commercial banking and trust business, offering a wide range of commercial, corporate, international, financial market, retail and fiduciary banking services. As of December 31, 2007, the Bank had consolidated assets of \$1,312,794,218,000, consolidated deposits of \$793,571,969,000 and stockholder’s equity of \$108,480,218,000 based on regulatory accounting principles.

The Corporation is a bank holding company and a financial holding company, with its principal executive offices located in Charlotte, North Carolina. Additional information regarding the Corporation is set forth in its Annual Report on Form 10-K for the fiscal year ended December 31, 2006, together with any subsequent documents it filed with the Securities and Exchange Commission (the “SEC”) pursuant to the Securities Exchange Act of 1934, as amended (the “Exchange Act”).

Additional information regarding the foregoing is available from the filings made by the Corporation with the SEC, which filings can be inspected and copied at the public reference facilities maintained by the SEC at 100 F Street, N.E., Washington, D.C. 20549, United States, at prescribed rates. In addition, the SEC maintains a website at <http://www.sec.gov>, which contains reports, proxy statements and other information regarding registrants that file such information electronically with the SEC.

The information concerning the Corporation and the Bank contained herein is furnished solely to provide limited introductory information and does not purport to be comprehensive. Such information is qualified in its entirety by the detailed information appearing in the documents and financial statements referenced herein.

The Liquidity Facility has been issued by the Bank. Moody’s Investors Service, Inc. (“Moody’s”) currently rates the Bank’s long-term debt as “Aaa” and short-term debt as “P-1.” The outlook is stable. Standard & Poor’s rates the Bank’s long-term debt as “AA+” and its short-term debt as “A-1+.” The outlook is stable. Fitch Ratings, Inc. (“Fitch”) rates long-term debt of the Bank as “AA” and short-term debt as “F1+.” The outlook is negative. Further information with respect to such ratings may be obtained from Moody’s, Standard & Poor’s and Fitch, respectively. No assurances can be given that the current ratings of the Bank’s instruments will be maintained.

The Bank will provide copies of the most recent Bank of America Corporation Annual Report on Form 10-K, any subsequent reports on Form 10-Q, and any required reports on Form 8-K (in each case as filed with the SEC pursuant to the Exchange Act), and the publicly available portions of the most recent quarterly Call Report of the Bank delivered to the Comptroller of the Currency, without charge, to each person to whom this document is delivered, on the written request of such person. Written requests should be directed to: Bank of America Corporate Communications, 100 North Tryon Street, 18th Floor, Charlotte, North Carolina 28255, Attention: Corporate Communications

PAYMENTS OF THE PURCHASE PRICE OF THE 2008 CERTIFICATES WILL BE MADE FROM DRAWINGS UNDER THE LIQUIDITY FACILITY IF REMARKETING PROCEEDS ARE NOT AVAILABLE. ALTHOUGH THE LIQUIDITY FACILITY IS A BINDING OBLIGATION OF THE BANK, THE 2008 CERTIFICATES ARE NOT DEPOSITS OR OBLIGATIONS OF THE CORPORATION OR ANY OF ITS AFFILIATED BANKS AND ARE NOT GUARANTEED BY ANY OF THESE ENTITIES. THE 2008 CERTIFICATES ARE NOT INSURED BY THE FEDERAL DEPOSIT INSURANCE CORPORATION OR ANY OTHER GOVERNMENTAL AGENCY AND ARE SUBJECT TO CERTAIN INVESTMENT RISKS, INCLUDING POSSIBLE LOSS OF THE PRINCIPAL AMOUNT INVESTED.

The delivery hereof shall not create any implication that there has been no change in the affairs of the Corporation or the Bank since the date hereof, or that the information contained or referred to herein.

## REMARKETING

***Remarketing Agreement.*** The Authority has entered into a Remarketing and Interest Services Agreement, dated as of May 1, 2008 (the “Remarketing Agreement”), with Banc of America Securities LLC as the Remarketing Agent. Under the Remarketing Agreement and subject to the limitations set forth therein, the Remarketing Agent has agreed to use its best efforts to offer for sale all 2008 Certificates tendered in accordance with the provisions of the Indenture.

The Remarketing Agent’s responsibilities include determining the interest rate from time to time and remarketing 2008 Certificates that are tendered by the owners thereof either pursuant to an optional or mandatory tender (subject, in each case, to the terms of the Remarketing Agreement), all as further described in this Official Statement. The Remarketing Agent is appointed by the Authority and is paid by the Authority for its services. As a result, the interests of the Remarketing Agent may differ from those of existing owners and potential purchasers of 2008 Certificates.

***The Remarketing Agent Routinely Purchases 2008 Certificates for its Own Account.*** The Remarketing Agent acts as remarketing agent for a variety of variable rate demand obligations and, in its sole discretion, routinely purchases such obligations for its own account. The Remarketing Agent is permitted, but not obligated, to purchase tendered 2008 Certificates for its own account and, in its sole discretion, routinely acquires such tendered 2008 Certificates in order to achieve a successful remarketing of the 2008 Certificates (i.e., because there otherwise are not enough buyers to purchase the 2008 Certificates) or for other reasons. However, the Remarketing Agent is not obligated to purchase 2008 Certificates, and may cease doing so at any time without notice. The Remarketing Agent may also make a market in the 2008 Certificates by routinely purchasing and selling 2008 Certificates other than in connection with an optional or mandatory tender and remarketing. Such purchases and sales may be at or below par. However, the Remarketing Agent is not required to make a market in the 2008 Certificates. The Remarketing Agent may also sell any 2008 Certificates it has purchased to one or more affiliated investment vehicles for collective ownership or enter into derivative arrangements with affiliates or others in order to reduce its exposure to the 2008 Certificates. The purchase of 2008 Certificates by the Remarketing Agent may cause the interest rate to be lower than it would be if the Remarketing Agent did not purchase 2008 Certificates and may create the appearance that there is greater third party demand for the 2008 Certificates in the market than is actually the case. The practices described above also may result in fewer 2008 Certificates being tendered in a remarketing.

***2008 Certificates May be Offered at Different Prices on Any Date Including a Rate Determination Date.*** Pursuant to the Remarketing Agreement, the Remarketing Agent is required to determine the applicable rate of interest that, in its judgment, is the lowest rate that would permit the sale of the 2008 Certificates bearing interest at the applicable interest rate at par plus accrued interest, if any, on and as of the applicable Rate Determination Date. The interest rate will reflect, among other factors, the level of market demand for the 2008 Certificates (including whether the Remarketing Agent is willing to purchase 2008 Certificates for its own account). The purchase of the 2008 Certificates by the Remarketing Agent may cause the interest rate to be lower than it would be if the Remarketing Agent did not purchase 2008 Certificates. There may or may not be 2008 Certificates tendered and remarketed on a rate determination date, the Remarketing Agent may or may not be able to remarket any 2008 Certificates tendered for purchase on such date at par and the Remarketing Agent may sell 2008 Certificates at varying prices to different investors on such date or any other date. The Remarketing Agent is not obligated to advise purchasers in a remarketing if it does not have third party buyers for all of the 2008 Certificates at the remarketing price. The Remarketing Agent, in its sole discretion, may offer 2008 Certificates on any date, including the Rate Determination Date, at a discount to par to some investors.

***The Ability to Sell the 2008 Certificates other than Through Tender Process May Be Limited.*** The Remarketing Agent may buy and sell 2008 Certificates other than through the tender process. However, it is not obligated to do so and may cease doing so at any time without notice and may require owners that wish to tender their 2008 Certificates to do so through the Tender Agent with appropriate notice. Thus, investors who purchase the 2008 Certificates, whether in a remarketing or otherwise, should not assume that they will be able to sell their 2008 Certificates other than by tendering the 2008 Certificates in accordance with the tender process.

***Under Certain Circumstances, the Remarketing Agent May Be Removed, Resign or Cease Remarketing the 2008 Certificates, Without a Successor Being Named.*** Under certain circumstances the Remarketing Agent may be removed or have the ability to resign or cease its remarketing efforts, without a successor having been named, subject to the terms of the Remarketing Agreement. In the event there is no Remarketing Agent, the Trustee is required to apply to a court of competent jurisdiction for appointment of a successor Remarketing Agent.

## **THE WATER UTILITY SYSTEM**

### **History of the Water Utility System**

The origin of the City's municipal water system dates back to 1876 when a privately-owned utility, later known as the Modesto Water Company, was established to provide water service to the village of Modesto. In 1895, the City purchased the Modesto Water Company, and in subsequent years it purchased other local water systems that have been incorporated in the present Water Utility System.

In April 1992, the City entered into the original Treatment and Delivery Agreement with MID and the Del Este Water Company ("Del Este"), providing for a supply of treated water for the City and Del Este from the Water Treatment Plant, which was constructed and is owned and operated by MID. See "— Sources of Water" below. In July 1995, the City purchased substantially all of the assets and assumed substantially all of the liabilities of Del Este, the last private water company within City limits. The acquisition included Del Este's other water service areas including the communities of Salida, Waterford, Empire, Hickman, Grayson, and parts of Turlock, Ceres and Del

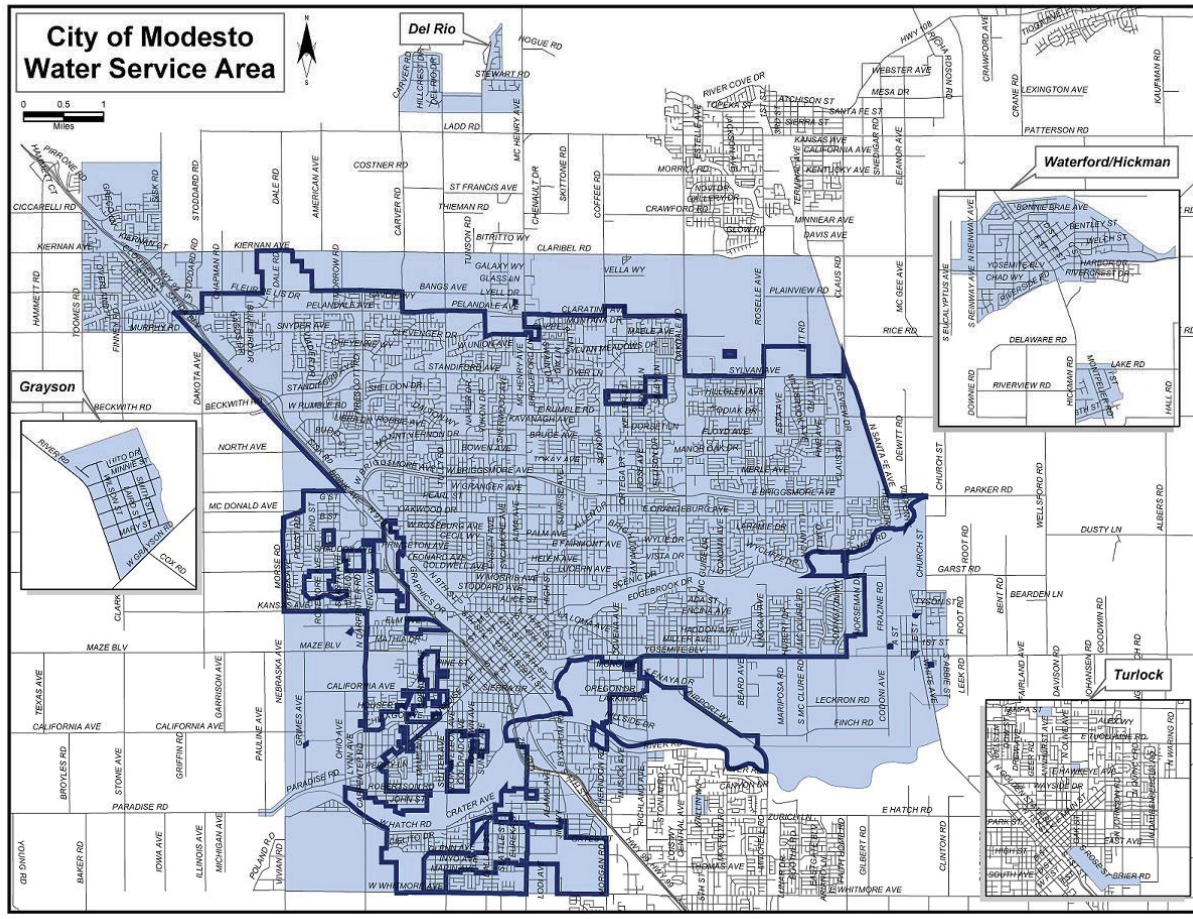
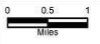
Rio Estates. As a consequence of the varying operating conditions among these communities, the City initially operated the Water Utility System in three separate zones. However, the three zones were essentially merged into a single zone for rate purposes when the City Council adopted a new rate structure that went into effect on January 1, 2005.

The original Treatment and Delivery Agreement provided the terms and conditions under which the City agreed to provide payments for, and MID agreed to finance, construct, own and operate, the Water Treatment Plant. Pursuant to the terms of the original Treatment and Delivery Agreement, the City was entitled to receive 30 million gallons per day of treated water from the Phase One Water Treatment Plant. The original Treatment and Delivery Agreement was amended and restated in 2005 to provide for the funding and construction of Phase Two of the Water Treatment Plant. Upon completion of Phase Two, the City will be entitled to receive 60 million gallons per day of treated water for use within the portion of the City's service area that is within MID's authorized service area. See "— Treatment and Delivery Agreement" below.

In general terms, the City's total water service area consists of one large contiguous area and several outlying, non-contiguous service areas. The contiguous water area includes all of the property currently within the corporate boundaries of the City as well as the property located within its sphere of influence and properties located within the communities of Ceres, Empire and Salida. There are five outlying non-contiguous water service areas. They are the communities of Del Rio, Grayson, Hickman and Waterford, as well as portions of the City of Turlock.

A map showing the City's water service area appears on page 38.

# City of Modesto Water Service Area



**Del Rio**

**Waterford/Hickman**

**Grayson**

**Turlock**

## Existing Facilities

The principal facilities of the existing Water Utility System consist of 125 domestic wells (111 of which are currently active), over 900 miles of mains, seven storage tanks, the MID's Water Treatment Plant and a terminal storage area serving surface water and/or groundwater to its customers through nearly 77,000 water connections.

MID surface water is treated at the Water Treatment Plant and conveyed to the City via transmission mains for direct use in the contiguous portion of the City's water service area. The City's facilities are designed to deliver both surface water and groundwater. The Water Treatment Plant does not provide surface water to the outlying portions of the City's water service areas including those portions that are outside of MID's authorized service boundaries.

Groundwater is pumped directly from the wells into the distribution system, which consists of 900 miles of water mains and pipelines. Most of the larger water mains are 10- and 12-inch diameter pipelines which have been installed by the City. The installation of smaller pipelines in subdivisions is typically the responsibility of the subdivider. Seven ground level tanks and booster pump stations provide storage capacities ranging from 500,000 to 1,300,000 gallons each.

The following table sets forth statistical information relating to the Water Utility System during the periods shown.

### WATER UTILITY SYSTEM STATISTICS Calendar Years

	2003	2004	2005	2006	2007
Number of Service Accounts	72,907	73,916	74,779	76,227	76,661
Total Water Production (MG) <sup>(1)</sup>	27,000	26,580	25,720	25,605	25,857
Capacity (MGD) <sup>(2)</sup>	166	166	166	166	166
Peak Daily Distribution (MGD)	133.6	124.9	129.8	131.4	115.4
Average Daily Distribution (MGD)	73.7	72.4	70.4	70.2	70.9

<sup>(1)</sup> "MG" means million gallons.

<sup>(2)</sup> "MGD" means million gallons per day. The actual capacity of the Water Utility System during each of the years shown varied slightly from the 166 MGD figure depending upon the number and capacity of the wells going in and out of service in each of said years.

Source: City of Modesto.

During the five year period covered by the table the City's population grew by nearly 3% while the aggregate volume of water sold declined by approximately 4%. Thus, on a per capita basis, consumption of water in the City's service area has been reduced over the course of this period. This reduction has been the result of many variables including water conservation efforts, weather, system repairs, more efficient water consumption by customers and the availability of alternative water sources (onsite private wells).

## Sources of Water

The City's primary sources of water supply are surface water provided by MID under the Treatment and Delivery Agreement (described below) and its local groundwater sources. During the 1990's, MID, the City, and Del Este partnered to develop a new municipal water supply. This was implemented by the original Treatment and Delivery Agreement, under which the 30 MGD Water

Treatment Plant and delivery system came on line in January 1995. The Water Treatment Plant serves as the baseline supply, and seasonal demands are served by the groundwater wells. In general the Water Treatment Plant currently supplies approximately 60% of the City's water requirement during the winter and approximately 35% thereof during the summer season. Groundwater supplies the remainder.

MID issued the Notice to Proceed on July 16, 2007 to Western Summit Constructors, Inc. for the construction of the Modesto Regional Water Treatment Project – Phase 2 expansion. This project will bring the nominal plant capacity up to 60 million gallons per day (60 MGD) with a peak capacity of 72 MGD. The original contract amount was \$57,333,902 and contract change orders have totaled \$47,813.00 to date. Currently the project is 20% complete and the completion date is October 23, 2009. Performance testing will follow that date and the plant is expected to be fully operational in early 2010.

The following table sets forth the total water production for the Water Utility System during the last five calendar years.

**WATER UTILITY SYSTEM  
Service Area Total Production (Billion Gallons)**

<i>Year Ending December 31</i>	<i>Groundwater</i>	<i>Surface Water</i>	<i>Total</i>
2003	15.49	11.51	27.00
2004	15.15	11.43	26.58
2005	15.13	10.59	25.72
2006	14.74	10.92	25.66
2007	13.94	11.92	25.86

Source: City of Modesto.

Outside of the City corporate limits there are no regulations controlling the number of water wells that are drilled or the quantity of water pumped from such wells. Prior to the availability of surface water from the Water Treatment Plant, the groundwater withdrawal had been increasing and water levels had been declining since the early 1950's. As a result thereof, the groundwater resources of the Water Utility System were subject to long-term overdraft, i.e., the depletion of the water table was greater than the replenishment, of an average of 3,000 acre-feet per year. With the introduction of surface water from the Water Treatment Plant, this long-term overdraft was halted, and the City's dependency upon groundwater was reduced. The City expects that the expansion of the Water Treatment Plant and the installation of the various capital projects associated therewith, including the 2006 Project, will further reduce its reliance on groundwater supplies.

**Treatment and Delivery Agreement**

In April 1992, MID entered into the original Treatment and Delivery Agreement with the City and Del Este. Pursuant to the Treatment and Delivery Agreement, MID agreed to finance, construct, own and operate the Water Treatment Plant and certain related facilities, and the City agreed to pay the costs of acquisition, construction and operation of the Water Treatment Plant. Pursuant to the Treatment and Delivery Agreement, the City was initially allocated a 70% share of

the Water Treatment Plant, and was likewise responsible for 70% of its costs; Del Este was allocated a 30% share and was likewise responsible for 30% of its cost.

The Modesto Irrigation District Financing Authority (“MIDFA”) issued its Series 1992A Water Notes in the aggregate principal amount of \$39,990,000 to provide construction financing for Del Este’s 30% of the estimated acquisition and construction costs of the Water Treatment Plant. MIDFA also issued its Series 1992A Water Bonds and Series 1992B Water Bonds in the aggregate principal amount of \$77,385,000 in order to finance the City’s 70% share of the estimated acquisition and construction costs of the Water Treatment Plant. In 1995, MIDFA issued its Series 1995C Water Bonds in an aggregate principal amount of \$24,235,000 to repay the Series 1992A Water Notes; and in 1998, MIDFA issued its Series 1998D Water Bonds in an aggregate principal amount of \$94,715,000 to defease all of the outstanding Series 1992B Water Bonds and Series 1995C Water Bonds. (MIDFA’s Series 1998D Water Bonds are referred to as the “Domestic Water Bonds.”) On June 26, 2007, MIDFA issued the MIDFA 2007 Bonds in order to provide financing for the Water Treatment Plant Expansion described above. The ultimate source of funds expected to be used to pay debt service on the MIDFA 2007 Bonds consists of payments to be made by the City to MID pursuant to the Treatment and Delivery Agreement. See “THE WATER UTILITY SYSTEM — Treatment and Delivery Agreement.”

In July 1995, the City purchased substantially all of the assets and liabilities of Del Este and in accordance with the provisions of the original Treatment and Delivery Agreement assumed all interests, rights and obligations of Del Este under the original Treatment and Delivery Agreement. Accordingly, Del Este had no further obligation to make payments under the Treatment and Delivery Agreement or otherwise with respect to the Domestic Water Bonds.

Construction of the Water Treatment Plant began in October 1992, and the Water Treatment Plant was placed into operation in May 1995. It is located directly south of the Modesto Reservoir on an approximately 30-acre site, about 15 miles east of the City. Treated water is pumped from a five million gallon treated water storage reservoir through approximately 14 miles of transmission pipeline to two five million gallon terminal-storage reservoirs. The water is then distributed to distribution mains in the City water system.

Raw water delivered for treatment under the original Treatment and Delivery Agreement was provided under MID’s pre-1914 water rights, which are not subject to the permitting authority of the State Water Board. The rights available to MID to treat and deliver water to the City through the Water Treatment Plant consist of (i) various water rights owned by MID, including the pre-1914 water right and (ii) water available to it under a license held by MID and Turlock Irrigation District (License 11058) which authorizes the two districts to store up to 1,046,800 acre-feet of water in New Don Pedro Reservoir between November 1 and the succeeding July 31 for irrigation and recreational use. MID petitioned for and received an order from the State Water Resources Control Board (WR Order 2005-0022-DWR) which amended License 11058 and authorized a long-term transfer of up to 67,200 acre-feet of water per year to the City and which added municipal and industrial uses to the uses of water permitted under the transfer. This long-term transfer is effective through December 31, 2054. During the period of the long-term transfer, MID is required to comply with all of the terms and conditions required by the Federal Energy Regulatory Commission for the New Don Pedro Project. In addition, pursuant to California Water Code Sections 100 and 275 as well as the common law public trust doctrine, all rights and privileges under the long-term transfer order, including method of diversion, method of use and quantity of water diverted, are subject to the continuing authority of the State Water Board in accordance with law and in the interest of the public welfare to

protect public trust uses and to prevent waste, unreasonable use, unreasonable method of use or unreasonable method of diversion.

The original Treatment and Delivery Agreement provided that the City would receive 30 million gallons per day of treated water. The terms of the original Treatment and Delivery Agreement were subsequently amended and restated to provide for an expansion of the Water Treatment Plant upon the completion of which the City will be entitled to receive 60 million gallons per day of treated water on an average annual basis.

In accordance with the Treatment and Delivery Agreement, MID owns, operates, and maintains the Water Treatment Plant for the purposes of treatment and delivery of water to the City. MID may not assign its maintenance and operation responsibility for the Water Treatment Plant without the consent of the City. The City is granted a permanent beneficial interest in the Water Treatment Plant output, which may not be transferred or assigned without the consent of MID.

The City has agreed to pay all costs and expenses of all phases of the Water Treatment Plant, including (i) payments of Debt Service in connection with the financing of the Water Treatment Plant (a Parity Obligation), (ii) raw water charges for raw water furnished to the Water Treatment Plant by MID, (iii) payments of operation, maintenance, repair, replacement and modification costs attributable to the operation of the Water Treatment Plant, (iv) costs of administrative services of MID attributable to the operation of the Water Treatment Plant and the administration of the Treatment and Delivery Agreement, (v) costs of insurance required to be maintained by MID pursuant to the Treatment and Delivery Agreement (as described below), (vi) cost of electric energy provided to the Water Treatment Plant by MID, and (vii) other payments or costs (and deductions from payments or costs from the reserve and contingency fund and the certain reserve funds relating to the Domestic Water Bonds) and other amounts as specified by the Treatment and Delivery Agreement.

Some of the key provisions of the Treatment and Delivery Agreement, as amended and restated, are:

The City will continue to receive raw water at the same unit cost as MID's agricultural users.

The City will reimburse MID for all capital and operating costs associated with the treatment of the water.

Reductions in water deliveries required as a result of a drought will be borne proportionately by the City and MID's agricultural customers.

MID's commitments to its agricultural customers and to the City must be met before MID may transfer any water for delivery outside of its boundaries.

The Policy Committee, which advises the Board of Directors of MID and City Council of the City on matters related to the project, consists of two members of the City Council and two members of the MID Board.

***Delivery of Treated Water.*** Under the terms of the Treatment and Delivery Agreement, MID is generally required to make available to the City 33,602.1 acre-feet of treated water per year, or

30 million gallons per day. Upon completion of the expansion of the Water Treatment Plant those amounts will be increased to 67,204.2 acre-feet per year and 60 million gallons per day. However, in a drought situation, MID may reduce its deliveries of water to the City, but only if and to the extent that MID reduces its deliveries to its own agricultural customers proportionally. Moreover, MID's commitments to the City and to its own agricultural customers must be met before any water is transferred for delivery outside of MID's boundaries (other than transfers to and from MID and Turlock Irrigation District that are made in the ordinary course of operations). The City may exchange groundwater for use by MID's irrigation system for treated water in the event of a reduced allocation. The City will bear all costs, including the costs of additional capital facilities, if any are necessary, associated with delivering the groundwater supply to MID's irrigation system. MID may not sell any treated water from the Water Treatment Plant without first offering such water to the City. Treated water delivered by MID to the City must be utilized by the City within MID's irrigation service area. MID will consult with the City regularly with respect to the scheduling of delivery of treated water from the Water Treatment Plant. MID shall be excused from its obligation to deliver treated water in the event that MID is rendered unable, wholly or in part, by force majeure to carry out its obligations under the Treatment and Delivery Agreement. Upon the occurrence of any event of force majeure which impacts MID's ability to deliver treated water, the provisions of the Treatment and Delivery Agreement shall be determinative as to whether the City is excused from its obligation to pay debt service and fixed costs pursuant to the Treatment and Delivery Agreement.

Pursuant to the Treatment and Delivery Agreement two advisory committees are formed for the purposes of the Water Treatment Plant, the Policy Committee and the Technical Committee. Each of these Committees include representatives from MID and the City.

The Board of Directors of MID has the authority to make final decisions with respect to the Water Treatment Plant, subject to the rights of the City to review and advise MID with respect to certain budgetary matters as provided in the Treatment and Delivery Agreement.

***Conservation Program.*** The City has an ongoing water conservation program which includes limitations on watering hours and certain water uses. In the event of drought, the City will likely expand its water conservation program to include additional water use restrictions, such as imposing limitations on the landscaping of new developments.

## **Water Quality**

Land use in the vicinity of the City is a mixture of rural, residential, agricultural, commercial and industrial uses. Potential sanitary hazards include the percolation of agricultural chemicals and fertilizers in adjacent fields and underground storage of fuels in single contained tanks. All wells are adequately located away from sewer lines and sewage disposal facilities. Above-ground on-site fuel storage tanks are or will be provided with a containment system.

Historically, the overall well system has not required major treatment facilities to deliver potable water supplies to date. However, over the past ten years, the number of natural and man-made contaminants which the City is required to monitor has increased from 22 to 96 and there have been significant changes in the maximum contaminant levels permitted under regulations adopted by federal and State regulatory agencies. As a result, concerns over water quality have necessitated the closure of wells with poor water quality and has led to the requirement for treatment of several groundwater wells. The City has commenced litigation to protect, and/or to recover damages to, its groundwater supplies. See “— DBCP Settlement Agreement” and “— PCE Litigation” below.

The operation of the wells is performed automatically in response to system pressure and reservoir water level. All wells are monitored in accordance with State water quality monitoring regulations. Samples are collected for general physical, general mineral, inorganic chemical, radioactivity and organic chemical analysis. Additional monitoring is conducted for bacteriological and general mineral analysis on a routine basis. Bacteriological quality of the groundwater sources is generally good. Follow-up samples on positive total coliform test results are generally negative.

In addition to water wells as a domestic supply source, the City manages approximately 9,500 rock wells for the drainage of stormwater. Stormwater runoff occurs when rainfall intensity exceeds the infiltration rate of the soil. Suspended solids, heavy metals, and oil and grease are the major types of pollutants conveyed by runoff water to drainage facilities. The pollutant loading in runoff typically increases with increased urbanization. About 70 percent of the City service area employs rock wells which vary in depth from 25 to 50 feet. As a precaution to any risk of pollutants from stormwater and other wastewater entering the rock wells and percolating into the usable groundwater aquifer, the City seals its water wells at appropriate depths in relation to rock wells. After 40 years of operation of rock wells, no pollutants attributable to urban drainage have been detected in the drinking water supply. Recent studies of the federal Environmental Protection Agency conclude that properly operated rock wells provide significant treatment and removal of pollutants from percolating water.

### **DBCP Settlement Agreement**

In January 1997, the City came to a settlement in litigation with certain defendants who are the manufacturers and distributors of dibromochloropropane (“DBCP”), which was impacting the drinking water quality throughout the combined City and former Del Este water systems. The settlement agreement (the “Settlement Agreement”) compensated the City for past expenses related to complying with drinking water standards and providing well-head treatment. The Settlement Agreement and the damage recovery covers the City’s entire current and projected service area over the 40 years following the execution of the Settlement Agreement. The Settlement Agreement provides a formula by which the majority of future capital and operating expenses for DBCP mitigation will be compensated by the defendants. The Settlement Agreement includes cost escalation indexes and requires that these payments be used in the area where the damage occurs, as a protection for the defendants against possible Del Este ratepayer actions. The Settlement Agreement puts a variety of operating obligations on the City to ensure that the contamination is managed economically and in compliance with applicable regulations.

The annual proceeds from Settlement Agreement are included in the Historical Operating Results and the Projected Operating Results of the Water Utility System described below. For operating costs, the City receives a specified amount for each well which is receiving well head treatment for DBCP, escalated annually by the Producer Price Index (“PPI”). For each additional or new well requiring GAC equipment, 90% of the capital costs, escalated by the PPI, will be compensated. The actual amount will depend on the type of GAC unit needed for the specific well. The process for compensation provides that the City file an annual claim with the trustee for operation and maintenance and capital costs for the preceding year. The defendants are required to maintain a certain balance in the trustee account, the amount of which declines over the 40 year life of the Settlement Agreement. The City is responsible for any difference between actual operating and capital expense and the stipulated compensation formula. Any shortfall would then be covered by the City through appropriate action, including without limitation a rate adjustment to assure compliance with the covenants in the Settlement Agreement.

Water supplied by the City has and continues to meet all federal and State requirements for quality standards. The City has in place a program to monitor and evaluate proposed regulatory water quality standards. The City anticipates that it will be able to meet increasingly stringent water standards.

### **PCE Litigation**

The City of Modesto Redevelopment Agency brought an action in 1998 against numerous defendants, alleging causes of action for strict liability, negligence, negligence per se, continuing trespass, private and public nuisance, private and public nuisance per se, response costs and declaratory relief under the Carpenter-Presley-Tanner Hazardous Substance Account Act (Health & Safety Code Section 25300 *et seq.*), ultrahazardous activity, and cost recovery under the Polanco Redevelopment Act (Health & Safety Code Section 33459 *et seq.*) (San Francisco County Superior Court Case No. 999345). Simultaneously with the filing of that action, the City, along with the City of Modesto Sewer District No. 1, brought another action against a nearly identical group of defendants seeking damages for solvent contamination under many of the same legal theories; but this action did not include a Polanco Redevelopment Act cause of action (San Francisco County Superior Court Case No. 999643). The defendants included chlorinated solvent manufacturers, distributors of solvents and dry cleaning equipment, chlorinated solvent equipment manufacturers, and dry cleaning retailers.

The complaints alleged that two cleaning solvents, perchloroethylene (“PERC” or “PCE”) and trichloroethylene, cause risks to health and the environment, that dry cleaners customarily dumped solvent wastewater into the public sewer systems, and that dry cleaners experienced a habitual problem of chlorinated solvents leaking into the environment. According to the complaints, the defendants who manufactured and supplied solvents and equipment instructed dry cleaners that chlorinated solvents could be discharged into sewers and/or failed to issue recalls or warnings regarding the equipment and solvents.

The plaintiffs tried five “bellweather” suits before a jury from February to June of 2006, and won a verdict for compensatory damages of \$3.1 million and a verdict for punitive damages of \$175 million, later lowered to \$12 million. In October of 2007, the plaintiffs reached an agreement with one of the defendants, Vulcan Materials Company (“Vulcan”), pursuant to which Vulcan agreed to pay the plaintiffs \$20 million to settle the actions pending against Vulcan. The City’s water system and its sewer system were each credited with half of net amount of the settlement after payment of litigation fees and expenses and certain other costs (approximately \$6.5 million each), but the money may be expended only for projects that will remediate PCE.

The plaintiffs expect to proceed to trial against the remaining defendants in July.

### **Employees**

The Public Works Director has primary responsibility for the management of the Water Utility System, as well as for the sewer system, streets and storm drains. The Water Utility System currently has 82 full-time employees. Employees are represented by the Modesto City Employees Association (MCEA) whose current Memorandum of Understanding expired in July 2007 and by the Modesto Confidential and Management Association whose current Memorandum of Understanding expires on June 23, 2008. The City and MCEA are participating in mediation procedures in hopes

of reaching a negotiated agreement by the end of the current fiscal year. The City has never experienced a labor strike.

### **Retirement Programs**

All permanent full-time employees of the City are covered under the Public Employees' Retirement System (PERS) of the State of California, a defined benefit plan. Pension costs are funded by monthly contributions from the City. Required contributions by the City during fiscal year 2006-07 were \$12,214,853 of which \$569,648 was allocated to the Water Utility System. The City's net assets available for benefits as of June 30, 2005 (the latest data available) were \$47,334,409 less than pension benefit obligations.

As of June 30, 2007, most employee contributions (7.5% out of a total 9% for fire and police and 6.6% out of a total 7% for miscellaneous employees, including Water Utility System employees) are paid by the City on behalf of the employees. The City is also required to contribute all remaining amounts necessary to fund the benefits for its members, using the actuarial basis recommended by the PERS actuaries and actuarial consultants and adopted by the Board of Administration. The current rate is 9.256% of annual covered payroll for miscellaneous employees and 23.692% for safety employees.

In addition to the defined benefit plan described above, the City also maintains a program providing "other post-employment benefits" ("OPEB") for its employees. The City has created an internal service fund to track the OPEB liability, annual expenses and revenues and has been disclosing its liability for OPEB in its Comprehensive Annual Financial Statements for over ten years.

As of December 1, 2006 the Entry Age Actuarial Accrued Liability was \$89,305,020. The City has been funding the current cost of annual benefits and a portion of the long-term cost in each of the years that the liability has been disclosed in its financial statements.

In June 2004, the Governmental Accounting Standards Board ("GASB") issued Statement No. 45 ("GASB 45"), which addresses how state and local governments should account for and report their costs and obligations related to post-employment health care and other non-pension benefits ("OPEB"). GASB 45 generally requires that employers account for and report the annual cost of OPEB and the outstanding obligations and commitments related to OPEB in essentially the same manner as they currently do for pensions. Annual OPEB costs for most employers will be based on actuarially determined amounts that, if paid on an ongoing basis, generally would provide sufficient resources to pay benefits as they come due. The provisions of GASB 45 may be applied prospectively and do not require governments to fund their OPEB plans. An employer may establish its OPEB liability at zero as of the beginning of the initial year of implementation. However, the unfunded actuarial liability is required to be amortized over future periods on the income statement. GASB 45 also established disclosure requirements for information about the plans in which an employer participates, the funding policy followed, the actuarial valuation process and assumptions, and for certain employers, the extent to which the plan has been funded over time. These disclosure requirements are effective for the City's Fiscal Year ending June 30, 2008. GASB 45 may result in an increase in the annual expense recognized by the City for post retirement health care benefits. The City has retained the services of an actuary to determine the extent of the City's OPEB liability. The City has reported its OPEB liability for over 10 years in its Comprehensive Annual Financial Report (CAFR). Further, the City has been funding both the current and a portion of the long-term

liability for much of this time. Discussions are being held to determine whether the City will utilize an irrevocable trust to hold plan assets.

**Insurance**

The City is exposed to various risks of loss including those related to torts as well as the theft of, damage to and destruction of its assets. The City maintains an Insurance Internal Service Fund to account for and finance its risks of loss. Under this program, the City is self-insured for the following risks up to the maximum amount per claim as follows: workers’ compensation - \$750,000, liability - \$1,000,000 and dental care - \$1,200. The City purchases commercial insurance for property loss, airport liability and claims in excess of the preceding self-insured coverage amounts. For liability claims, the City is one of twelve members of the Authority for California Cities Excess Liability risk pool. This pool covers City claims between \$1 million and \$4 million. Commercial insurance covers claims over \$4 million up to an additional \$30 million per claim.

The City currently maintains insurance against damage to the Water Utility System. Coverage thereunder is currently \$10,000,000, but damage resulting from earthquakes is not covered.

**Service Area and Customers**

The water service area of the Water Utility System is within the metropolitan area of the City, located in the central portion of Stanislaus County, consisting of approximately 36 square miles as well as the communities of Salida, Waterford, Empire, Hickman, Grayson, and portions of Turlock, Ceres and Del Rio Estates.

The following tables set forth the revenues for the periods indicated and the ten largest water customers of the Water Utility System in terms of total water sales and total billings for the fiscal year ended June 30, 2007. During calendar year 2007, the Water Utility System delivered approximately 25.9 billion gallons of water to an average of approximately 77,000 customers. Residential accounts (single family as well as multi-family accounts) represent approximately 64.36% of the City’s water consumption and water sales revenues. Commercial, industrial and municipal accounts represent approximately 35.64% of the City’s water consumption and water sales revenues. The City’s ten largest customers represented approximately 8.31% of total water revenues in fiscal year 2006-07.

**WATER UTILITY SYSTEM  
Sale of Water**

	<i>Fiscal Year Ended June 30</i>				
	<i>2003</i>	<i>2004</i>	<i>2005</i>	<i>2006</i>	<i>2007</i>
Revenues (\$000)					
Residential (Flat Rates)	\$ 16,682	\$ 16,849	\$ 19,117	\$ 26,591	\$ 30,716
Commercial, Industrial and Municipal (Metered)	<u>10,075</u>	<u>10,524</u>	<u>10,847</u>	<u>14,516</u>	<u>17,007</u>
Total	<u>\$ 26,757</u>	<u>\$ 27,323</u>	<u>\$ 29,964</u>	<u>\$ 41,107</u>	<u>\$ 47,723</u>

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Source: City of Modesto.

**WATER UTILITY SYSTEM  
Ten Largest Customers  
(Fiscal Year ended June 30, 2007)**

<i>Customer</i>	<i>Business Type</i>	<i>Usage (ccf)<sup>(1)</sup></i>	<i>% of Total Usage</i>	<i>Water Sales Revenues</i>	<i>% of Total Water Sales Revenue</i>
Signature Fruit Co.	Cannery	541,261	1.58%	\$ 648,435	1.36%
Modesto City Schools	Education	458,038	1.34	635,965	1.33
Grover Landscaping (Parks)	Landscape Maintenance	392,111	1.14	580,507	1.22
Stanislaus Foods	Cannery	377,600	1.10	460,575	0.97
Foster Farms	Dairy Processor	338,786	0.99	398,235	0.83
Stanislaus County	Government	200,874	0.59	284,742	0.60
Modesto Irrigation District	Power Company	206,179	0.60	263,276	0.55
Stanislaus Housing Authority	Housing Authority	176,057	0.51	261,904	0.55
City of Modesto	Government	159,911	0.47	239,405	0.50
Sylvan Union School District	Education	<u>141,445</u>	<u>0.41</u>	<u>191,940</u>	<u>0.40</u>
Top Ten Total		2,992,262	8.73%	\$ 3,964,984	8.31%
Total Flat/Metered Revenues				\$47,723,020	

<sup>(1)</sup> "ccf" means hundred cubic feet  
Source: City of Modesto.

**Water Charges and Billing**

**Water Service Rates.** Water rates are fixed by the City Council and are not subject to regulation by the California Public Utility Commission or any other State or federal agency. Customer service charges for single family residential accounts were historically generally based on a flat monthly service charge, which varied only based on the size of the lot and in which of three zones the lot was located. However, under a new rate structure which went into effect on January 1, 2005, a uniform rate for each applicable lot size has been established for all three zones. See "Rate Setting Process" below for a discussion of the process followed by the City in implementing the new rate structure.

Historically, the City has not metered water use by its single family residential customers; however, since 1992 all new construction has been equipped with a meter; and those single family residential properties that are equipped with water meters that are read for billing purposes are charged the metered water rate. Pursuant to State legislation, the City will be required to install meters and to read and bill for water service based on metered rates by 2025. The City Council has adopted a metering plan schedule pursuant to which those requirements would be satisfied by 2019; and, in connection therewith, the City Council recently approved contracts with Automatic Meter Reading in order to provide the most cost efficient and manner of implementing its plan.

Multifamily residential units are currently metered. Each commercial account pays a monthly service charge and a volume charge per hundred cubic feet of water delivered. All regular customers are liable for service charges unless service is permanently discontinued. In addition, all new regular water service connections, increases in meter sizes, and the connection of additional dwelling units to existing services require the payment of a connection fee.

As noted above, the City Council established a new rate structure that went into effect on January 1, 2005. The new rate structure established a single service area, combining all three prior water zones into a single zone. The new rates include a uniform volume-based charge reflecting the volume of water consumed. Residential metered and flat rates are designed so that monthly bills for these types of customers will be comparable were water consumption is estimated to be comparable. Residential flat rates are standardized by lot size (previously, the size ranges varied between water zones) based upon the number of parcels in each range and patterns of water use.

In addition to the rate increases described above, the rate structure adopted by the City Council also provided for uniform increases of 20% effective July 1, 2005, 15% effective July 1, 2006, 5% effective July 1, 2007 and 5% effective July 1, 2008. On each July 1, commencing July 1, 2009 rates are expected to be adjusted to reflect increases in the Consumer Price Index.

The table below sets forth the adopted single family residential flat rates approved through fiscal year 2008-09.

**CITY WATER UTILITY SYSTEM**  
**Monthly Single Family Residential Flat Water Rates<sup>(1)</sup>**

<i>Lot Size</i>	<i>Effective January 1, 2005</i>	<i>Effective July 1, 2005</i>	<i>Effective July 1, 2006</i>	<i>Effective July 1, 2007</i>	<i>Effective July 1, 2008</i>
0-5,000 sq. ft. lot	\$24.47	\$29.36	\$33.77	\$35.45	\$37.23
5,001-7,000 sq. ft. lot	27.81	33.37	38.38	40.30	42.31
7,001-11,000 sq. ft. lot	33.00	39.60	45.54	47.82	50.21
11,001-17,000 sq. ft. lot	35.03	42.04	48.34	50.76	53.30
Over 17,000 sq. ft. lot	41.19	49.42	56.84	59.68	62.66

<sup>(1)</sup> Single family residential properties with water meters that are read for billing purposes, are charged the metered water rate.  
Source: City of Modesto.

The following table sets forth adopted monthly service charge and volume charge for commercial accounts through fiscal year 2008-09.

**CITY WATER UTILITY SYSTEM  
Water Rates and Charges  
Commercial Accounts**

	<i>Effective January 1, 2005</i>	<i>Effective July 1, 2005</i>	<i>Effective July 1, 2006</i>	<i>Effective July 1, 2007</i>	<i>Effective July 1, 2008</i>
<b>Volume-based Rate (\$/hcf)</b>	\$ 0.84	\$ 1.01	\$ 1.16	\$ 1.22	\$ 1.28
<b>Fixed Monthly Meter Charge (in addition to volume-based charges)</b>					
5/8" – 3/4" meter	\$ 9.01	\$ 10.82	\$ 12.44	\$ 13.06	\$ 13.71
1" meter	12.78	15.34	17.64	18.52	19.45
1-1/2" meter	22.13	26.55	30.53	32.06	33.66
2" meter	33.38	40.06	46.06	48.37	50.79
3" meter	63.43	76.12	87.53	91.91	96.51
4" meter	97.19	116.63	134.13	140.83	147.88
6" meter	190.95	229.14	263.51	276.68	290.51
8" meter	303.49	364.19	418.82	439.76	461.75
10" meter	434.84	521.80	600.07	630.08	661.58
12" meter	809.95	971.95	1,117.74	1,173.62	1,232.31

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Source: City of Modesto.

The following table sets forth connection fees for all users except multi-family units by meter size for fiscal year 2007-08.

**CITY WATER UTILITY SYSTEM  
Connection Fees for All Users  
Except Multi-Family Units  
(Fiscal Year 2007-08)**

<i>Meter Size</i>	<i>Connection Fees</i>
5/8"	\$2,162
1"	5,404
1-1/2"	10,808
2"	17,291
3"	34,582
4"	54,035
6"	108,069
8"	172,910
10"	248,558
12" or larger	464,694

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Source: City of Modesto.

**Comparison of Rates and Charges.** The following table lists certain water suppliers in the Modesto region and their average monthly residential water service charges.

**WATER UTILITY SYSTEM  
Comparison of  
Average Monthly Water Rates  
Flat Rate (1" Service)  
As of July 1, 2007**

<i>City</i>	<i>Flat Rate Typical Home</i>
Modesto	\$47.82
Tracy	No Flat Rates
Stockton	No Flat Rates
Turlock	\$30 - \$40
Merced	30.43
Sacramento	25.97
Atwater	15.65
Ceres	15.30

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Source: City of Modesto.

The City’s water rates reflect the steps the City has taken to assure a long-term water supply by entering into the regional water management partnership with MID. The rates of the other nearby cities reflect the particular circumstances of each city’s water system, such as the degree to which it relies on ground water or surface water. The rates also reflect their specific circumstances with regard to the cost of current and prospective water supplies.

**Rate Setting Process.** In connection with its consideration of the new water rate structure which took effect on January 1, 2005, the City Council followed a process which it believes satisfies the requirements of Article XIID of the California Constitution. See “Impact of Proposition 218 on Water Utility System Fees and Charges” below. Specifically, by October 8, 2004, nearly 75,000 notices of the proposed increase in water rates had been mailed to the owners of record of the parcels within the City’s water service area. The notices advised property owners of their right to file written protests to the proposed increase and of a public hearing, set for November 23, 2004, at which such protests would be considered. The number of protests received prior to the completion of the November 23, 2004 public hearing was 8,856, far less than the majority required in order to prevent the implementation of the proposed rate increase. Following the completion of the public hearing, the City Council proceeded to adopt the rate increase as described above. See “Water Charges and Billing” above.

**Rate Study.** Prior to adopting the new water rate structure which took effect on January 1, 2005, the City Council engaged an outside consultant to prepare a water rate study that was ultimately presented to the City Council. In early 2005, the City’s staff noted differences between the amount of revenue actually realized from the initial water rate increases adopted by the City Council and the revenue projections contained in the rate study. In light of those differences, the Water Utility System budgets for fiscal years 2005-06 and 2006-07 use revenue estimates based on actual levels of income received from Water Utility System rates and charges and not on projections included in the rate study. Similarly, the projected operating results of the Water Utility System set

forth below under the caption “Summary of Projected Operating Results of the Water Utility System” are also based on the actual amount of income that is being received by the Water Utility System and not on the forecast thereof shown in the rate study.

The errors in the revenue forecast have been traced to one table in the rate study which contains a series of errors unrelated to the formulas underlying the current water rate structure, and the City believes that there is nothing at this time indicating that the rate structure itself is flawed. The City staff has established a revised revenue forecast for each fiscal year for use in establishing the annual budget. Billed revenues are tracking closely with this revised revenue forecast.

***Challenges to Rates.*** The 2005-2006 Stanislaus County Civil Grand Jury received complaints from Del Rio, an outlying community that receives its water from the City’s Water Utility System Modesto. Del Rio is a wealthy area which includes homes on large lots that had previously received flat rate water. Part of the City’s new rate structure (see “— Water Charges and Billing – Water Service Rates” above) required metering rates for Del Rio, which had the effect of accentuating the accompanying rate hikes. However, the Civil Grand Jury found no evidence to support Del Rio’s contention that the City’s Proposition 218 notice informing the public of the new rate schedule was inadequate. Del Rio also charged that the City’s water rate policy violated a Proposition 218 requirement that a parcel be charged only its proportional costs. The Civil Grand Jury concluded there is no difference in the rate structure between Del Rio and the rest of the City’s water customers that are billed a metered rate; and the Civil Grand Jury made no recommendation regarding the proportionality issues. Del Rio further charged that there was a misuse of funds by using water collections for purposes other than water. While it did make study recommendations, the Civil Grand Jury ultimately determined that the City is accounting for water costs and revenues separately from non-water related accounts. Del Rio’s last charge was that unfairness in the rate process led to Del Rio paying more than other water customers. The Civil Grand Jury could not substantiate this charge, but rather made study recommendations regarding actual customer costs between metered and flat rates, and a further recommendation that conversion from flat to metered rates occur as quickly as possible. The City is continuing its city-wide meter installation program that was begun several years ago with the intent of having every service location on a metered billing by the year 2019.

## **Delinquencies**

The City’s municipal water department has historically accounted for water system revenues on a full accrual basis. The City has developed procedures for handling delinquent accounts, There has not generally been a significant delinquency problem. The threatened suspension of water delivery is normally sufficient incentive to induce customers to make payment on their billings. In addition, the City customers may have tax liens placed on their property when water bills are delinquent. Uncollectible accounts have historically been less than 1% of revenues and remain at that level. The City staff is monitoring delinquencies closely during this period of high foreclosures. Liens are being filed against many delinquent properties to provide greater leverage in the recovery and collection process.

## Historical Operating Results

The following table summarizes operating revenues, operating expenses and net income of the Water Utility System for the five fiscal years 2002-03 through 2006-07, The information for each of the fiscal years shown was prepared by the City on the basis of its audited financial statements.

### WATER UTILITY SYSTEM Historical Debt Service Coverage

	<i>Fiscal Year 2003</i>	<i>Fiscal Year 2004</i>	<i>Fiscal Year 2005</i>	<i>Fiscal Year 2006</i>	<i>Fiscal Year 2007<sup>(1)</sup></i>
<b>GROSS OPERATING REVENUES</b>					
Charges for services	\$27,986,082	\$ 31,353,046	\$31,315,920	\$42,670,821	\$49,289,417
DBCP Settlement	214,803	210,834	2,960,781	1,259,010	0
Connection charges	1,169,995	1,159,296	1,371,958	1,728,973	2,023,224
Interest and Rental Income	964,817	316,688	279,616	532,794	2,279,905
Draw from (Deposit to) Rate Stab. Fund	<u>153,200</u>	<u>0</u>	<u>0</u>	<u>(153,200)</u>	<u>15,616</u>
<b>GROSS OPERATING REVENUES</b>	<b>\$30,488,897</b>	<b>\$33,039,864</b>	<b>\$35,928,275</b>	<b>\$46,038,398</b>	<b>\$53,608,162</b>
<b>OPERATING EXPENSES:</b>					
Total operating expenses <sup>(2)</sup>	\$27,815,253	\$26,757,108	\$29,227,465	\$25,884,448	\$32,466,468
Less: Depreciation	(1,884,768)	(2,173,845)	(2,305,953)	N/A	(2,396,440)
T&DA debt service component paid to MID <sup>(3)</sup>	(6,713,244)	(6,700,881)	(6,705,344)	(6,690,994)	(6,687,444)
Property taxes	77,676	89,921	82,673	84,556	85,487
Plus: Operating Transfers	<u>0</u>	<u>0</u>	<u>218,902</u>	<u>95,385</u>	<u>65,000</u>
<b>TOTAL OPERATING EXPENSES</b>	<b>\$19,294,917</b>	<b>\$17,972,303</b>	<b>\$20,517,743</b>	<b>\$19,373,395</b>	<b>\$23,533,071</b>
<b>NET OPERATING REVENUES</b>	<b>\$11,193,980</b>	<b>\$15,067,561</b>	<b>\$15,410,532</b>	<b>\$26,665,003</b>	<b>\$30,075,091</b>
<b>TOTAL DEBT SERVICE:</b>					
Revenue obligations:					
1997 Certificates of Participation	\$ 1,774,093	\$ 1,780,288	\$ 1,784,908	\$ 1,790,658	\$ 1,794,120
2006 Certificates of Participation	0	0	0	0	1,082,432
Treatment & Delivery Agreement	6,713,244	6,700,881	6,705,344	6,690,994	6,687,444
CDWR Loan	<u>264,656</u>	<u>264,656</u>	<u>264,654</u>	<u>264,454</u>	<u>264,719</u>
<b>TOTAL DEBT SERVICE</b>	<b>\$ 8,751,993</b>	<b>\$ 8,745,825</b>	<b>\$ 8,754,906</b>	<b>\$ 8,746,106</b>	<b>\$ 9,828,715</b>
<b>DEBT SERVICE COVERAGE</b>					
(Net Operating Revenues/Total Debt Service)	1.27	1.72	1.76	3.05	3.06

<sup>(1)</sup> Reflects estimated, unaudited amounts.

<sup>(2)</sup> Includes Treatment and Delivery Agreement debt service component paid to MID.

<sup>(3)</sup> Based on debt service paid pursuant to the Treatment and Delivery Agreement.

Source: City of Modesto.

## Capital Improvement Program

The capital improvement program of the City for the Water Utility System for fiscal years 2007-08 through 2014-15 includes budgeted or planned programs and projects expected to be funded by the City from annual revenues and additional parity obligations. Currently underway is a project to construct 2.5 miles of 24 inch transmission mains and installation of 15 pressure reducing valves at the interfaces with the MID transmission main. Other improvements planned include: construction of a 4 million gallon (MG) storage tank; booster pumps and associated transmission mains in the area west of the City; a 6 MG Storage tank in the north area and a 4 MG tank in the industrial area to the south along with associated booster pumps and transmission mains for those tanks; additional pressure reducing valves and additional transmission mains. These projects are expected to be under

construction during fiscal years 2009-10 and 2010-11. Total capital expenditures for fiscal year 2007-2008 are estimated to be approximately \$26 million.

The City's capital improvement program is a 10-year plan revised annually. Consequently, projects planned for future years may be cancelled, and new projects not presently anticipated may be undertaken. To the extent that total funds required exceed cash available, the City expects that the projects will either be funded by bond proceeds or deferred or terminated.

### **Summary of Projected Operating Results of the Water Utility System**

The City has prepared the following table of projections of operating results of the Water Utility System for the fiscal years ending June 30, 2008 through 2011. The projected amounts set forth below are based on certain assumptions made by the City. To the extent that actual future conditions vary from those assumed in preparing the projections, the actual results will vary from those set forth herein.

**WATER UTILITY SYSTEM  
Projected Operating Results**

	<i>Fiscal Year 2008</i>	<i>Fiscal Year 2009</i>	<i>Fiscal Year 2010</i>	<i>Fiscal Year 2011</i>	<i>Fiscal Year 2012</i>
<b>GROSS OPERATING REVENUES</b>					
Charges for services <sup>(1)</sup>	\$51,378,353	\$53,926,734	\$55,005,269	\$56,105,374	\$57,227,482
DBCP Settlement	-	-	-	-	-
Connection charges	1,747,487	1,497,500	1,747,500	1,747,500	1,747,500
Interest and Rental Income	2,270,948	523,780	539,500	539,500	539,500
Transfers In	-	-	-	-	-
Miscellaneous Revenue	381,275	390,462	315,000	315,000	315,000
Draw from (Deposit to) Rate Stab. Fund	-	-	-	-	-
<b>GROSS OPERATING REVENUES</b>	<u>\$55,778,063</u>	<u>\$56,338,476</u>	<u>\$57,607,269</u>	<u>\$58,707,374</u>	<u>\$59,829,482</u>
<b>OPERATING EXPENSES:</b>					
Total operating expenses <sup>(2)</sup>	\$32,725,156	\$32,915,103	\$35,323,695	\$41,999,985	\$43,291,609
Less: Depreciation	-	-	-	-	-
T&DA debt service component paid to MID	(6,696,543)	(6,693,931)	(6,703,419)	(10,748,405)	(10,794,040)
Less: Litigation Costs	(600,000)	(600,000)	-	-	-
Property taxes	91,084	96,460	-	-	-
Plus: Operating Transfers	<u>99,634</u>	<u>65,000</u>	<u>65,000</u>	<u>65,000</u>	<u>65,000</u>
<b>TOTAL OPERATING EXPENSES</b>	<u>\$25,619,331</u>	<u>\$25,782,632</u>	<u>\$28,685,277</u>	<u>\$31,316,580</u>	<u>\$32,562,569</u>
<b>NET OPERATING REVENUES</b>	<u>\$30,158,732</u>	<u>\$30,555,844</u>	<u>\$28,921,992</u>	<u>\$27,390,794</u>	<u>\$27,266,913</u>
<b>TOTAL DEBT SERVICE:</b>					
Revenue obligations:					
1997 Certificates of Participation	\$ 1,791,930	\$ 1,792,258	\$ 1,794,688	\$ 1,794,013	\$ 1,795,513
Treatment & Delivery Agreement	6,696,543	6,693,931	6,703,419	10,748,405	10,794,040
CDWR Loan	265,000	265,000	265,000	265,000	265,000
2006 Certificates	1,393,332	-	-	-	-
2008 Certificates <sup>(3)</sup>	-	<u>1,962,419</u>	<u>2,077,699</u>	<u>2,066,472</u>	<u>2,055,817</u>
<b>TOTAL DEBT SERVICE</b>	<u>\$10,146,805</u>	<u>\$10,713,607</u>	<u>\$10,840,805</u>	<u>\$14,873,889</u>	<u>\$14,910,370</u>
<b>DEBT SERVICE COVERAGE</b>					
With Connection Fees	2.97	2.85	2.67	1.84	1.83
Without Connection Fees	2.80	2.71	2.51	1.72	1.71

<sup>(1)</sup> Estimated based on approved increase in rates of 5% on July 1, 2008 and of 2%, based on the CPI factor, on each subsequent July 1.

<sup>(2)</sup> Includes estimated Treatment and Delivery Agreement debt service component payable to MID.

<sup>(3)</sup> Assumes an interest rate equal to the fixed rate of interest used in calculating the scheduled payments to be made by the City pursuant to the 2008 Swap Agreement. Includes certain estimated ongoing expenses.

Source: City of Modesto.

**Impact of Proposition 218 on Water Utility System Fees and Charges**

**General.** An initiative measure entitled the “Right to Vote on Taxes Act” (the “Initiative”) was approved by the voters of the State of California at the November 5, 1996 general election. The Initiative added Article XIIC and Article XIID to the California Constitution. According to the “Title and Summary” of the Initiative prepared by the California Attorney General, the Initiative limits “the authority of local governments to impose taxes and property-related assessments, fees and charges.”

**Article XIID.** Article XIID defines the terms “fee” and “charge” to mean “any levy other than an ad valorem tax, a special tax or an assessment, imposed by an agency upon a parcel or upon a person as an incident of property ownership, including user fees or charges for a property-related

service.” A “property-related service” is defined as “a public service having a direct relationship to property ownership.” Article XIID further provides that reliance by an agency on any parcel map (including an assessor’s parcel map) may be considered a significant factor in determining whether a fee or charge is imposed as an incident of property ownership.

Article XIID requires that any agency imposing or increasing any property-related fee or charge must provide written notice thereof to the record owner of each identified parcel upon which such fee or charge is to be imposed and must conduct a public hearing with respect thereto. The proposed fee or charge may not be imposed or increased if a majority of owners of the identified parcels file written protests against it. As a result, if and to the extent that a fee or charge imposed by a local government for water service is ultimately determined to be a “fee” or “charge” as defined in Article XIID, the local government’s ability to increase such fee or charge may be limited by a majority protest.

In *Richmond et al. v. Shasta Community Services District*, 32 Cal. 4th 409 (2004) the California Supreme Court ruled that water connection fees are not property related fees or charges subject to Article XIID while at the same time stating in *dicta* that fees for ongoing water service through an existing connection were property related fees and charges. On July 24, 2008, in *Bighorn-Desert View Water Agency v. Verjil*, 39 Cal. 4th 205 (2008), in what is technically *dicta*, the California Supreme Court cited its decision in *Richmond, supra* in support of its conclusion that a public water agency’s charges for ongoing water delivery are fees and charges within the meaning of Article XIID. Despite the fact that the statement is *dicta*, it does represent the unanimous view of the California Supreme Court. The City believes that it has complied with the requirements of Article XIID, as said article has been construed by the California Supreme Court, in establishing its current rate structure for the Water Service.

In addition, Article XIID includes a number of limitations applicable to pre-existing fees and charges including provisions to the effect that (i) revenues derived from the fee or charge shall not exceed the funds required to provide the property-related service, (ii) such revenues shall not be used for any purpose other than that for which the fee or charge was imposed, (iii) the amount of a fee or charge imposed upon any parcel or person as an incident of property ownership shall not exceed the proportional cost of the service attributable to the parcel and (iv) no such fee or charge may be imposed for a service unless that service is actually used by, or immediately available to, the owner of the property in question. Property-related fees or charges based on potential or future use of a service are not permitted. It is unclear whether, under the foregoing standards, fees and charges may be established at levels that permit deposits to a rate stabilization fund or maintenance of uncommitted cash reserves.

**Article XIIC.** Article XIIC provides that the initiative power shall not be prohibited or otherwise limited in matters of reducing or repealing any local tax, assessment, fee or charge and that the power of initiative to affect local taxes, assessments, fees and charges shall be applicable to all local governments. Article XIIC does not define the terms “local tax,” “assessment,” “fee” or “charge.” However, in *dicta* in its decision in *Bighorn-Desert View Water Agency, supra*, the California Supreme Court concluded that a public water agency’s charges for ongoing water delivery (which, as noted above, it had concluded were fees and charges within the meaning of Article XIID) are also fees within the meaning of Article XIIC and are therefore subject to initiative measures. However, the Court did note that, in doing so:

... [W]e are not holding that the authorized initiative power is free of all limitations. In particular, we are not determining whether the electorate's initiative power is subject to the statutory provision [applicable to Bighorn-Desert View Water Agency] requiring that water service charges be set at a level that "will pay the operating expenses of the agency, ... provide for repairs and depreciation of works, provide a reasonable surplus for improvements, extensions, and enlargements, pay the interest on any bonded debt, and provide a sinking or other fund for the payment of the principal of such debt as it may become due." ... That issue is not currently before us.

Again, while the court's conclusion set forth above is *dicta*, it does represent the unanimous view of the justices.

While the City does not believe that Article XIIC grants to the voters within the City the power to repeal or reduce rates and charges for the Water Service in a manner which would impair its ability to meet its contractual obligations, there can be no assurance as to the availability of particular remedies adequate to protect the Beneficial Owners of the 2008 Certificates. Remedies available to Beneficial Owners of the 2008 Certificates in the event of a default by the City are dependent upon judicial actions which are often subject to discretion and delay and could prove both expensive and time-consuming to obtain.

#### **Effect of Proposition 218 and of Possible General Limitations on Enforcement Remedies**

The ability of the City to comply with its covenants under the Contract and to generate Gross Revenues sufficient to pay the 1997 Payments, the 2008 Payments and any other Parity Obligations may be adversely affected by actions and events outside of the control of the City and by actions taken (or not taken) under Article XIIC or Article XIID by voters, property owners, taxpayers or payers of assessments, fees and charges. Furthermore, any remedies available to the Owners and Beneficial Owners of the 2008 Certificates upon the occurrence of an Event of Default under the 2008 Trust Agreement are in many respects dependent upon judicial actions which are often subject to discretion and delay and could prove both expensive and time consuming to obtain. In addition to the possible limitations on the ability of the City to comply with its covenants under the Contract, the rights and obligations of the City and the Authority under the 2008 Trust Agreement and the Contract may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to limitations on legal remedies against cities in the State of California,

Based on the foregoing, in the event the City fails to comply with its covenants under the Contract, including its covenants to generate sufficient Gross Revenues to pay the 1997 Payments, the 2008 Payments and any other Parity Obligations, there can be no assurance that available remedies will be adequate to fully protect the interests of the Owners or Beneficial Owners of the 2008 Certificates.

#### **Investment Policy**

The cash attributable to the Water Utility System must be invested in accordance with the City's Investment Policy, adopted by the City Council during 1984 and most recently revised during

2008. In accordance with Sections 53601 and following of the California Government Code, idle cash management and investment transactions are the responsibility of the City Finance Director/Treasurer and permitted investments include the following:

- Securities of the U.S. Government, or its agencies,
- Certificates of deposit (or time deposits) and negotiable certificates of deposit placed with commercial banks,
- Banker's acceptances,
- Commercial paper of "prime" quality,
- Local Agency Investment Fund (State Pool) and California Asset Management Program Demand Deposits, and
- Repurchase agreements.

Criteria for selecting investments and the order of priority are:

- Safety of Principal - Preservation of principal and interest,
- Liquidity - Ability to readily convert investment to cash at any moment in time, and
- Yield - Potential dollar earnings on an investment.

The City's cash management system is designed to accurately monitor and forecast expenditures and revenues, thus enabling the City to invest funds to the fullest extent possible. The City attempts to obtain the highest yield when selecting an investment, provided the criteria for safety and liquidity are met.

### **Financial Statements**

The City's annual financial report is audited in accordance with generally accepted auditing standards, and contains opinions that the financial statements present fairly, in all material respects, the financial position of the City. The reports include certain notes to the financial statements. Such notes constitute an integral part of the audited financial statements. The annual financial reports of the City have received the Government Finance Officers Association Certificate of Achievement for each of the past 22 years.

The basic financial statements of the City as of June 30, 2007, which are incorporated by reference in and portions of which are included in Appendix A to this Official Statement, have been audited by Maze & Associates (the "Auditor"), independent certified public accountants, as set forth in their report. In connection with the incorporation of the financial statements and the report of the Auditor thereon in Appendix A to this Official Statement, the City did not request the Auditor to, and the Auditor has not undertaken to, update its report or to take any action intended or likely to elicit information concerning the accuracy, completeness or fairness of the statements made in this Official Statement; and no opinion is expressed by the Auditor with respect to any event subsequent to the date of its report. The Auditor has not been engaged to perform, and has not performed, since the date of its report included herein any procedures on the financial statements addressed in that report.

### **RISK FACTORS**

Some of the factors which could impair the ability of the City to pay the 2008 Payments as they become due under the 2008 Contract are summarized below. This discussion is not meant to be an exhaustive list of the risks associated with the purchase of the 2008 Certificates and does not

necessarily reflect the relative importance of the various factors discussed. Potential investors are advised to consider the following factors, along with all other information in this Official Statement, in evaluating the 2008 Certificates. There can be no assurance that other risk factors will not become material in the future.

## **General**

The payment of principal and interest on the 2008 Certificates is secured solely by a pledge of the Gross Revenues of the Water Utility System and money on deposit in certain funds under the 2008 Trust Agreement. Under the terms of the Master Contract, Gross Revenues are to be deposited in the Revenue Fund and used by the City, ratably, without preference or priority, to (i) pay charges for Maintenance and Operation Costs of the Water Utility System (including amounts reasonably required to be set aside in contingency reserves for Maintenance and Operation Costs the payment of which is not immediately required) as such charges are due and payable and (ii) deposit in the Parity Obligation Payment Fund the amount described in the Master Contract (in general terms, debt service which has accrued or will accrue during the next succeeding month on all Parity Obligations and net payments due or which will be due on all Parity Payment Agreements). See “SECURITY FOR THE 2008 CERTIFICATES — Flow of Funds.” The realization of revenues sufficient in amount to meet both of said obligations is subject to, among other things, the capabilities of management of the City, the ability of the City to provide water service to its users, and the ability of the City to establish and maintain water fees and charges sufficient to provide the required debt service coverage as well as pay for Maintenance and Operation Costs.

If Gross Revenues are insufficient to meet both of the requirements described above, the amounts available to pay Maintenance and Operation Costs will be reduced ratably along with the money to be deposited in the Parity Obligation Payment Fund. This could result in an inability on the part of the City to pay Maintenance and Operation Costs as the same become due which, in turn, could adversely affect the ability of the City to operate the Water Utility System thereby further reducing Gross Revenues.

Among other matters, drought, general and local economic conditions and changes in law and government regulations (including initiatives and moratoriums on growth) could adversely affect the amount of Gross Revenues realized by the City.

## **Earthquakes, Floods and Other Natural Disasters**

Earthquakes, floods or other natural disasters could interrupt operation of the Water Utility System and cause increased costs thereby impairing the ability of the City to realize Gross Revenues. The Master Contract requires the City to “procure and maintain such insurance relating to the Water Utility System which it shall deem advisable or necessary to protect its interests and the interests of the Authority, which insurance shall afford protection in such amounts and against such risks as are usually covered in connection with water systems similar to the Water Utility System.” Such insurance is permitted to be maintained under a program of self-insurance so long as such program is maintained in the amounts and manner as is, in the opinion of an accredited actuary, actuarially sound. While City currently maintains insurance against damages to its Water Utility System in amounts up to \$10,000,000, damages resulting from earthquakes are not covered. MID does not currently maintain insurance for damages to the Water Treatment Plant resulting from either floods or earthquakes.

Natural disasters could also adversely affect the service area of the Water Utility System, leading to reduced demand for water service and could also result in a loss or contamination of groundwater supplies and/or surface water supplies otherwise available to the City.

### **Demand for Water**

There can be no assurance that the demand for water service will occur as described in this Official Statement. Not only is it possible that future increases in demand for water service will not occur at the rate described herein, it is also possible that current levels of demand could be reduced. A reduction in the level of demand could require an increase in rates or charges in order to comply with the Rate Covenant. See “SECURITY FOR THE 2008 CERTIFICATES — Rate Covenant.”

### **Water Supply**

There can be no assurance that the supply of water available to the City to meet potential system-wide demand will be consistent with the assumptions described in this Official Statement. Adequacy of supply could be adversely affected by factors such as prolonged drought or increases in water quality standards which restrict the ability of the City to use existing groundwater supplies to meet demand. See “THE WATER UTILITY SYSTEM — Water Quality.” While the expansion of the Water Treatment Plant and the construction of the 2006 Project and subsequent improvements to the Water Utility System are intended to reduce the City’s dependence upon groundwater supplies, there is no assurance that any of such improvements will be completed or that they will be completed within a time frame and at a cost consistent with the various projections set forth in this Official Statement.

In addition to the potential problems of insufficient water to meet system-wide demand discussed above, it is possible that the supply of water to meet the demands of particular portions of the City’s water service area will be inadequate for such purposes. Some portions of the service area lack the wells necessary to supply them with groundwater, and other portions lack the infrastructure which would be required in order to deliver water from other portions of the service area.

### **Water Utility System Expenses**

There can be no assurance that the Maintenance and Operation Costs will be consistent with the descriptions in this Official Statement. Increases in such costs could require a significant increase in rates or charges in order to pay for existing and future improvements to the Water Utility System and comply with the Rate Covenant.

### **Rate Process**

The passage of Proposition 218 by the California electorate affects the City’s ability to impose future rate increases, and no assurance can be given that future rate increases will not encounter majority protest opposition under Proposition 218. See “THE WATER UTILITY SYSTEM — Impact of Proposition 218 on Water Utility System Fees and Charges” and “— Effect of Proposition 218 and of Possible General Limitations on Enforcement Remedies.”

### **Statutory and Regulatory Impact**

Laws and regulations governing the treatment and delivery of water are enacted and promulgated by governmental agencies on the federal, state and local levels. Compliance with these

laws and regulations may prove costly; and, as more stringent statutory and regulatory standards are developed to protect both the health of consumers and environment, these costs will likely continue to increase. Claims against the City with respect to the Water Utility System could be significant, and such claims will be payable from Gross Revenues. No assurance can be given that the cost of compliance with applicable laws and regulations will not materially adversely affect the ability of the City to comply with the Rate Covenant.

### **Limitations on Remedies and Bankruptcy**

The ability of the City to increase fees and charges for water service and to comply with the Rate Covenant may be adversely affected by actions and events outside of the control of the City and may be adversely affected by actions taken (or not taken) by voters, property owners, taxpayers or payers of fees and charges. See “THE WATER UTILITY SYSTEM — Impact of Proposition 218 on Water Utility System Fees and Charges” and “— Effect of Proposition 218 and of Possible General Limitations on Enforcement Remedies.” Furthermore, any remedies available to the Owners of the 2008 Certificates upon the occurrence of an event of default under the Contract are in many respects dependent upon judicial actions which are often subject to discretion and delay and could prove both expensive and time consuming to obtain.

In addition to the limitations on remedies contained in the Contract, the rights and obligations under the 2008 Certificates and the Contract may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors’ rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to limitations on legal remedies against cities in the State of California. Various legal opinions to be delivered concurrently with the issuance of the 2008 Certificates will be so qualified. In addition, the opinion to be delivered by Sidley Austin LLP, Special Counsel, concurrently with the execution and delivery of the 2008 Certificates, will also state that the enforceability of the Contract is subject to the limitations on the imposition of fees and charges by the City relating to the Water Utility System under Articles XIIC and XIID of the California Constitution. A copy of the proposed form of opinion of Special Counsel is set forth in Appendix C hereto. In the event the City fails to comply with its covenants under the Contract or to pay principal or interest evidenced by the 2008 Certificates, there can be no assurance that available remedies will be adequate to fully protect the interests of the Owners of the 2008 Certificates.

The enforcement of the remedies provided in the Contract could prove both expensive and time consuming. In addition, the rights and remedies provided in the Contract may be limited by and are subject to provisions of the federal bankruptcy laws, as now or hereafter enacted, and to other laws or equitable principles that may affect creditors’ rights.

### **Limited Obligations**

The 2008 Certificates are limited obligations of the City are not secured by a legal or equitable pledge or charge or lien upon any property of the City or any of its income or receipts, except the Gross Revenues of the Water Utility System. The obligation of the City to make the 2008 Payments does not constitute an obligation of the City to levy or pledge any form of taxation or for which the City has levied or pledged any form of taxation.

## **THE AUTHORITY**

The Authority was established pursuant to the provisions of Sections 6500 *et seq.* of the California Government Code and a Joint Exercise of Powers Agreement, dated as of December 1, 1989, by and between the City and the Industrial Development Authority of the City of Modesto. The Authority was established for the purpose of financing the acquisition, construction, improvement and equipping of public capital improvements. The governing board of the Authority consists of the City Council of the City.

## **APPROVAL OF LEGAL PROCEEDINGS**

The legality and enforceability of the 2008 Contract and certain other legal matters are subject to the approval of Sidley Austin LLP, San Francisco, California, acting as Special Counsel. The proposed form of said firm's legal opinion with respect to the 2008 Contract and the 2008 Certificates is attached hereto as APPENDIX C, and such legal opinion will be attached to each 2008 Certificate. Special Counsel undertakes no responsibility for the accuracy, completeness or fairness of this Official Statement. Certain legal matters will be passed upon for the City and the Authority by the City Attorney and by Stradling Yocca Carlson & Rauth, a Professional Corporation, Newport Beach, California, Disclosure Counsel; for the Trustee by the Jensen Law Office, Orinda, California; for the 2008 Certificate Insurer by its General Counsel, for the Liquidity Facility Provider by Kathleen C. Johnson, Esq., Santa Barbara, California. Both Sidley Austin LLP and Stradling Yocca Carlson & Rauth, a Professional Corporation have represented the Underwriter in transactions not involving the City or the Authority. The payment of the fees of Special Counsel, Disclosure Counsel, Counsel to the Underwriter and the Trustee is contingent upon the execution and delivery of the 2008 Certificates.

## **LITIGATION**

There is no action, suit, proceeding, inquiry or investigation, at law or in equity, before or by any court, regulatory agency, public board or body, pending or, to the knowledge of the City or the Authority, threatened against the City or the Authority affecting the existence of the City or the Authority or the titles of their respective directors or officers to their respective offices or seeking to restrain or to enjoin the sale or delivery of the 2008 Certificates, the application of the proceeds thereof in accordance with the 2008 Trust Agreement, or in any way contesting or affecting the validity or enforceability of the 2008 Certificates, the 2008 Trust Agreement, the Contract, or any action of the City or the Authority contemplated by any of said documents, or in any way contesting the completeness or accuracy of this Official Statement or any amendment or supplement thereto, or contesting the powers of the City or the Authority or their respective authority with respect to the 2008 Certificates or any action of the City or the Authority contemplated by any of said documents, nor to the knowledge of the City, is there any basis therefor.

## **TAX MATTERS**

In the opinion of Sidley Austin LLP, San Francisco, California, Special Counsel, based on existing statutes, regulations, rulings and judicial decisions and assuming compliance with certain covenants in the Trust Agreement and the 2008 Contract and requirements of the Internal Revenue Code of 1986, as amended (the "Code"), regarding the use, expenditure and investment of proceeds of the 2008 Certificates and the timely payment of certain investment earnings to the United States, interest with respect to the 2008 Certificates is not includable in the gross income of the owners of

the 2008 Certificates for federal income tax purposes. Failure to comply with such covenants and requirements may cause interest with respect to the 2008 Certificates to be included in gross income retroactively to the date of execution and delivery of the 2008 Certificates.

In the further opinion of Special Counsel, interest with respect to the 2008 Certificates is not treated as an item of tax preference in calculating the federal alternative minimum taxable income of individuals and corporations. Interest with respect to the 2008 Certificates, however, is included as an adjustment in the calculation of federal corporate alternative minimum taxable income and may therefore affect a corporation's alternative minimum tax liability.

Ownership of, or the receipt of interest with respect to, tax-exempt obligations may result in collateral tax consequences to certain taxpayers, including, without limitation, financial institutions, property and casualty insurance companies, certain foreign corporations doing business in the United States, certain S corporations with excess passive income, individual recipients of Social Security or Railroad Retirement benefits, taxpayers that may be deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations and taxpayers who may be eligible for the earned income tax credit. Special Counsel expresses no opinion with respect to any collateral tax consequences and, accordingly, prospective purchasers of the 2008 Certificates should consult their tax advisors as to the applicability of any collateral tax consequences.

Certain requirements and procedures contained or referred to in the Trust Agreement and the 2008 Contract may be changed, and certain actions may be taken, under the circumstances and subject to the terms and conditions set forth in such documents, upon the advice or with the approving opinion of counsel nationally recognized in the area of tax-exempt obligations. Special Counsel expresses no opinion as to the effect of any change to any document pertaining to the 2008 Certificates or of any action taken or not taken where such change is made or action is taken or not taken without our approval or in reliance upon the advice of counsel other than Sidley Austin LLP with respect to the exclusion from gross income of the interest represented by the 2008 Certificates for federal income tax purposes.

### **Information Reporting and Backup Withholding**

Interest paid on tax-exempt obligations is subject to information reporting in a manner similar to interest paid on taxable obligations. While this reporting requirement does not, by itself, affect the excludability of interest from gross income for federal income tax purposes, the reporting requirement causes the payment of interest with respect to the 2008 Certificates to be subject to backup withholding if such interest is paid to beneficial owners that (a) are not "exempt recipients," and (b) either fail to provide certain identifying information (such as the beneficial owner's taxpayer identification number) in the required manner or have been identified by the IRS as having failed to report all interest and dividends required to be shown on their income tax returns. Generally, individuals are not exempt recipients, whereas corporations and certain other entities are exempt recipients. Amounts withheld under the backup withholding rules from a payment to a beneficial owner are allowed as a refund or credit against such beneficial owner's federal income tax liability so long as the required information is furnished to the IRS.

### **State Tax Exemption**

In the further opinion of Special Counsel, interest with respect to the 2008 Certificates is exempt from personal income taxes imposed by the State of California.

## **Future Developments**

Future legislative proposals, if enacted into law, regulations, rulings or court decisions may cause interest with respect to the 2008 Certificates to be subject, directly or indirectly, to federal income taxation or to State or local income taxation, or otherwise prevent beneficial owners from realizing the full current benefit of the tax status of such interest. Further, legislation or regulatory actions and proposals may affect the economic value of the federal or state tax exemption or the market value of the 2008 Certificates.

Prospective purchasers of the 2008 Certificates should consult their tax advisors regarding pending or proposed federal or state tax legislation, regulations, rulings or litigation, as to which Special Counsel expresses no opinion.

A copy of the proposed form of opinion of Special Counsel is attached hereto as Appendix C.

## **RATINGS**

Moody's Investors Service, Inc. ("Moody's") and Standard & Poor's Ratings Services ("S&P") will assign their ratings of "Aaa/VMIG-1" and "AAA/A-1+", respectively, to the 2008 Certificates upon the satisfaction of the following conditions: upon delivery of the 2008 Certificates, (a) the 2008 Certificate Insurance Policy will be issued by the 2008 Certificate Insurer and (b) the Liquidity Facility will be executed and delivered by the Liquidity Facility Provider. In addition, Moody's has assigned an underlying rating of "A2" to the 2008 Certificates, and S&P has assigned them an underlying rating of "A+." Generally, rating agencies base their ratings on information and material furnished directly to them and on investigations, studies and assumptions made by them. The ratings reflect only the views of such organizations and an explanation of the significance of such ratings may be obtained from Moody's Investors Service, 99 Church Street, New York, New York 10017 and Standard & Poor's Ratings Services, 55 Water Street, New York, New York 10041. There is no assurance that the ratings will continue for any given period of time or that they will not be revised downward or withdrawn entirely by such rating agencies, if, in the judgment of such rating agencies, circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price of the 2008 Certificates.

## **FINANCIAL ADVISOR**

The City has retained Public Financial Management, Inc., of San Francisco, California, as Financial Advisor (the "Financial Advisor") in connection with the execution and delivery of the 2008 Certificates. The Financial Advisor is not obligated to undertake, and has not undertaken to make, an independent verification or assume responsibility for the accuracy, completeness, or fairness of the information contained in this Official Statement. Public Financial Management, Inc. is an independent financial advisory firm and is not engaged in the business of underwriting, trading or distributing municipal securities or other public securities.

## **CERTAIN RELATIONSHIPS**

Banc of America Securities LLC, the Underwriter and Remarketing Agent, and Bank of America, N.A., the Swap Provider and the Liquidity Facility Provider, are affiliates, both being subsidiaries of Bank of America Corporation.

**UNDERWRITING**

The 2008 Certificates will be purchased by Banc of America Securities LLC (the “Underwriter”), under a Purchase Contract pursuant to which the Underwriter has agreed to purchase all, but not less than all, of the 2008 Certificates for an aggregate purchase price of \$47,471,079.37 (representing the principal evidenced thereby less Underwriter’s discount of \$153,920.63).

**MISCELLANEOUS**

Insofar as any statements made in this Official Statement involve matters of opinion or of estimates, whether or not expressly stated, they are set forth as such and not as representations of fact. No representation is made that any of such statements made will be realized. Neither this Official Statement nor any statement which may have been made verbally or in writing is to be construed as a contract with the Owners of the 2008 Certificates.

The execution and delivery of this Official Statement have been duly authorized by the City and the Authority.

**CITY OF MODESTO, CALIFORNIA**

By: /s/ Wayne Padilla  
Finance Director/Treasurer

**MODESTO PUBLIC FINANCING AUTHORITY**

By: /s/ Wayne Padilla  
Auditor and Treasurer

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## **APPENDIX A**

### **EXCERPTS FROM THE CITY'S FINANCIAL STATEMENTS**

The City has filed its Comprehensive Annual Financial Report ("CAFR") for Fiscal Year 2006-07 with the Nationally Recognized Municipal Securities Information Repositories. Such CAFR is incorporated herein by reference. The following are excerpts from the CAFR relating to the Water Utility System.

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**CITY OF MODESTO**  
**STATEMENT OF NET ASSETS - PROPRIETARY FUNDS**  
**June 30, 2007**

	<i>Enterprise</i>					<i>Internal Service</i>
	<i>Water</i>	<i>Sewer</i>	<i>Bus</i>	<i>Other Enterprise</i>	<i>Total Enterprise</i>	
<b>ASSETS</b>						
Current assets:						
Cash and cash equivalents	\$ 39,127,144	\$ 22,773,037	\$ 4,152,663	\$ 5,032,664	\$ 71,085,508	\$ 53,382,339
Cash and cash equivalents with fiscal agent	2,445,103	4,049,547		610,647	7,105,297	
Receivables:						
Accounts		44,534	34,844	239,580	318,958	857,956
Interest	337,254	166,699	17,008	16,360	537,321	144,238
Utilities, net	6,441,602	2,641,080		557,922	9,640,604	
Taxes	5,109			796	5,905	
Due from governments			1,803,311	784,877	2,588,188	
Prepaid expenses	706,673				706,673	
Inventories						763,492
Property held for resale				630,000	630,000	
Advances to other funds						1,782,462
Total current assets	<u>49,062,885</u>	<u>29,674,897</u>	<u>6,007,826</u>	<u>7,872,846</u>	<u>92,618,454</u>	<u>56,930,487</u>
Noncurrent assets:						
Restricted assets-cash and cash equivalents	42,767,102	16,432,541			59,199,643	
Unamortized costs of issuance	892,938	892,896			1,785,834	
Land and construction in progress	15,958,371	34,942,347	5,416,369	13,989,727	70,306,814	821,033
Other capital assets, net of accumulated depreciation	<u>63,948,764</u>	<u>103,300,068</u>	<u>13,726,444</u>	<u>43,184,021</u>	<u>224,159,297</u>	<u>19,509,723</u>
Total noncurrent assets	<u>123,567,175</u>	<u>155,567,852</u>	<u>19,142,813</u>	<u>57,173,748</u>	<u>355,451,588</u>	<u>20,330,756</u>
Total assets	<u>172,630,060</u>	<u>185,242,749</u>	<u>25,150,639</u>	<u>65,046,594</u>	<u>448,070,042</u>	<u>77,261,243</u>
<b>LIABILITIES</b>						
Current liabilities:						
Accounts payable	\$ 523,698	\$ 2,715,641	\$ 753,143	\$ 995,442	\$ 4,987,924	\$ 1,401,535
Accrued salaries and benefits	73,227	99,100	18,910	47,027	238,264	87,910
Interest payable	264,620	410,407		51,807	726,834	1,038
Current portion - compensated absences						3,259,769
Current portion - claims liability						4,583,644
Current portion - long-term debt	1,018,977	1,710,000		289,148	3,018,125	102,188
Current portion - developer advances	92,822				92,822	
Deferred revenues			<u>2,897,511</u>	<u>221,058</u>	<u>3,118,569</u>	
Total current liabilities	<u>1,973,344</u>	<u>4,935,148</u>	<u>3,669,564</u>	<u>1,604,482</u>	<u>12,182,538</u>	<u>9,436,084</u>
Noncurrent liabilities:						
Payable from restricted assets						
refundable deposits	656,522	424,851			1,081,373	
Compensated absences						64,628,743
Claims liability						12,042,593
Long-term debt:						
Revenue bonds payable		49,848,192			49,848,192	
Loan payable	1,754,299				1,754,299	
Notes payable						116,220
Obligations under capital leases				77,485	77,485	137,392
Certificates of participation	63,541,989			5,435,000	68,976,989	
Developer advances	1,990,367				1,990,367	
Advances from other funds				<u>878,704</u>	<u>878,704</u>	
Total noncurrent liabilities	<u>67,943,177</u>	<u>50,273,043</u>	<u>3,669,564</u>	<u>6,391,189</u>	<u>124,607,409</u>	<u>76,924,948</u>
Total liabilities	<u>69,916,521</u>	<u>55,208,191</u>	<u>3,669,564</u>	<u>7,995,671</u>	<u>136,789,947</u>	<u>86,361,032</u>
<b>NET ASSETS</b>						
Invested in capital assets, net of related debt	55,702,450	102,691,913	19,142,813	51,372,115	170,791,021	20,091,176
Unrestricted	47,011,089	27,342,645	2,338,262	5,678,808	140,489,074	(29,190,965)
Total net assets	<u>\$ 102,713,539</u>	<u>\$ 130,034,558</u>	<u>\$ 21,481,075</u>	<u>\$ 57,050,923</u>	311,280,095	<u>\$ (9,099,789)</u>
Adjustment to reflect the consolidation of internal service fund activities related to enterprise funds.					<u>(875,700)</u>	
Net assets of business-type activities					<u>\$ 310,404,395</u>	

The notes to basic financial statements are an integral part of this statement.

**CITY OF MODESTO**  
**STATEMENT OF REVENUES, EXPENSES AND CHANGES**  
**IN FUND NET ASSETS - PROPRIETARY FUNDS**  
**Year Ended June 30, 2007**

	<i>Enterprise</i>				<i>Total Enterprise</i>	<i>Internal Service</i>
	<i>Water</i>	<i>Sewer</i>	<i>Bus</i>	<i>Other Enterprise</i>		
<b>OPERATING REVENUES:</b>						
Charges for services	\$ 49,289,417	\$ 24,776,869	\$ 2,390,892	\$ 11,086,967	\$ 87,544,145	\$ 43,641,010
Sales						4,757,411
Cost of sales						(3,939,828)
Miscellaneous	<u>15,616</u>	<u>56,150</u>	<u>154,898</u>	<u>45,875</u>	<u>272,539</u>	
Total operating revenues	<u>49,305,033</u>	<u>24,833,019</u>	<u>2,545,790</u>	<u>11,132,842</u>	<u>87,816,684</u>	<u>44,458,593</u>
<b>OPERATING EXPENSES:</b>						
Salaries and wages	4,105,016	5,136,040	914,950	2,633,769	12,789,775	4,379,438
Contractual services	2,041,814	2,700,492	7,667,756	4,921,651	17,331,713	983,009
Utilities	1,926,634	1,107,437	78,238	413,330	3,525,639	485,393
Maintenance and supplies	4,034,053	2,770,550	1,599,586	2,375,374	10,779,563	3,935,434
Water purchases	12,904,328				12,904,328	
Insurance	131,337	298,464	55,941	160,279	646,021	13,398,895
Claims expense						9,231,869
Employee benefits	1,561,618	2,100,382	339,276	1,032,997	5,034,273	10,851,683
Administration services	2,237,066	1,238,155	497,071	1,302,286	5,274,578	1,504,323
Allocated indirect administrative costs	1,049,489	760,932	277,794	406,422	2,494,637	264,010
Other	78,673	130,838	89,894	77,925	377,330	147,574
Depreciation	<u>2,396,440</u>	<u>5,028,528</u>	<u>2,093,587</u>	<u>2,527,966</u>	<u>12,046,521</u>	<u>3,198,649</u>
Total operating expenses	<u>32,466,468</u>	<u>21,271,818</u>	<u>13,614,093</u>	<u>15,851,999</u>	<u>83,204,378</u>	<u>48,380,277</u>
<b>OPERATING INCOME (LOSS)</b>	<u>16,838,565</u>	<u>3,561,201</u>	<u>(11,068,303)</u>	<u>(4,719,157)</u>	<u>4,612,306</u>	<u>(3,921,684)</u>
<b>NONOPERATING REVENUES (EXPENSES)</b>						
Operating grants			9,672,682	554,649	10,227,331	4,000
Gain (Loss) on disposition of capital assets	(147,600)	(112,741)	(18,470)	(189,445)	(468,256)	(659,282)
Tax revenue				222,776	222,776	
Tax expense	(85,487)	(91,495)		(14,801)	(191,783)	
Interest income	2,242,135	812,288	113,220	100,579	3,268,222	1,481,764
Net increase in fair value of investments	734,296	400,169	40,923	61,723	1,237,111	628,481
Rental income	37,770	58,354	78,106	727,076	901,306	
Settlements and recoveries	831,798	663,663			1,495,461	
Interest expense	(2,249,824)	(1,931,309)		(305,560)	(4,486,693)	(10,577)
Amortization of costs of issuance	<u>(33,378)</u>	<u>(46,220)</u>			<u>(79,598)</u>	
Total nonoperating revenues (expenses)	<u>1,329,710</u>	<u>(247,291)</u>	<u>9,886,461</u>	<u>1,156,997</u>	<u>12,125,877</u>	<u>1,444,386</u>
<b>INCOME (LOSS) BEFORE CAPITAL CONTRIBUTIONS AND TRANSFERS</b>						
CONTRIBUTIONS AND TRANSFERS	18,168,275	3,313,910	(1,181,842)	(3,562,160)	16,738,183	(2,477,298)
Capital contributions	2,345,957	2,666,690	363,651	1,922,714	7,299,012	558,148
Transfers in	264,000	226,389	1,500	985,437	1,477,326	1,298,335
Transfers out	(65,000)	(65,000)	(65,694)	(128,000)	(323,694)	(38,550)
Special item	<u>(296,407)</u>	<u>(209,091)</u>			<u>(505,498)</u>	
CHANGE IN NET ASSETS	20,416,825	5,932,898	(882,385)	(782,009)	24,685,329	(659,365)
NET ASSETS, July 1	<u>82,296,714</u>	<u>124,101,660</u>	<u>22,363,460</u>	<u>57,832,932</u>		<u>(8,440,424)</u>
NET ASSETS, June 30	<u>\$ 102,713,539</u>	<u>\$ 130,034,558</u>	<u>21,481,075</u>	<u>\$ 57,050,923</u>		<u>\$ (9,099,789)</u>
Adjustment to reflect the consolidation of internal service fund activities related to enterprise funds.					<u>(1,712,901)</u>	
Change in net assets of business-type activities					<u>\$ 22,972,428</u>	

The notes to basic financial statements are an integral part of this statement.

**CITY OF MODESTO**  
**STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS**  
**Year Ended June 30, 2007**

	<i>Enterprise</i>					<i>Internal Service</i>
	<i>Water</i>	<i>Sewer</i>	<i>Bus</i>	<i>Other Enterprise</i>	<i>Total Enterprise</i>	
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>						
Receipts from customers and users	\$ 47,758,187	\$ 24,828,928	\$ 2,595,078	\$ 11,954,968	\$ 87,137,161	\$ 4,812,775
Receipts from interfund services provided	427,858	65,035		23,521	516,414	39,660,607
Payments to suppliers	(19,473,381)	(2,969,190)	(9,054,243)	(5,884,024)	(37,380,838)	(18,835,253)
Payment of insurance claims						(8,936,742)
Payments to employees	(5,661,907)	(7,237,125)	(1,251,420)	(3,663,140)	(17,813,592)	(8,956,088)
Payments for interfund services used	<u>(5,310,466)</u>	<u>(3,964,147)</u>	<u>(1,412,537)</u>	<u>(3,364,808)</u>	<u>(13,781,958)</u>	<u>(2,244,913)</u>
Net cash provided (used) by operating activities	<u>17,740,291</u>	<u>10,723,501</u>	<u>(8,853,122)</u>	<u>(933,483)</u>	<u>18,677,187</u>	<u>5,500,386</u>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>						
Operating grants received			11,935,926	565,482	12,501,408	5,038
Taxes received				222,776	222,776	
Settlements and recoveries	831,798	663,663			1,495,461	
Transfers in	264,000	226,389	1,500	985,437	1,477,326	1,298,335
Transfers out	(65,000)	(65,000)	(65,694)	(128,000)	(323,694)	(38,550)
New advances from other funds				878,704		121,014
Net cash provided (used) by noncapital financing activities	<u>1,030,798</u>	<u>825,052</u>	<u>11,871,732</u>	<u>2,524,399</u>	<u>15,373,277</u>	<u>1,385,837</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>						
Acquisition and construction of capital assets	(6,058,751)	(10,512,609)	(1,222,095)	(2,120,363)	(19,913,818)	(3,732,362)
Proceeds of sale of capital assets		13,502				
Proceeds of debt issues	46,275,000	16,535,000				
Costs of issuance paid	(685,703)	(339,604)				
Bond discount paid		(323,867)				
Principal repayments	(1,072,336)	(1,650,000)		(275,955)	(2,998,291)	(26,587)
Interest paid	(2,163,506)	(2,055,524)		(309,551)	(4,528,581)	(10,577)
Capital grants received			363,651	1,546,459	1,910,110	
Connection fees for capital purposes	<u>2,023,224</u>	<u>663,316</u>			<u>2,686,540</u>	
Net cash used by capital and related financing activities	<u>38,317,928</u>	<u>2,330,214</u>	<u>(858,444)</u>	<u>(1,159,410)</u>	<u>(22,844,040)</u>	<u>(3,769,526)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>						
Interest received	2,029,235	1,227,069	105,360	136,465	3,498,129	1,557,085
Net increase in the fair value of investments	<u>734,296</u>	<u>400,169</u>	<u>40,923</u>	<u>61,723</u>	<u>1,237,111</u>	<u>628,481</u>
Net cash provided by investing activities	<u>2,763,531</u>	<u>1,627,238</u>	<u>146,283</u>	<u>198,188</u>	<u>4,735,240</u>	<u>2,185,566</u>
Net increase (decrease) in cash and cash equivalents	59,852,548	15,506,005	2,306,449	629,694	78,294,696	5,354,364
CASH AND CASH EQUIVALENTS, JULY 1	<u>24,486,801</u>	<u>27,749,120</u>	<u>1,846,214</u>	<u>5,013,617</u>	<u>59,095,752</u>	<u>48,027,975</u>
CASH AND CASH EQUIVALENTS, JUNE 30	<u>\$ 84,339,349</u>	<u>\$ 43,255,125</u>	<u>\$ 4,152,663</u>	<u>\$ 5,643,311</u>	<u>\$ 137,390,448</u>	<u>\$ 53,382,339</u>
<b>RECONCILIATION TO STATEMENT OF NET ASSETS:</b>						
Cash and cash equivalents	\$ 39,127,144	\$ 22,773,037	\$ 4,152,663	\$ 5,032,664	\$ 71,085,508	\$ 53,382,339
Cash and cash equivalents with fiscal agent	2,445,103	4,049,547		610,647	7,105,297	
Restricted assets-cash and cash equivalents	<u>42,767,102</u>	<u>16,432,541</u>			<u>59,199,643</u>	
TOTAL CASH AND CASH EQUIVALENTS	<u>\$ 84,339,349</u>	<u>\$ 43,255,125</u>	<u>\$ 4,152,663</u>	<u>\$ 5,643,311</u>	<u>\$ 137,390,448</u>	<u>\$ 53,382,339</u>

(continued)

	<i>Enterprise</i>					
	<i>Water</i>	<i>Sewer</i>	<i>Bus</i>	<i>Other Enterprise</i>	<i>Total Enterprise</i>	<i>Internal Service</i>
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:						
Operating income (loss)	<u>\$ 16,838,565</u>	<u>\$ 3,561,201</u>	<u>\$ (11,068,303)</u>	<u>\$ (4,719,157)</u>	<u>\$ 4,612,306</u>	<u>\$(3,921,684)</u>
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:						
Depreciation	2,396,440	5,028,528	2,093,587	2,527,966	12,046,521	3,198,649
Rental income	37,770	58,354	78,106	727,076	901,306	
Taxes paid	(85,487)	(91,495)		(15,597)	(192,579)	
Special item	(296,407)	(209,091)			(505,498)	
Change in assets and liabilities:						
(Increase) in accounts receivable	1,440	14,175	(28,818)	120,541	107,338	(23,898)
(Increase) in utilities receivable	(1,149,441)	(200,399)		490	(1,349,350)	
(Increase) in taxes receivable	(1,169)				(1,169)	
Decrease in due from governments		127,064			127,064	38,687
(Increase) decrease in prepaid expenses	296,327				296,327	
(Increase) in inventories						(246,573)
(Decrease) in accounts payable and accrued expenses	(294,886)	2,374,117	69,500	423,236	2,571,967	(114,955)
Increase in accrued salaries and benefits	4,727	(703)	2,806	3,626	10,456	3,475
Increase in compensated absences						6,271,558
(Decrease) in claims liability						295,127
Increase in deferred revenues				(1,664)	(1,664)	
Increase (decrease) in refundable deposits	<u>(7,588)</u>	<u>61,750</u>			<u>54,162</u>	
Total adjustments	<u>901,726</u>	<u>7,162,300</u>	<u>2,215,181</u>	<u>3,785,674</u>	<u>14,064,881</u>	<u>9,422,070</u>
Net cash provided (used) by operating activities	<u>\$ 17,740,291</u>	<u>\$ 10,723,501</u>	<u>\$(8,853,122)</u>	<u>\$ (933,483)</u>	<u>\$ 8,677,187</u>	<u>\$ 5,500,386</u>
NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES:						
Capital assets transferred in	\$ 38,683	\$ 444,898		\$ 18,545	\$ 502,126	\$ 558,148
Developer infrastructure contributions	284,050	1,558,476			1,842,526	

## APPENDIX B

### DEFINITIONS AND SUMMARY OF PRINCIPAL LEGAL DOCUMENTS

The following is a summary of the provisions of the Contract and the Trust Agreement. This summary is not intended to be definitive and is qualified in its entirety by reference to the aforementioned documents. Copies of the Contract and the Trust Agreement are available upon request from the Trustee.

All capitalized terms not defined herein or elsewhere in this Official Statement shall have the meanings set forth in the Contract and the Trust Agreement.

#### THE CONTRACT

Certain provisions of the Contract are summarized below. THIS SUMMARY DOES NOT PURPORT TO BE COMPLETE OR DEFINITIVE AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO THE FULL TERMS OF THE CONTRACT.

#### Definitions

The following are summaries of definitions of certain terms from the Contract used in this Summary of Principal Legal Documents or elsewhere in this Official Statement.

“Accountant’s Report” means a report signed by an Independent Certified Public Accountant.

“Adjusted Annual Gross Revenues” means, for any Fiscal Year or any designated twelve (12) month period in question, the Gross Revenues during such Fiscal Year or twelve (12) month period, plus deposits to the Revenue Fund from amounts on deposit in the Rate Stabilization Fund, but only as and to the extent specified in the Master Contract; minus, (y) amounts transferred from the Revenue Fund to the Rate Stabilization Fund in accordance with the Master Contract and, (z) for the purposes of determining compliance with the rate covenant only set forth in the Master Contract, earnings from the investments in the Parity Reserve Fund that are deposited in the Revenue Fund in such Fiscal Year or twelve (12) month period.

“Adjusted Annual Net Revenues” means, for any Fiscal Year or any designated twelve (12) month period in question, the Adjusted Annual Gross Revenues during such Fiscal Year or twelve (12) month period less the Maintenance and Operation Costs during such Fiscal Year or twelve (12) month period.

“Annual Debt Service” means, for any Fiscal Year or any designated twelve (12) month period in question, the required payments to be made with respect to all Outstanding Parity Obligations in such Fiscal Year or twelve (12) month period; provided, that for purposes of determining compliance with the rate covenant set forth in the Master Contract, the Reserve Fund Requirement and conditions for the execution of Parity Obligations:

(A) Generally. Except as otherwise provided by subparagraph (B) with respect to Variable Interest Rate Parity Obligations and by subparagraph (C) with respect to Parity Obligations with respect to which a Payment Agreement is in force, interest on any Parity Obligation will be calculated based on the actual amount of interest that is payable under that Parity Obligation;

(B) Interest on Variable Interest Rate Parity Obligations. The amount of interest deemed to be payable on any Variable Interest Rate Parity Obligation will be calculated on the assumption that the interest rate on that Parity Obligation would be equal to the rate (the “assumed RBI-based rate”) that is ninety percent (90%) of the average RBI during the twelve (12) calendar month period immediately preceding the date in which the calculation is made;

(C) Interest on Parity Obligations with respect to which a Payment Agreement is in force. The amount of interest deemed to be payable on any Parity Obligations with respect to which a Payment Agreement is in force will, so long as the Qualified Counterparty thereto is not in default thereunder, be based on the net economic effect on the City expected to be produced by the terms of such Parity Obligation and such Payment Agreement, including but not limited to the effects that (i) such Parity Obligation would, but for such Payment Agreement, be treated as an obligation bearing interest at a Variable Interest Rate instead will be treated as an obligation bearing interest at a fixed interest rate, and (ii) such Parity Obligation would, but for such Payment Agreement, be treated as an obligation bearing interest at a fixed interest rate instead will be treated as an obligation bearing interest at a Variable Interest Rate; and accordingly, the amount of interest deemed to be payable on any Parity Obligation with respect to which a Payment Agreement is in force will, so long as the Qualified Counterparty thereto is not in default thereunder, be an amount equal to the amount of interest that would be payable at the rate or rates stated in such Parity Obligation plus the Payment Agreement Payments minus the Payment Agreement Receipts, and for the purpose of calculating Payment Agreement Receipts and Payment Agreement Payments under such Payment Agreement, the following assumptions will be made:

(1) Counterparty Obligated to Pay Actual Variable Interest Rate on Variable Interest Rate Parity Obligations. If the Payment Agreement obligates a Qualified Counterparty to make payments to the City based on the actual Variable Interest Rate on a Parity Obligation that would, but for the Payment Agreement, be treated as a Variable Interest Rate Parity Obligation and obligates the City to make payments to the Qualified Counterparty based on a fixed rate, payments by the City to the Qualified Counterparty will be assumed to be made at the fixed rate specified by the Payment Agreement and payments by the Qualified Counterparty to the City will be assumed to be made at the actual Variable Interest Rate on such Parity Obligation, without regard to the occurrence of any event that, under the provisions of the Payment Agreement, would permit the Qualified Counterparty to make payments on any basis other than the actual Variable Interest Rate on such Parity Obligation, and such Parity Obligation will set forth a debt service schedule based on that assumption;

(2) Variable Interest Rate Parity Obligations and Payment Agreements Having the Same Variable Interest Rate Component. If both a Payment Agreement and the related Parity Obligation that would, but for the Payment Agreement, be treated as a Variable Interest Rate Parity Obligation, include a variable interest rate payment component that is required to be calculated on the same basis (including, without limitation, on the basis of the same variable interest rate index), it will be assumed that the variable interest rate payment component payable pursuant to the Payment Agreement is equal in amount to the variable interest rate component payable on such Parity Obligation;

(3) Variable Interest Rate Parity Obligations and Payment Agreements Having Different Variable Interest Rate Components. If a Payment Agreement obligates either the City or the Qualified Counterparty to make payments of a variable interest rate component on a basis that is different (including, without limitation, on a different variable interest rate index) from the basis that

is required to be used to calculate interest on the Parity Obligation that would, but for the Payment Agreement, be treated as a Variable Interest Rate Parity Obligation it will be assumed:

(a) City Obligated to Make Payments Based on Variable Interest Rate Index. If payments by the City under the Payment Agreement are based on a variable interest rate index and payments by the Qualified Counterparty are based on a fixed interest rate, payments by the City to the Qualified Counterparty will be based upon an interest rate equal to the assumed RBI-based rate, and payments by the Qualified Counterparty to the City will be based on the fixed rate specified by the Payment Agreement; and

(b) City Obligated to Make Payments Based on Fixed Interest Rate. If payments by the City under the Payment Agreement are based on a fixed interest rate and payments by the Qualified Counterparty are based on a variable interest rate index, payments by the City to the Qualified Counterparty will be based on an interest rate equal to the rate (the “assumed fixed payor rate”) that is one hundred and five percent (105%) of the fixed interest rate specified by the Payment Agreement to be paid by the City, and payments by the Qualified Counterparty to the City will be based on a rate equal to the actual variable interest rate on the Variable Interest Rate Parity Obligation.

(4) Certain Payment Agreements May be Disregarded. Notwithstanding the provisions of subparagraphs (C)(1), (2) and (3) of this definition, the City will not be required to (but may at its option) take into account as set forth in subparagraph (C) of this definition (for the purpose of determining Annual Debt Service) the effects of any Payment Agreement that has a remaining term of ten (10) years or less;

(D) Debt Service on Parity Payment Agreements. No interest will be taken into account with respect to a Parity Payment Agreement for any period during which Payment Agreement Payments on that Parity Payment Agreement are taken into account in determining Annual Debt Service on a related Parity Obligation under subparagraph (C) of this definition; provided, that for any period during which Payment Agreement Payments are not taken into account in calculating Annual Debt Service on any Parity Obligation because the Parity Payment Agreement is not then related to any Parity Obligation, interest on that Parity Payment Agreement will be taken into account by assuming:

(1) City Obligated to Make Payments Based on Fixed Interest Rate. If the City is obligated to make Payment Agreement Payments based on a fixed interest rate and the Qualified Counterparty is obligated to make payments based on a variable interest rate index, payments by the City will be based on the assumed fixed payor rate, and payments by the Qualified Counterparty will be based on a rate equal to the average rate determined by the variable interest rate index specified by the Payment Agreement during the quarter preceding the quarter in which the calculation is made; and

(2) City Obligated to Make Payments Based on Variable Interest Rate Index. If the City is obligated to make Payment Agreement Payments based on a variable interest rate index and the Qualified Counterparty is obligated to make payments based on a fixed interest rate, payments by the City will be based on an interest rate equal to the average rate determined by the variable interest rate index specified by the Payment Agreement during the quarter preceding the quarter in which the calculation is made, and the Qualified Counterparty will make payments based on the fixed rate specified by the Parity Payment Agreement; and

(3) Certain Payment Agreements May be Disregarded. Notwithstanding the provisions of subparagraphs (D)(1) and (2) of this definition, the City will not be required to (but may at its option) take into account (for the purpose of determining Annual Debt Service) the effects of any Payment Agreement that has a remaining term of ten (10) years or less;

(E) Balloon Parity Obligations. For purposes of calculating Annual Debt Service on any Balloon Parity Obligations, it will be assumed that the principal of those Balloon Parity Obligations, together with interest thereon at a rate equal to the assumed RBI-based rate, will be amortized in equal annual installments over a term of thirty (30) years from the date of issuance.

“Authority” means the Modesto Public Financing Authority, a joint exercise of powers authority duly organized and existing under and by virtue of the laws of the State of California.

“Average Annual Debt Service” means the sum of the Annual Debt Service for all Fiscal Years during the period commencing with the Fiscal Year in which such calculation is made (or if appropriate, the first full Fiscal Year following the issuance of Parity Obligations) and terminating with the last Fiscal Year in which payments are due under Outstanding Parity Obligations, divided by the number of such Fiscal Years.

“Balloon Parity Obligation” means any Parity Obligation described as such in such Parity Obligation.

“Business Day” means any day (other than a Saturday or a Sunday) on which banks in New York, New York, are open for business and on which the Trustee is open for business at its corporate trust office in San Francisco, California.

“CDWR Loan” means the loan to the City from the State of California Department of Water Resources in the principal amount of \$3,895,000, which obligation is payable from Gross Revenues on a parity with the Payments under the Contracts.

“Certificate of the City” means an instrument in writing signed by the City Manager, the Finance Director, or any other officer of the City duly authorized by the City Council for that purpose.

“City” means the City of Modesto, a charter city and municipal corporation, duly organized and existing under and by virtue of the Constitution and laws of the State of California.

“Code” means the Internal Revenue Code of 1986, and the regulations issued thereunder, as the same may be amended from time to time, and any successor provisions of law. Reference to a particular section of the Code will be deemed to be a reference to any successor to any such section.

“Connection Fees” means all fees and charges payable to the City for the privilege of connecting to the Water Utility System.

“Consultant’s Report” means a report signed by an Independent Consultant.

“Continuing Disclosure Agreement” means any continuing disclosure agreement, by and between the City and the Trustee, delivered pursuant to the Contracts.

“Contracts” means the Master Contract and all Supplemental Contracts.

“Event of Default” means an event described as an event of default under the Master Contract.

“Federal Securities” means United States of America Treasury bills, notes, bonds or certificates of indebtedness, or obligations for which the full faith and credit of the United States of America are pledged for the payment of interest and principal, or securities evidencing ownership interests in such obligations or in specified portions of the interest on or principal of such obligations.

“Finance Director” means the Finance Director of the City.

“Fiscal Year” means the period beginning on July 1 of each year and ending on the next succeeding June 30, or any other annual accounting period hereafter selected and designated by the City Council of the City as the Fiscal Year of the City.

“Generally Accepted Accounting Principles” means the uniform accounting and reporting procedures set forth in publications of the American Institute of Certified Public Accountants or its successor, or by any other generally accepted authority on such procedures selected by the City, and includes, as applicable, the standards set forth by the Governmental Accounting Standards Board or its successor.

“Gross Revenues” means all gross income and revenue received or receivable by the City from the ownership or operation of the Water Utility System, determined in accordance with Generally Accepted Accounting Principles, including all rates, fees and charges (including all Connection Fees, contributions in aid of construction, and charges and standby water availability charges legally available for debt service) received by the City for the Water Service and the other services and facilities of the Water Utility System and all net proceeds of insurance covering business interruption loss relating to the Water Utility System and all other income and revenue howsoever derived by the City from the ownership or operation of the Water Utility System or arising from the Water Utility System, and including all Payment Agreement Receipts, and including all income from the deposit or investment of any money in the Revenue Fund or, to the extent deposited in the Revenue Fund, in the Parity Reserve Fund, but excluding in all cases any proceeds of taxes and any refundable deposits made to establish credit and advances.

“Improvement Fund” means the City of Modesto Water Utility System Improvement Fund established pursuant to the Master Contract.

“Independent Certified Public Accountant” means any certified public accountant or firm of such accountants duly licensed and entitled to practice and practicing as such under the laws of the State of California, appointed and paid by the City, and who, or each of whom:

(1) is in fact independent according to the Statement of Auditing Standards No. 1 and not under the domination of the City;

(2) does not have a substantial financial interest, direct or indirect, in the operations of the City; and

(3) is not connected with the City as a director, officer or employee of the City, but who may be regularly retained to audit the accounting records of and make reports thereon to the City.

“Independent Consultant” means any registered engineer or firm of registered engineers of national reputation generally recognized to be well qualified in engineering matters relating to water systems, or any other financial consultant or firm of financial consultants generally recognized to be well qualified in matters relating to water systems, appointed and paid by the City, and who or each of whom:

- (1) is in fact independent and not under the domination of the City;
- (2) does not have a substantial financial interest, direct or indirect, in the operations of the City; and
- (3) is not connected with the City as a director, officer or employee of the City, but may be regularly retained to make reports to the City.

“Maintenance and Operation Costs” means the costs paid or incurred by the City for maintaining and operating the Water Utility System, determined in accordance with Generally Accepted Accounting Principles, including, but not limited to, (a) all reasonable expenses of management and repair and other expenses necessary to maintain and preserve the Water Utility System in good repair and working order, (b) all costs of water purchased by the City, including all costs under the Treatment and Delivery Agreement which do not constitute debt service thereunder, (c) all administrative costs of the City that are charged directly or apportioned to the operation of the Water Utility System, such as salaries and wages of employees, overhead, taxes (if any) and insurance premiums, payments into pension funds, and (d) all other reasonable and necessary costs of the City or charges required to be paid by it to comply with the terms of the Master Contract or of any resolution authorizing the execution of any Parity Obligation or of such Parity Obligation, such as compensation, reimbursement and indemnification of the trustee or remarketing agent for any such Parity Obligation, letter of credit fees for any such Parity Obligations and fees and expenses of Independent Certified Public Accountants and Independent Consultants; but excluding in all cases (1) depreciation, replacement and obsolescence charges or reserves therefor and amortization of intangibles, premiums and discounts, (2) interest expense, (3) amounts paid from funds of the City other than Gross Revenues, and (4) in-lieu transfers or recoupment of contributed capital to the City’s general fund.

“Master Contract” means the Master Installment Purchase Contract executed and entered into as of November 1, 1997, by and between the City and the Authority, as the same may be amended or supplemented from time to time.

“Maximum Annual Debt Service” means the greatest Annual Debt Service payable on Parity Obligations in any Fiscal Year during the period commencing with the Fiscal Year in which the determination is being made and terminating with the last Fiscal Year in which payments are due under Outstanding Parity Obligations.

“Moody’s” means Moody’s Investors Service, a corporation duly organized and existing under and by virtue of the laws of the State of Delaware, and its successors or assigns, except that if such corporation will be dissolved or liquidated or will no longer perform the services of a municipal securities rating agency, then “Moody’s” will be deemed to refer to any other nationally recognized municipal securities rating agency rating Parity Obligations at the Request of the City.

“Net Proceeds” means, when used with respect to any condemnation award or with respect to any insurance proceeds, the amount of such condemnation award or such insurance proceeds remaining after payment of all expenses (including attorneys’ fees) incurred in the collection of such award or such proceeds.

“1997 Certificates” means the \$25,585,000 Refunding Revenue Certificates of Participation (1997 Water Utility System Refinancing Project), evidencing and representing proportionate interests of the owners thereof in the 1997 Payments to be made by the City.

“1997 Payments” means the installment payments required to be made by the City to the Authority under and pursuant to the 1997 Supplemental Contract.

“1997 Supplemental Contract” means the 1997 Supplemental Installment Purchase Contract, executed and entered into as of November 1, 1997, by and between the City and the Authority, supplementing the Master Contract.

“1997 Trust Agreement” means that certain Trust Agreement, dated as of November 1, 1997, by and between the Authority and State Street Bank and Trust Company, N.A., which has been succeeded by The Bank of New York Trust Company, N.A., as trustee, pursuant to which there was executed and delivered the 1997 Certificates.

“Opinion of Counsel” means a written opinion of counsel of recognized national standing in the field of law relating to municipal bonds, retained by the City.

“Outstanding,” when used as of any particular time with reference to Parity Obligations, means all Parity Obligations which have not been paid or otherwise satisfied as provided in the Master Contract.

“Parity Bank Agreements” means an agreement with a bank or other financial institution relating to an irrevocable letter of credit, guarantee or other credit enhancement device providing liquidity or irrevocable credit or security for the payment of Parity Obligations.

“Parity Obligation Payment Fund” means the City of Modesto Water Utility System Parity Obligation Payment Fund established pursuant to the Master Contract.

“Parity Obligations” means the payment obligations under the Treatment and Delivery Agreement which constitute debt service, the payment obligations under the CDWR Loan Agreement, and all Supplemental Contracts and all other obligations hereafter incurred by the City the payment of which constitutes a charge and lien on the Gross Revenues equal to and on a parity with the charge and lien upon the Gross Revenues for the payment of the Payments, other than (i) such portion of the payment obligations (including certain payments due upon an early termination thereof) under any Parity Payment Agreement to the extent such obligations are expressly subordinate to Parity Obligations pursuant to the terms of such Parity Payment Agreement and (ii) Parity Bank Agreements; provided that no amounts have been drawn under any such Parity Bank Agreements which have not been reimbursed by the City.

“Parity Payment Agreement” means a Payment Agreement which is a Parity Obligation.

“Parity Reserve Fund” means the City of Modesto Water Utility System Parity Reserve Fund established pursuant to the 1997 Trust Agreement.

“Payment Agreement” means a written agreement for the purpose of managing or reducing the City’s exposure to fluctuations in interest rates or for any other interest rate, investment, cash flow, asset or liability managing purposes, entered into either on a current or forward basis by the City and a Qualified Counterparty in connection with, or incidental to, the entering into of any Parity Obligation, that provides for an exchange of payments based on interest rates, ceilings or floors on such payments, cash flows, options on such payments, or any combination thereof or any similar device.

“Payment Agreement Payments” means the amounts required to be paid periodically by the City to the Qualified Counterparty pursuant to a Payment Agreement.

“Payment Agreement Receipts” means the amounts required to be paid periodically by the Qualified Counterparty to the City pursuant to a Payment Agreement.

“Payment Date” means any date on which Payments are scheduled to be paid by the City under and pursuant to any Supplemental Contract.

“Payments” means the installment payments scheduled to be paid by the City under and pursuant to the Master Contract and all Supplemental Contracts.

“Permitted Investments” means any of the following obligations if and to the extent that they are permissible investments of funds of the City as stated in its current investment policy (copies of which the City will provide on a current basis to the Trustee) and to the extent then permitted by law:

- (1) Federal Securities;
- (2) Obligations issued by the Resolution Funding Corporation and the Student Loan Marketing Association, or obligations, participations, or other instruments of or issued by, or fully guaranteed as to interest and principal by, the Government National Mortgage Association (excluding stripped mortgage backed securities which are valued at greater than par on the unpaid principal);
- (3) Bills of exchange or time drafts drawn on and accepted by a commercial bank (including the Trustee or any of its affiliates), otherwise known as bankers acceptances, which are eligible for purchase by the Federal Reserve System and which are drawn on any bank the short-term obligations of which are rated in the highest letter and numerical rating category as provided by Moody’s and by S&P; provided, that purchases of eligible bankers acceptances may not exceed two hundred seventy (270) days’ maturity;
- (4) Commercial paper of “prime” quality of the highest ranking or of the highest letter and numerical rating category as provided by Moody’s and by S&P, which commercial paper is limited to issuing corporations that are organized and operating within the United States of America and that have total assets in excess of five hundred million dollars (\$500,000,000) and that have an “A” or higher rating for the issuer’s unsecured debentures, other than commercial paper, as provided by Moody’s and by S&P; provided, that purchases of eligible commercial paper may not exceed one hundred eighty (180) days’ maturity nor represent more than ten percent (10%) of the outstanding commercial paper of an issuing corporation;

(5) Non-negotiable certificates of deposit issued by a state or national bank (including the Trustee or any of its affiliates) that have maturities of not more than three hundred sixty-five (365) days and that are fully insured by the Federal Deposit Insurance Corporation or the short-term obligations of which state or national bank are rated no lower than “A1” by Moody’s and “A+” by S&P;

(6) Any repurchase agreement of any securities enumerated in subdivisions (1) and (2) with any state or national bank (including the Trustee or any of its affiliates) or government bond dealer reporting to, trading with, and recognized as a primary dealer by the Federal Reserve Bank of New York, which agreement is either (A) with any institution which has debt rated no lower than “A1” by Moody’s and “A+” by S&P or whose commercial paper is rated no lower than “P-1” by Moody’s and no lower than “A-1” by S&P; (B) with any corporation or other entity that falls under the jurisdiction of the Federal Bankruptcy Code; provided, that (a) the term of such repurchase agreement is less than one (1) year or due on demand; (b) the Trustee or a third party acting solely as agent for the Trustee has possession of the collateral; (c) the market value of the collateral (as determined at least once in every fourteen (14) days) exceeds the principal amount of the repurchase agreement plus accrued interest and the market value of the collateral is maintained at levels acceptable to Moody’s and to S&P; (d) failure to maintain the requisite collateral levels will require the Trustee to liquidate the collateral immediately; and (e) the repurchase agreement securities are free and clear of any third-party lien or claim; or (C) with financial institutions insured by the Federal Deposit Insurance Corporation or any broker-dealer with retail customers which falls under the jurisdiction of the Securities Investors Protection Corporation; provided, that: (a) the market value of the collateral (as determined at least once in every fourteen (14) days) exceeds the principal amount of the repurchase agreement plus accrued interest and the market value of the collateral is maintained at levels acceptable to Moody’s and to S&P; (b) the Trustee or a third party acting solely as agent for the Trustee has possession of the collateral; (c) the Trustee has a perfected first priority security interest in the collateral; (d) the collateral is free and clear of third-party liens and in the case of a Securities Investors Protection Corporation broker was not acquired pursuant to a repurchase agreement or reverse repurchase agreement; and (e) failure to maintain the requisite collateral percentage will require the Trustee to liquidate the collateral immediately;

(7) Certificates, notes, warrants, bonds or other evidence of indebtedness of the State of California or any local agencies therein which are rated in the highest short-term rating category or within one of the three highest long-term rating categories by Moody’s and by S&P (excluding securities that do not have a fixed par value and/or whose terms do not promise a fixed dollar amount at maturity or call date);

(8) For amounts less than one hundred thousand dollars (\$100,000), interest-bearing demand or time deposits (including certificates of deposit) in a nationally or state-chartered bank fully insured by the Federal Deposit Insurance Corporation, including the Trustee or any affiliate thereof, and of which an aggregate total of one hundred thousand dollars (\$100,000) is not exceeded in any one financial institution;

(9) Investments in units of a money-market fund portfolio that is rated in the highest letter and numerical rating category by Moody’s and by S&P (including funds for which the Trustee, its affiliates or subsidiaries provide investment advisory or other management services) and that is composed of direct obligations of, or on obligations guaranteed by, the full faith and credit of the United States of America or repurchase agreements collateralized by such obligations;

(10) a guaranteed investment contract with a financial institution or insurance company (or guaranteed by a financial institution or insurance company) which has at the date of execution thereof an outstanding issue of unsecured, uninsured and unguaranteed debt obligations or a claims paying ability rated within the two highest rating categories of any Rating Agency;

(11) Obligations approved in writing by Moody's and by S&P;

(12) The Local Agency Investment Fund or similar pooled fund operated by or on behalf of the State of California and which is authorized to accept investments by or on behalf of the City of the moneys held by the Trustee in any of the accounts or funds established pursuant to the Master Contract; and

(13) The California Asset Management Program (CAMP).

“Project” means any additions, betterments, extensions or improvements to the Water Utility System designated by the City Council of the City as a Project, the acquisition and construction of which (together with the incidental costs and expenses related thereto) is to be financed or refinanced by the proceeds of any Parity Obligation as provided therein.

“Qualified Counterparty” means a party (other than the City) who is the other party to a Payment Agreement and (1) (a) whose senior debt obligations are rated in one of the three (3) highest rating categories of each of the Rating Agencies then rating any Parity Obligations (without regard to any gradations within a rating category), or (b) whose obligations under the Payment Agreement are guaranteed for the entire term of the Payment Agreement by a bond insurer or other institution which has been, or whose debt service obligations have been, assigned a credit rating in one of the three highest rating categories of each of the Rating Agencies then rating any Parity Obligations, and (2) who is otherwise qualified to act as the other party to a Payment Agreement with the City under any applicable laws.

“Rate Stabilization Fund” means the fund by that name established pursuant to the Master Contract.

“Rating Agencies” means Moody's and S&P, and their respective successors or assigns, or any other nationally recognized securities rating agency or agencies rating any Parity Obligations at the Request of the City.

“RBI” means the Bond Buyer Revenue Bond Index or comparable index of long-term municipal obligations chosen by the City, or, if no comparable index can be obtained, eighty percent (80%) of the interest rate on actively traded thirty (30) year United States Treasury obligations.

“Request of the City” means an instrument in writing signed by the City Manager of the City, the Finance Director, or any other officer of the City duly authorized by the City Council for that purpose.

“Reserve Fund Requirement” means, as of any date of determination and excluding any Parity Obligations which are not Supplemental Contracts and the debt service thereon, the least of (a) ten percent (10%) of the initial offering price to the public of the Parity Obligations as determined under the Code, or (b) the Maximum Annual Debt Service, or (c) one hundred twenty-five percent (125%) of the Average Annual Debt Service, all as computed and determined by the City and

specified in writing to the Trustee; provided, that such requirement (or any portion thereof) may be provided by one or more policies of municipal bond insurance or surety bonds issued by a municipal bond insurer or by a letter of credit issued by a bank or other institution if the obligations insured by such insurer or issued by such bank or other institution, as the case may be, have ratings at the time of issuance of such policy or surety bond or letter of credit equal to “Aa” or higher assigned by Moody’s (if Moody’s is then rating any of the Parity Obligations) and “AA” or higher assigned by S&P (if S&P is then rating any of the Parity Obligations) and that maintain at all times ratings at least equal to the lowest ratings (without giving effect to municipal bond insurance or other credit enhancement) on any of the Parity Obligations provided by Moody’s (if Moody’s is then rating any of the Parity Obligations) and by S&P (if S&P is then rating any of the Parity Obligations). If at any time, obligations insured by any such municipal bond insurer issuing a policy of municipal bond insurance or surety bond or a bank or other institution issuing a letter of credit as permitted by this definition will no longer maintain such ratings as required in accordance with the immediately preceding sentence, the City will provide or cause to be provided cash or a substitute municipal bond insurance policy or surety bond or a letter of credit meeting such requirements.

“Revenue Fund” means the City of Modesto Water Utility System Revenue Fund established pursuant to the Master Contract.

“S&P” means Standard & Poor’s Ratings Services, a division of the McGraw Hill Companies, Inc., a corporation duly organized and existing under and by virtue of the laws of the State of New York, and its successors or assigns, except that if such entity will be dissolved or liquidated or will no longer perform the services of a municipal securities rating agency, then “S&P” will be deemed to refer to any other nationally recognized municipal securities rating agency rating Parity Obligations at the Request of the City.

“State” means the State of California.

“Subordinate Obligations” means obligations of the City authorized and executed by the City under applicable law, the payments under and pursuant to which are payable from Gross Revenues, subject and subordinate to payments under and pursuant to Parity Obligations and are payable from any fund established for the purpose of paying debt service on such Subordinate Obligations.

“Supplemental Contracts” means all installment purchase contracts of the City supplemental to the Master Contract and authorized and executed by the City under and pursuant to the Master Contract and applicable law, the installment payments under and pursuant to which are payable from Gross Revenues.

“Treatment and Delivery Agreement” means the Treatment and Delivery Agreement, by and among the City of Modesto, the Del Este Water Company, and the Modesto Irrigation District, which obligation is payable from the Gross Revenues on a parity with the Payments under the Master Contract and all Supplemental Contracts.

“Trust Agreements” means all trust agreements or indentures which are executed and delivered in connection with Parity Obligations, including the Trust Agreement.

“Trustee” means The Bank of New York Trust Company, N.A., a national banking association duly organized and existing under the laws of the United States of America, or any

association or corporation which may at any time be substituted in its place, as provided in the Trust Agreements.

“Special Counsel” will have the meaning given such term in the 2008 Trust Agreement.

“2008 Certificate Insurance Policy” means the municipal bond insurance policy issued by the 2008 Certificate Insurer guaranteeing the scheduled payments of principal of and interest evidenced and represented by the 2008 Certificates.

“2008 Certificate Insurer” means Assured Guaranty Corp., its successors and assigns.

“2008 Certificates” means the City of Modesto Water Refunding Revenue Certificates of Participation, 2008 Series A, evidencing and representing proportionate interests of the owners thereof in the 2008 Payments to be made by the City, executed and delivered pursuant to the 2008 Trust Agreement.

“2008 Interest Rate Swap Agreement” means, collectively, the ISDA Master Agreement (Local Currency–Single Jurisdiction 1992), the U.S. Municipal Counterparty Schedule thereto and a Credit Support Annex, each dated as of May 29, 2008, and an amended Confirmation, originally entered into on September 27, 2006, as amended as of May 29, 2008, between Bank of America, N.A., as a Qualified Counterparty, and the City.

“2008 Payment Date” means each Interest Payment Date and each day on which payments of principal evidenced and represented by the 2008 Certificates become due (whether at maturity or because of prepayment or acceleration).

“2008 Payments” means the Payments scheduled to be paid by the City under and pursuant to the terms of the 2008 Supplemental Contract.

“2008 Project” means the improvements to the Water Utility System to be refinanced with the proceeds of the 2008 Certificates, as shown on Exhibit A to the 2008 Supplemental Contract.

“2008 Supplemental Contract” means the 2008 Supplemental Installment Purchase Contract, dated as of May 1, 2008, by and between the City and the Authority, as originally executed and as it may from time to time be amended or supplemented in accordance with its terms.

“2008 Supplemental Contract Payment Account” means the account by that name within the Parity Obligation Payment Fund established pursuant to the 2008 Supplemental Contract.

“2008 Swap Insurance Policy” means the interest rate swap insurance policy issued by the 2008 Certificate Insurer guaranteeing certain payments due by the City under the 2008 Interest Rate Swap Agreement.

“2008 Tax Certificate” means the Tax Certificate concerning certain matters pertaining to the use and investment of proceeds of the 2008 Certificates executed and delivered by the City on the date of initial delivery of the 2008 Certificates, including any and all exhibits attached thereto.

“2008 Trust Agreement” means that certain Trust Agreement, dated as of May 1, 2008, by and between the Authority and the Trustee, delivered in connection with the 2008 Certificates.

“Variable Interest Rate” means any variable interest rate or rates to be paid under any Parity Obligations, the method of computing which variable interest rate will be as specified in the applicable Parity Obligation, which Parity Obligation will also specify either (i) the payment period or periods or time or manner of determining such period or periods or time for which each value of such variable interest rate will remain in effect, and (ii) the time or times based upon which any change in such variable interest rate will become effective, and which variable interest rate may, without limitation, be based on the interest rate on certain bonds or may be based on interest rate, currency, commodity or other indices.

“Variable Interest Rate Parity Obligations” means, for any period of time, any Parity Obligations that bear a Variable Interest Rate during such period, except that Parity Obligations will not be treated as Variable Interest Rate Parity Obligations if the net economic effect of interest rates on particular Payments or Parity Obligations and interest rates on other Payments of the same Supplemental Contract or Parity Obligations, as set forth in such Supplemental Contract or Parity Obligations, or the net economic effect of a Payment Agreement with respect to particular Parity Obligations, in either case is to produce obligations that bear interest at a fixed interest rate, and Supplemental Contracts with respect to which a Payment Agreement is in force will be treated as Variable Interest Rate Parity Obligations if the net economic effect of the Payment Agreement is to produce obligations that bear interest at a Variable Interest Rate, all in accordance with the definition of “Annual Debt Service” set forth in the Master Contract.

“Water Service” means the service furnished, made available or provided by the Water Utility System.

“Water Utility System” means (i) all property rights, contractual rights and facilities of the City relating to water, including all facilities, properties, structures or works for the treatment, conservation, storage, transmission or distribution of water now owned by the City; and (ii) all additions, betterments, extensions or improvements to such facilities, properties, structures or works or any part thereof hereafter acquired and constructed.

### **Acquisition, Construction and Sale of Projects; Funds**

Acquisition, Construction and Sale of Projects. Pursuant to the Master Contract, the Authority agrees to finance and refinance the costs of the acquisition and construction of the Projects for and to sell the Projects to the City, and in order to implement this provision, the Authority appoints the City as its agent for the purpose of such acquisition and construction, and the City agrees to enter into such construction contracts and purchase orders as may be necessary, as agent for the Authority, to provide for the complete acquisition and construction of the Projects.

The City agrees that as such agent it will cause the acquisition and construction of the Projects to be diligently completed after the deposit of funds in the Improvement Fund for such purpose pursuant to the Master Contract, and that it will use its best efforts to cause the acquisition and construction of the Projects to be completed in a timely fashion, unforeseeable delays beyond the reasonable control of the City only excepted, and, pursuant to the Master Contract, the Authority agrees to and sells the Projects to the City. Notwithstanding the foregoing, it is expressly understood and agreed that the Authority will be under no liability of any kind or character whatsoever for the payment of any costs or expenses incurred by the City for the acquisition and construction of the Projects and that all such costs and expenses will be paid by the City, regardless of whether the funds deposited in the Improvement Fund are sufficient to cover all such costs.

Improvement Fund. There is established under the Master Contract the City of Modesto Water Utility System Improvement Fund, which fund the City agrees to maintain until the completion of the acquisition and construction of the Projects to be funded from the separate accounts to be established in such fund as provided in the Supplemental Contracts.

Rate Stabilization Fund. There is established under the Master Contract a City of Modesto Water Utility System Rate Stabilization Fund, which fund the City agrees to maintain so long as any Parity Obligations remain unpaid. The City may deposit in the Rate Stabilization Fund any Gross Revenues, after providing for the payment of Parity Obligations and Maintenance and Operation Costs, and any other money received and available to be used therefor, provided that deposits from such Gross Revenues for each Fiscal Year may be made until (but not after) 180 days after the end of such Fiscal Year. The City may withdraw amounts from the Rate Stabilization Fund only for inclusion in Adjusted Annual Net Revenues, such withdrawal to be made until (but not after) 180 days after the end of such Fiscal Year. All interest or other earnings upon deposits in the Rate Stabilization Fund will be accounted for as Gross Revenues. Notwithstanding the foregoing, no Gross Revenues will be deposited in the Rate Stabilization Fund to the extent that such amount was included by the City in Adjusted Annual Net Revenues for purposes of determining compliance with certain provisions of the Master Contract relating to conditions for the execution of Parity Obligations or the rate covenant and deduction of the amounts to be deposited in the Rate Stabilization Fund would have caused noncompliance with such provisions.

Pledge of Gross Revenues; Revenue Fund. Pursuant to the Master Contract, all Gross Revenues of the Water Utility System are irrevocably pledged to the payment of the Payments, all payments required to be made by the City under all other Parity Obligations and the Maintenance and Operation Costs as provided in the Master Contract, and the Gross Revenues of the Water Utility System will not be used for any other purpose while any of the Payments remain unpaid; provided, however, that out of Gross Revenues there may be apportioned such sums for such purposes as are expressly permitted by the Master Contract. Such pledge constitutes a first pledge of and charge and lien upon the Gross Revenues of the Water Utility System for the payment of amounts due with respect to the Contracts, all other Parity Obligations and Maintenance and Operation Costs in accordance with the terms of the Master Contract.

In order to carry out and effectuate the obligation of the City contained in the Master Contract and in all Supplemental Contracts to pay the Payments, the City agrees and covenants that all Gross Revenues received by it will be deposited when and as received in the City of Modesto Water Utility System Revenue Fund, which fund is established under the Master Contract and which fund the City agrees and covenants to maintain separate and apart from other moneys of the City (subject to certain provisions of the Master Contract relating to investments) so long as any Parity Obligations remain unpaid, and all money on deposit in the Revenue Fund will be applied and used as follows. The City will pay at the following times in the following order of priority:

(a) Maintenance and Operation Costs and Parity Obligation Payment Fund Payments. The City will, from the money in the Revenue Fund, without preference or priority, and the event of any insufficiency of such moneys, ratably, without preference or priority, (i) pay charges for Maintenance and Operation Costs of the Water Utility System (including amounts reasonably required to be set aside in contingency reserves for Maintenance and Operation Costs the payment of which is not immediately required) as such charges are due and payable, and (ii) deposit in the City of Modesto Water Utility System Parity Obligation Payment Fund, which fund is established under the Master Contract and which fund the City agrees and covenants to maintain separate and apart

from other moneys of the City (subject to certain provisions of the Master Contract relating to investments) so long as any Parity Obligations remain unpaid, on the last Business Day of each month (1) an amount equal to the interest which has accrued or will accrue under all Parity Obligations during the next succeeding month calculated as if such interest has accrued or will accrue on a daily basis during such period, and (2) an amount equal to the principal which has accrued or will accrue (as a result of maturity, mandatory sinking fund payments or mandatory prepayment or otherwise) under all Parity Obligations during the next succeeding month calculated as if such principal has accrued or will accrue on a daily basis during such period, plus (3) the net payments due or which will be due on all Parity Payment Agreements calculated as if such net payments accrued or will accrue on a daily basis during such period, except that no such deposit need be made if the City then holds money in the Parity Obligation Payment Fund at least equal to the amount of interest and principal due or becoming due and payable under all Parity Obligations on the next succeeding date on which interest or principal becomes due and payable under any Parity Obligation plus the net payments due on all Parity Payment Agreements on such next succeeding due date therefor. Moneys on deposit in the Parity Obligation Payment Fund will be transferred by the City to make and satisfy the payments due on the next applicable date on which interest or principal becomes due and payable under any Parity Obligation or any net payment becomes due and payable by the City under any Parity Payment Agreement at least one Business Day prior to such next applicable due date.

Pursuant to the 2008 Supplemental Contract, there is established within the Parity Obligation Payment Fund a 2008 Supplemental Contract Payment Account to provide for the payment of the 2008 Payments. On or before the third Business Day immediately preceding each 2008 Payment Date or the date on which any net scheduled payment or insured termination payment is due under the 2008 Interest Rate Swap Agreement, the City will, from the money in the Parity Obligation Payment Fund, deposit in the 2008 Supplemental Contract Payment Account (i) a sum equal to the amount of the interest and principal components of the 2008 Payments becoming due and payable under the 2008 Supplemental Contract on the next succeeding 2008 Payment Date and (ii) the net scheduled payments and any insured termination payment, if applicable, due under the 2008 Interest Rate Swap Agreement, except that no such deposit need be made if the amount then on deposit in the 2008 Supplemental Contract Payment Account is at least equal to the amount of the interest and principal components of the 2008 Payments becoming due and payable under the 2008 Supplemental Contract on the next succeeding 2008 Payment Date plus the net scheduled payments and any insured termination payment, if applicable, due under the 2008 Interest Rate Swap Agreement on such next succeeding due date therefor. Moneys on deposit in the 2008 Supplemental Contract Payment Account will (i) be transferred by the City to the Trustee on the Business Day immediately preceding each 2008 Payment Date to make and satisfy the 2008 Payment due on such 2008 Payment Date and (ii) be transferred by the City to the Trustee on the due date therefor to satisfy the net scheduled payment and any insured termination payment, if applicable, due under the 2008 Interest Rate Swap Agreement, all in accordance with the Master Contract and the 2008 Trust Agreement.

(b) Parity Reserve Fund Deposits. On or before the last Business Day of each month, the City will, from the remaining money on deposit in the Revenue Fund after deposits and transfers pursuant to paragraph (a) above, transfer to the Trustee for deposit in the Parity Reserve Fund that sum, if any, necessary to restore the Parity Reserve Fund to an amount equal to the Reserve Fund Requirement. The City will also, from such remaining moneys in the Revenue Fund, transfer or cause to be transferred to the applicable reserve fund or account for any Parity Obligations for which a separate reserve has been funded pursuant to the Master Contract, without preference or priority between transfers made pursuant to this sentence and the preceding sentence, and in the event of any

insufficiency of such moneys ratably without any discrimination or preference, the sum or sums, if any, equal to the amount required to be deposited therein pursuant to such Parity Obligations.

After making the foregoing deposits and transfers required to be made, the City may apply any remaining money in the Revenue Fund for any lawful purpose of the City, including for the payment of any Subordinate Obligations in accordance with the instruments authorizing such Subordinate Obligations.

2008 Interest Rate Swap Agreement. Pursuant to the 2008 Supplemental Contract, the City and the Authority agree and acknowledge that the 2008 Interest Rate Swap Agreement (excluding the obligations thereunder to post collateral under certain circumstances and to make termination payments upon any early termination event or event of default except to the extent such termination payment is insured under the terms of the 2008 Swap Insurance Policy) constitutes a Parity Payment Agreement and a Parity Obligation payable solely from and secured by a pledge of Gross Revenues on a parity with all other existing and future Parity Obligations. The City and the Authority agree and acknowledge that obligations under the 2008 Interest Rate Swap Agreement to post collateral under certain circumstances or to make termination payments upon an early termination event or event of default under the 2008 Interest Rate Swap Agreement (other than to the extent such termination payment is insured under the terms of the 2008 Swap Insurance Policy) are Subordinate Obligations payable solely from and secured by a pledge of Gross Revenues on a subordinate basis to the Parity Obligations. Amounts payable by the City as a termination payment under the 2008 Interest Rate Swap Agreement upon an event of default with respect to the City thereunder and the designation of an early termination by the 2008 Certificate Insurer pursuant to the terms of the 2008 Interest Rate Swap Agreement (which payments are insured under the terms of the 2008 Swap Insurance Policy) constitute a Parity Obligation payable solely from and secured by a pledge of Gross Revenues on a parity with all other existing and future Parity Obligations. In the event any obligation of the City to post collateral or to make payments upon an early termination or event of default under the 2008 Interest Rate Swap Agreement constituting a Subordinate Obligation will arise, the City will establish a fund as necessary for the purpose of satisfying such obligation. As provided and on the dates under the Master Contract, the City will from the money in the Revenue Fund deposit in the 2008 Supplemental Contract Payment Account of the Parity Obligation Payment Fund a sum equal to the scheduled payments next due on the 2008 Interest Rate Swap Agreement. The City will not be required to advance any moneys derived from any source of income other than the Gross Revenues for the payments due under the 2008 Interest Rate Swap Agreement or for the performance of any agreements or covenants required to be performed by it contained in the 2008 Interest Rate Swap Agreement. The general fund of the City is not liable, and neither the faith and credit nor the taxing power of the City is pledged, for the payments under the 2008 Interest Rate Swap Agreement.

Investments. Any moneys held in the Revenue Fund or the Parity Obligation Payment Fund will be invested in Permitted Investments which will, as nearly as practicable, mature on or before the dates when such moneys are anticipated to be needed for disbursement under the Contracts. Any moneys held in the Rate Stabilization Fund will be invested in Permitted Investments which will mature at such dates as the City will determine but prior to the final date on which payments are due under any Outstanding Parity Obligation. All investment earnings from moneys or deposits in the Revenue Fund, the Parity Obligation Payment Fund and the Rate Stabilization Fund will be retained in such fund.

The City may commingle any of the funds or accounts (except for funds held in any rebate fund, which will be held separately) established pursuant to the Master Contract into a separate fund or funds for investment purposes only; provided however, that all funds or accounts held by the City under the Master Contract will be accounted for separately notwithstanding such commingling. For the purpose of determining the amount in any such fund or account, all Permitted Investments credited to such fund or account will, except as otherwise provided in the Master Contract, be valued at the lower of cost or market value (inclusive of all interest accrued but not paid).

### **Execution of Parity Obligations and Other Obligations**

Conditions for the Execution of Parity Obligations. The City may at any time execute any Parity Obligations the payments under and pursuant to which are payable from the Gross Revenues on a parity with the Payments due under all Supplemental Contracts; provided there will be on file with the Trustee either:

(1) A Certificate of the City demonstrating that during any twelve (12) consecutive calendar months out of the immediately preceding eighteen (18) calendar month period, the Adjusted Annual Net Revenues were at least equal to one hundred twenty-five percent (125%) of the Maximum Annual Debt Service for all existing Parity Obligations plus the Parity Obligations proposed to be executed; provided, that for the purpose of providing this Certificate, the City may adjust the foregoing Adjusted Annual Net Revenues to reflect:

(i) An allowance for Gross Revenues that would have been derived from each new connection to the Water Utility System that was made prior to the execution of such Parity Obligations but which, during all or any part of said twelve (12) month period, was not in existence, in an amount equal to the estimated additional Gross Revenues that would have been derived from each such connection if it had been made prior to the beginning of said twelve (12) month period, and

(ii) An allowance for Gross Revenues that would have been derived from any increase in the rates, fees and charges fixed and prescribed for Water Service which became effective prior to the execution of such Parity Obligations but which, during all or any part of said twelve (12) month period, was not in effect, in an amount equal to the estimated additional Gross Revenues that would have been derived from such increase in rates, fees and charges if it had been in effect prior to the beginning of said twelve (12) month period; or

(2) A Consultant's Report showing that the Adjusted Annual Net Revenues for the Fiscal Year next following the end of the period during which interest on the Parity Obligations proposed to be executed is to be capitalized or, if no interest is capitalized, the Fiscal Year in which the Parity Obligations proposed to be executed are executed, will be at least equal one hundred twenty-five percent (125%) of the Maximum Annual Debt Service; provided, that for the purpose of providing such Consultant's Report, the Independent Consultant may adjust the foregoing Adjusted Annual Net Revenues to reflect:

(i) An allowance for Gross Revenues that would have been derived from any increase in the rates, fees and charges prescribed for Water Service in effect and being charged, or rates, fees and charges for Water Service that are expected to be charged in accordance with a program of specific rates, fees, charges, rate levels or increases in overall Gross Revenues approved by a resolution of the City Council; and

(ii) An allowance for Gross Revenues from customers of the Water Utility System anticipated to be served by the facilities or improvements financed in substantial part by the Parity Obligations proposed to be executed together with any additional Parity Obligations expected to be executed prior to the Fiscal Year of determination.

Notwithstanding the foregoing provisions, there will be no limitations on the ability of the City to execute any Parity Obligation at any time to refund any Outstanding Parity Obligation.

Other Obligations. The City may incur Subordinate Obligations without meeting any of the tests set forth above.

### **Covenants of the City**

Compliance with Contracts. The City will punctually pay the Payments in strict conformity with the terms of the Master Contract, and will faithfully observe and perform all the agreements, conditions, covenants and terms contained in the Master Contract required to be observed and performed by it, and will not terminate the Contracts or fail to make any Payment required by the Contracts for any cause including, without limiting the generality of the foregoing, any acts or circumstances that may constitute failure of consideration, destruction of or damage to the Projects or the Water Utility System, commercial frustration of purpose, any change in the tax or other laws of the United States of America or of the State or any political subdivision of either or any failure of the Authority to observe or perform any agreement, condition, covenant or term contained in the Contracts required to be observed and performed by it, whether express or implied, or any duty, liability or obligation arising out of or connected with the Contracts or the insolvency, or deemed insolvency, or bankruptcy or liquidation of the Authority or any force majeure, including acts of God, tempest, storm, earthquake, war, rebellion, riot, civil disorder, acts of public enemies, blockade or embargo, strikes, industrial disputes, lockouts, lack of transportation facilities, fire, explosion, or acts or regulations of governmental authorities.

Use of Proceeds. The Authority and the City agree that the proceeds of the Contracts will be used by the City, as agent for the Authority, to pay the costs of financing or refinancing the acquisition and construction of the Projects and to pay the incidental costs and expenses related thereto as provided in the Contracts.

Against Encumbrances. The City will pay or cause to be paid when due all sums of money that may become due or purporting to be due for any labor, services, materials, supplies or equipment furnished, or alleged to have been furnished, to or for the City in, upon, about or relating to the Water Utility System and will keep the Water Utility System free of any and all liens against any portion of the Water Utility System. In the event any such lien attaches to or is filed against any portion of the Water Utility System, the City will cause each such lien to be fully discharged and released at the time the performance of any obligation secured by any such lien matures or becomes due, except that if the City desires to contest any such lien it may do so if contesting such lien will not materially impair operation of the Water Utility System. If any such lien will be reduced to final judgment and such judgment or any process as may be issued for the enforcement thereof is not promptly stayed, or if so stayed and such stay thereafter expires, the City will forthwith pay or cause to be paid and discharged such judgment. The City will, to the maximum extent permitted by law, indemnify and hold the Authority harmless from, and defend it against, any claim, demand, loss, damage, liability or expense (including attorneys' fees) as a result of any such lien or claim of lien against any portion of the Water Utility System.

Sale or Other Disposition of Property. The City will not sell, transfer or otherwise dispose of any of the works, plant, properties, facilities or other part of the Water Utility System or any real or personal property comprising a part of the Water Utility System if such sale, transfer or disposition would cause the City to be unable to meet the requirements of the rate covenant set forth in the Master Contract.

Prompt Acquisition and Construction of the Projects. The City will take all necessary and appropriate steps to acquire and construct the Projects, with all practicable dispatch and in an expeditious manner and in conformity with law so as to complete the same in a timely fashion.

Maintenance and Operation of the Water Utility System; Budgets. The City will maintain and preserve the Water Utility System in good repair and working order at all times and will operate the Water Utility System in an efficient and economical manner and will pay all Maintenance and Operation Costs as they become due and payable. The City will adopt and file with the Authority, not later than October 1 of each year, a budget approved by the City Council setting forth the estimated Maintenance and Operation Costs for the then current Fiscal Year and will take such action as may be necessary to include all Payments required to be made under the Contracts in its annual budget; provided, that any such budget may be amended at any time during any Fiscal Year and such amended budget will be filed by the City with the Authority.

Compliance with Contracts for Use of the Water Utility System. The City will comply with, keep, observe and perform all agreements, conditions, covenants and terms, express or implied, required to be performed by it contained in all contracts for the use of the Water Utility System and all other contracts affecting or involving the Water Utility System to the extent that the City is a party thereto.

Insurance. The City will procure and maintain such insurance relating to the Water Utility System which it will deem advisable or necessary to protect its interests and the interests of the Authority, which insurance will afford protection in such amounts and against such risks as are usually covered in connection with water systems similar to the Water Utility System; provided, that any such insurance may be maintained under a self-insurance program so long as such self-insurance is maintained in the amounts and manner as is, in the opinion of an accredited actuary, actuarially sound. All policies of insurance required to be maintained under the Master Contract will provide that the Authority will be given thirty (30) days, written notice of any intended cancellation thereof or reduction of coverage provided thereby.

#### **Accounting Records; Financial Statements and Other Reports.**

(a) The City will keep appropriate accounting records in which complete and correct entries will be made of all transactions relating to the Water Utility System, which records will be available for inspection by the Authority at reasonable hours and under reasonable conditions.

(b) The City will prepare and file with the Authority annually within one hundred eighty (180) days after the close of each Fiscal Year:

(1) financial statements of the City for such Fiscal Year prepared in accordance with Generally Accepted Accounting Principles, together with an Accountant's Report thereon and a special report prepared by the Independent Certified Public Accountant who examined such financial statements stating that nothing came to its attention in connection with such examination that caused

it to believe that the City was not in compliance with any of the agreements or covenants contained in the Master Contract; and

(2) a detailed report as to all insurance policies maintained and self-insurance programs maintained by the City with respect to the Water Utility System as of the close of such Fiscal Year, including the names of the insurers which have issued the policies and the amounts thereof and the property or risks covered thereby.

Protection of Security and Rights of the Authority. The City will preserve and protect the security of the Payments under the Contracts and the rights of the Authority to the Payments under the Contracts and will warrant and defend such rights against all claims and demands of all persons.

Payment of Taxes and Compliance with Governmental Regulations. The City will pay and discharge all taxes, assessments and other governmental charges which may hereafter be lawfully imposed upon the Water Utility System or any part thereof when the same will become due. The City will duly observe and conform with all valid regulations and requirements of any governmental authority relative to the operation of the Water Utility System or any part thereof, but the City will not be required to comply with any regulations or requirements so long as the validity or application thereof will be contested in good faith and contesting such validity or application will not materially impair operation of the Water Utility System.

Amount of Rates, Fees and Charges. The City will at all times fix, prescribe and collect rates, fees and charges for the Water Service during each Fiscal Year which are reasonably fair and nondiscriminatory and which will be at least sufficient to yield Adjusted Annual Net Revenues for such Fiscal Year equal to at least 125% of Annual Debt Service to be paid during the Fiscal Year.

Collection of Rates, Fees and Charges. The City will have in effect at all times rules and regulations requiring each consumer or customer located on any premises connected with the Water Utility System to pay the rates, fees and charges applicable to the Water Service to such premises and providing for the billing thereof and for a due date and a delinquency date for each bill. The City will not permit any part of the Water Utility System or any facility thereof to be used or taken advantage of free of charge by any corporation, firm or person, or by any public agency (including the United States of America, the State of California and any city, county, district, political subdivision, public corporation or agency of any thereof); provided, that the City may without charge use the Water Service.

Eminent Domain and Insurance Proceeds. If all or any part of the Water Utility System will be taken by eminent domain proceedings, or if the City receives any insurance proceeds resulting from a casualty loss to the Water Utility System, the Net Proceeds thereof, at the option of the City, will be applied either to the proportional prepayment of Outstanding Parity Obligations or will be used to substitute other components for the condemned or destroyed components of the Water Utility System.

Tax Covenants. Pursuant to the 2008 Supplemental Contract, the City covenants it will not take any action, or fail to take any action, if any such action or failure to take action would adversely affect the exclusion from gross income of the portion of the 2008 Payments constituting interest under Section 103 of the Code. The City will not, directly or indirectly, use or permit the use of proceeds of the 2008 Supplemental Contract or any of the property financed or refinanced with proceeds of the 2008 Supplemental Contract, or any portion thereof, by any person other than a

governmental unit (as such term is used in Section 141 of the Code), in such manner or to such extent as would result in the loss of exclusion from gross income for federal income tax purposes of the portion of the 2008 Payments constituting interest.

The City will not take any action, or fail to take any action, if any such action or failure to take action would cause any obligations delivered in connection with the 2008 Supplemental Contract to be “private activity bonds” within the meaning of Section 141 of the Code, and in furtherance thereof, will not make any use of the proceeds of the 2008 Supplemental Contract or any of the property financed or refinanced with proceeds of the 2008 Supplemental Contract, or any portion thereof, or any other funds of the City, that would cause any of the 2008 Certificates on other obligations delivered in connection with the 2008 Supplemental Contract to be “private activity bonds” within the meaning of Section 141 of the Code. To that end, so long as any 2008 Payments are unpaid, the City, with respect to such proceeds and property and such other funds, will comply with applicable requirements of the Code and all regulations of the United States Department of the Treasury issued thereunder to the extent such requirements are, at the time, applicable and in effect. The City will establish reasonable procedures necessary to ensure continued compliance with Section 141 of the Code and the continued qualification of any obligations delivered in connection with the 2008 Supplemental Contract as “governmental bonds.”

The City will not, directly or indirectly, use or permit the use of any proceeds of the 2008 Supplemental Contract, or of any property financed or refinanced thereby, or other funds of the City, or take or omit to take any action, that would cause any obligations delivered in connection with the 2008 Supplemental Contract to be “arbitrage bonds” within the meaning of Section 148 of the Code. To that end, the City will comply with all requirements of Section 148 of the Code and all regulations of the United States Department of the Treasury issued thereunder to the extent such requirements are, at the time, in effect and applicable to the 2008 Supplemental Contract.

The City will not make any use of the proceeds of the 2008 Supplemental Contract or any other funds of the City, or take or omit to take any other action, that would cause the 2008 Supplemental Contract to be “federally guaranteed” within the meaning of Section 149(b) of the Code.

In furtherance of the foregoing tax covenants, the City covenants that it will comply with the provisions of the 2008 Tax Certificate. Such covenants will survive payment in full or discharge of the 2008 Certificates and the 2008 Payments.

The Authority and the City covenant that, in the event of any change in the 2008 Trust Agreement, the 2008 Supplemental Contract or other relevant documents relating to the 2008 Certificates, or any other actions taken or omitted by the City or the Authority, upon the advice or with the approving opinion of Special Counsel other than Sidley Austin LLP, Special Counsel in connection with the original execution and delivery of the 2008 Certificates, the Authority and the City will, upon the making of any such change, or the taking or omission of any such other action, cause to be delivered an opinion of Special Counsel (together with a reliance letter thereon addressed to the 2008 Certificate Insurer and the Trustee) nationally recognized in the area of municipal bonds to the effect that the portion of each 2008 Payment due under the 2008 Supplemental Contract designated as and comprising interest with respect to the 2008 Certificates is excluded from gross income for federal income tax purposes.

Continuing Disclosure. Pursuant to the 2008 Supplemental Contract, the City covenants and agrees that it will comply with and carry out all of its obligations under the Continuing Disclosure Agreement delivered in connection with the execution and delivery of the 2008 Certificates. Notwithstanding any other provision of the Master Contract or hereof, failure of the City to comply with the Continuing Disclosure Agreement will not be considered an Event of Default under the Master Contract or the 2008 Supplemental Contract.

Further Assurances. The City will adopt, deliver, execute and make any and all further assurances, instruments and resolutions as may be reasonably necessary or proper to carry out the intention or to facilitate the performance of the Contracts and for the better assuring and confirming unto the Authority of the rights and benefits provided to it in the Contracts.

### **Events of Default and Remedies**

Events of Default and Acceleration of Principal. If one or more of the following Events of Default will happen, that is to say:

(1) if default will be made in the due and punctual payment of any payment on any Parity Obligation when and as the same will become due and payable;

(2) if default will be made by the City in the performance of any of the agreements or covenants contained in the Master Contract or in any Parity Obligation required to be performed by it, and such default will have continued for a period of sixty (60) days after the City will have been given notice in writing of such default by the Authority; or

(3) if the City will file a petition or answer seeking arrangement or reorganization under the federal bankruptcy laws or any other applicable law of the United States of America or any state therein, or if a court of competent jurisdiction will approve a petition filed with or without the consent of the City seeking arrangement or reorganization under the federal bankruptcy laws or any other applicable law of the United States of America or any state therein, or if under the provisions of any other law for the relief or aid of debtors any court of competent jurisdiction will assume custody or control of the City or of the whole or any substantial part of its property;

then and in each and every such case during the continuance of such Event of Default specified in clause (1) above, the Authority will, and for any other such Event of Default the Authority may, by notice in writing to the City, declare the entire principal amount of the unpaid Payments and the accrued interest thereon to be due and payable immediately, and upon any such declaration the same will become immediately due and payable, anything contained in the Master Contract to the contrary notwithstanding. The foregoing provision is subject to the condition, however, that if at any time after the entire principal amount of the unpaid Payments and the accrued interest thereon will have been so declared due and payable and before any judgment or decree for the payment of the money due will have been obtained or entered the City will deposit with the Authority a sum sufficient to pay the unpaid principal amount of the Payments or the unpaid principal amount of any payments under any Parity Obligation referred to in clause (i) above due and payable prior to such declaration and the accrued interest thereon, with interest on such overdue installments at the rate or rates applicable to such unpaid principal amounts of the Payments if paid in accordance with their terms, and the reasonable expenses of the Authority, and any and all other defaults known to the Authority (other than in the payment of the entire principal amount of the unpaid Payments and the accrued interest thereon due and payable solely by reason of such declaration) will have been made good or

cured to the satisfaction of the Authority or provision deemed by the Authority to be adequate will have been made therefor, then and in every such case the Authority, by written notice to the City, may rescind and annul such declaration and its consequences; but no such rescission and annulment will extend to or will affect any subsequent default or will impair or exhaust any right or power consequent thereon.

Application of Gross Revenues upon Acceleration. All Gross Revenues upon the date of the declaration of acceleration by the Authority as provided in the Master Contract and all Gross Revenues thereafter received will be applied in the following order:

First, to the payment of the costs and expenses of the Authority, if any, in carrying out the provisions of the Master Contract relating to Events of Default and acceleration of principal, including reasonable compensation to its agents, accountants and counsel and including any indemnification expenses; and

Second, to the payment of the Maintenance and Operation Costs of the Water Utility System and the payment of the entire principal amount of the unpaid Parity Obligations, and the accrued interest thereon, with interest on the overdue principal and interest amounts of the unpaid Parity Obligations at the rate or rates of interest then applicable to such Parity Obligations if paid in accordance with their terms, provided that if the amount available will not be sufficient to pay in full all such amounts then due and payable, then to the payment thereof ratably, according to the amounts due thereon without any discrimination or preference.

Gross Revenues may also be applied to make payments required under any Parity Payment Agreement on a parity with the payments under paragraph Second above, to the extent and in the manner provided by the terms of such Parity Obligation relating to such Parity Payment Agreement.

Other Remedies. The Authority will have the right:

(a) by mandamus or other action or proceeding or suit at law or in equity to enforce its rights against the City or any director, officer or employee thereof, and to compel the City or any such director, officer or employee to perform and carry out its or his duties under the law and the agreements and covenants required to be performed by it or him contained in the Contracts;

(b) by suit in equity to enjoin any acts or things which are unlawful or violate the rights of the Authority; or

(c) by suit in equity upon the happening of an Event of Default to require the City and its directors, officers and employees to account as the trustee of an express trust.

Non-Waiver. Nothing in the Master Contract will affect or impair the obligation of the City, which is absolute and unconditional, to pay the Payments from the Gross Revenues to the Authority at the respective due dates or upon acceleration or prepayment, or will affect or impair the right of the Authority, which is also absolute and unconditional, to institute suit to enforce such payment by virtue of the contract embodied in the Contracts.

A waiver of any default or breach of duty or contract by the Authority will not affect any subsequent default or breach of duty or contract or impair any rights or remedies on any such subsequent default or breach of duty or contract. No delay or omission by the Authority to exercise

any right or remedy accruing upon any default or breach of duty or contract will impair any such right or remedy or will be construed to be a waiver of any such default or breach of duty or contract or an acquiescence therein, and every right or remedy conferred upon the Authority by law or by the Master Contract may be enforced and exercised from time to time and as often as will be deemed expedient by the Authority.

If any action, proceeding or suit to enforce any right or exercise any remedy is abandoned or determined adversely to the Authority, the City and the Authority will be restored to their former positions, rights and remedies as if such action, proceeding or suit had not been brought or taken.

Remedies Not Exclusive. No remedy in the Master Contract conferred upon or reserved to the Authority is intended to be exclusive of any other remedy, and each such remedy will be cumulative and will be in addition to every other remedy given under the Master Contract or now or hereafter existing in law or in equity or by statute or otherwise and may be exercised without exhausting and without regard to any other remedy conferred by law.

### **Discharge of Obligations**

(a) If the City will pay or cause to be paid all the Payments at the times and in the manner provided in the Master Contract, the right, title and interest of the Authority in the Master Contract and the obligations of the City under the Master Contract and under all Supplemental Contracts will cease, terminate, become void and be completely discharged and satisfied.

(b) Any unpaid principal installment of any of the Payments will on its payment date or date of prepayment be deemed to have been paid within the meaning of and with the effect expressed in subsection (a) above if the City makes payment of such Payment and the prepayment premium, if applicable, in the manner provided in the Master Contract.

(c) All or any portion of unpaid principal installments of the Payments will, prior to their payment dates or dates of prepayment, be deemed to have been paid within the meaning of and with the effect expressed in subsection (a) above if (i) there will have been deposited with the Trustee either money in an amount which will be sufficient, or Federal Securities which are not subject to redemption except by the holder thereof prior to maturity (including any such securities issued or held in book-entry form) or municipal obligations which have been defeased under irrevocable escrow instructions with Federal Securities and which are rated in the highest rating category by the Rating Agencies, the interest on and principal of which when paid will provide money which, together with money, if any, deposited with the Trustee, will be sufficient (as evidenced by a report of an Independent Certified Public Accountant regarding such sufficiency) to pay when due the principal installments of such Payments or such portions thereof on their payment dates or their dates of prepayment, as the case may be, the interest installments of such Payments due on and prior to such payment dates or dates of prepayment, and the prepayment premiums, if any, applicable thereto, and (ii) an Opinion of Counsel is filed with the Trustee to the effect that the action taken pursuant to this subsection will not cause the interest installments of such Payments so paid to be includable in gross income under the Code for federal income tax purposes.

(d) After the payment of all Payments and prepayment premiums, if any, as provided in this section, and payment in full of all fees and expenses of the Authority, the Authority, upon request of the City, will cause an accounting for such period or periods as may be requested by the City to be prepared and filed with the City and the Authority, and will execute and deliver to the City

all such instruments as may be necessary or desirable to evidence such total discharge and satisfaction of the Contracts, and the Authority will pay over and deliver to the City, as an overpayment of Payments, all such money or investments held by it pursuant to the Master Contract other than such money and such investments as are required for the payment or prepayment of the Payments and interest installments of such Payments and the prepayment premiums, if any, applicable thereto, which money and investments will continue to be held in trust for the payment of the Payments.

### **Liability of City Limited to Gross Revenues**

Notwithstanding anything contained in Contracts, the City will not be required to advance any moneys derived from any source of income other than the Gross Revenues for the payment of the Payments or for the performance of any agreements or covenants required to be performed by it contained in the Master Contract. The City may, however, advance moneys for any such purpose so long as such moneys are derived from a source legally available for such purpose and may be legally used by the City for such purpose.

The obligation of the City to make the Payments is a special obligation of the City payable solely from the Gross Revenues as provided in the Master Contract. The general fund of the City is not liable, and neither the credit nor taxing power of the City is pledged, for the payment of the Payments under the Contracts or any other payments required to be made by the City under other Parity Obligations.

## **THE TRUST AGREEMENT**

Certain provisions of the Trust Agreement are summarized below. THIS SUMMARY DOES NOT PURPORT TO BE COMPLETE OR DEFINITIVE AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO THE FULL TERMS OF THE TRUST AGREEMENT.

### **Definitions**

The following are summaries of definitions of certain terms from the Trust Agreement used in this Summary of Principal Legal Documents or elsewhere in this Official Statement.

“Alternate Liquidity Facility” means a letter of credit, line of credit, surety bond, standby purchase agreement or other security or liquidity instrument, as the case may be, approved by the 2008 Certificate Insurer and issued in accordance with the terms hereof with respect to the 2008 Certificates as a replacement or substitute for any Liquidity Facility then in effect.

“Authority” means the Modesto Public Financing Authority, a joint exercise of powers authority duly organized and existing under and by virtue of the laws of the State.

“Authorized Denominations” means (i) with respect to 2008 Certificates in a Daily Mode or Weekly Mode, \$100,000 and any integral multiple of \$5,000 in excess thereof; (ii) with respect to 2008 Certificates in a Flexible Mode, \$100,000 and any integral multiple of \$1,000 in excess thereof; and (iii) with respect to 2008 Certificates in a Term Rate Mode or Fixed Rate Mode, \$5,000 and any integral multiple thereof.

“Automatic Termination Event” means an event of default set forth in a Reimbursement Agreement between the Authority and a Liquidity Facility Provider which would result in the

immediate termination of the Liquidity Facility provided pursuant to such Reimbursement Agreement prior to its stated expiration date without prior notice from the Liquidity Facility Provider to the Trustee.

“Book-Entry System” means a system under which physical certificates in fully registered form are registered only in the name of a Securities Depository or its nominee.

“Business Day” means any day other than (i) a Saturday or Sunday or (ii) a day on which the Trustee is required or authorized to be closed or (iii) a day on which the office of the applicable Credit Enhancement Provider at which draws or advances will be paid is required or authorized to be closed or (iv) a day on which The New York Stock Exchange is closed.

“Certificate of the Authority” means an instrument in writing signed by the Auditor and Treasurer of the Authority or by any other officer of the Authority duly authorized by the Authority for that purpose.

“Certificate Payment Date” means, with respect to any 2008 Certificate, the Certificate Payment Date designated therein, which is the October 1 on which or, in the case of 2008 Certificates subject to mandatory sinking fund prepayment, by which, the principal component of the final 2008 Payment evidenced and represented thereby will become due and payable.

“City” means the City of Modesto, a charter city and municipal corporation, duly organized and existing under and by virtue of the Constitution and laws of the State.

“Code” means the Internal Revenue Code of 1986, and the regulations issued thereunder, as the same may be amended from time to time, and any successor provisions of law. Reference to a particular section of the Code will be deemed to be a reference to any successor to any such section.

“Contract” means that certain Master Contract, as supplemented by the 1997 Supplemental Contract and the 2008 Supplemental Contract, and as otherwise amended or supplemented from time to time.

“Corporate Trust Office” means the corporate trust office of the Trustee in San Francisco, California, or such other office as may be specified by written notice from the Trustee to the Authority.

“Costs of Issuance” means all items of expense directly or indirectly payable by or reimbursable to the City or the Authority and related to the authorization, execution and delivery of the 2008 Supplemental Contract and the Trust Agreement and the execution, sale and delivery of the 2008 Certificates, including, but not limited to, costs of preparation and reproduction of documents, costs of rating agencies and costs to provide information required by rating agencies, filing and recording fees, initial fees and charges of the Trustee and its counsel, legal fees and charges, fees and disbursements of consultants and professionals, fees and expenses of the underwriter, fees and charges for preparation, execution and safekeeping of the 2008 Certificates, fees of the Liquidity Facility Provider, fees of the Authority and any other cost, charge or fee in connection with the original execution and delivery of the 2008 Certificates.

“Costs of Issuance Fund” means the fund by that name established pursuant to the Trust Agreement.

“Credit Enhancement Provider” means the 2008 Certificate Insurer.

“Daily Mode” means the Mode during which the 2008 Certificates evidence interest at the Daily Rate.

“Daily Rate” means the per annum interest rate with respect to the 2008 Certificates in the Daily Mode determined pursuant to the Trust Agreement.

“Daily Rate Period” means the period during which the 2008 Certificates in the Daily Mode will evidence interest at a Daily Rate, which will be from the Business Day upon which a Daily Rate is set to but not including the next succeeding Business Day.

“Delivery Date” means May 30, 2008.

“Event of Default” means an event described in the Trust Agreement.

“Expiration Date” means the stated expiration date of a Liquidity Facility, as it may be extended from time to time as provided in such Liquidity Facility, or any earlier date on which such Liquidity Facility will terminate at the direction of the Authority, expire or be cancelled (other than the date on which a Liquidity Facility will terminate as a result of an Automatic Termination Event or an event of default under the Reimbursement Agreement entered into in connection with such Liquidity Facility).

“Favorable Opinion of Special Counsel” means, with respect to any action the occurrence of which requires such an opinion, an Opinion of Special Counsel, addressed to the Trustee, to the effect that the action proposed to be taken will not, in and of itself, adversely affect any exclusion from gross income of interest with respect to the 2008 Certificates.

“Federal Securities” shall have the meaning ascribed thereto in the Contract.

“Fiscal Year” means the period beginning on July 1 of each year and ending on the next succeeding June 30, or any other annual accounting period hereafter selected and designated by the Authority as its Fiscal Year.

“Fixed Rate” means the per annum interest rate or interest rates evidenced by the 2008 Certificates in a Fixed Rate Mode determined pursuant to the Trust Agreement.

“Fixed Rate Mode” means the Mode during which the 2008 Certificates evidence interest at a Fixed Rate.

“Fixed Rate Period” means, with respect to 2008 Certificates converted to the Fixed Rate Mode, the period from the Mode Change Date upon which the 2008 Certificates were converted to a Fixed Rate Mode to but not including the Maturity Date.

“Flexible Mode” means the Mode during which the 2008 Certificates evidence interest at Flexible Rates.

“Flexible Rate” means, with respect to the 2008 Certificates in a Flexible Mode, the per annum interest rate determined for the 2008 Certificate pursuant to the Trust Agreement.

“Flexible Rate Certificates” means the 2008 Certificates in a Flexible Mode.

“Flexible Rate Period” means, with respect to the 2008 Certificates in a Flexible Mode, the period of from 1 to 397 calendar days (which Flexible Rate Period must end on a day preceding a Business Day) during which a Flexible Rate Certificate will evidence interest at a Flexible Rate, as established by the Remarketing Agent pursuant to the Trust Agreement.

“Improvement Fund” means the fund by that name established pursuant to the Contract.

“Independent Certified Public Accountant” means any certified public accountant or firm of such accountants duly licensed and entitled to practice and practicing as such under the laws of the State, appointed and paid by the Authority, and who, or each of whom:

(1) is in fact independent according to the Statement of Auditing Standards No. 1 and not under the domination of the Authority;

(2) does not have a substantial financial interest, direct or indirect, in the operations of the Authority; and

(3) is not connected with the Authority as a member, officer or employee of the Authority, but who may be regularly retained to audit the accounting records of and make reports thereon to the Authority.

“Information Services” means Financial Information, Inc.’s “Daily Called Bond Service,” 30 Montgomery Street, 10th Floor, Jersey City, New Jersey 07302, Attention: Editor; FIS/Mergent, Inc., 5250 77 Center Drive, Suite 150, Charlotte, North Carolina 28217, Attn: Call Notification; Standard & Poor’s Securities Evaluation, Inc., 55 Water Street, 45th Floor, New York, New York 10041, Attention: Notification Department; Xcitek, 5 Hanover Square, New York, New York 10004; and, in accordance with then current guidelines of the Securities and Exchange Commission, such other addresses and/or such other services providing information with respect to the redemption of bonds or the prepayment of certificates of participation as the Authority may designate in a Certificate of the Authority filed with the Trustee.

“Interest Payment Date” means each date on which interest is to be paid and is: (i) with respect to the 2008 Certificates in a Daily Mode or a Weekly Mode, the first Business Day of each month; (ii) with respect to the 2008 Certificates in a Flexible Mode, each Mandatory Purchase Date applicable thereto; (iii) with respect to the 2008 Certificates in a Fixed Rate Mode or a Term Rate Mode, the first day of April or October, which is at least 3 months after the month in which such Long-Term Mode takes effect, and the first day of each April and October thereafter or, upon the receipt by the Trustee of a Favorable Opinion of Special Counsel, any other six-month interval chosen by the Authority (beginning with the first such day which is at least three months after the Mode Change Date) and, with respect to a Term Rate Mode, the final day of the current Interest Period if other than a regular six-month interval; (iv) (without duplication as to any Interest Payment Date listed above) any Mode Change Date, other than a change between a Daily Mode and a Weekly Mode, and each Maturity Date; and (v) with respect to any Liquidity Provider Certificates, the day set forth in the applicable Reimbursement Agreement.

“Interest Period” means, for the 2008 Certificates in a particular Mode, the period of time that the 2008 Certificates evidence interest at the rate (per annum) which becomes effective at the

beginning of such period, and will include a Daily Rate Period, a Weekly Rate Period, a Flexible Rate Period, a Term Rate Period, and a Fixed Rate Period.

“Liquidity Facility” means, initially, the Stand-by Certificate Purchase Agreement, dated as of May 1, 2008, between the Authority and Bank of America, N.A., and any future line of credit, letter of credit, standby purchase agreement or other instrument, if any, which provides for the payment of the purchase price of the 2008 Certificates upon the tender thereof in the event remarketing proceeds are insufficient therefor.

“Liquidity Facility Provider” means, initially, Bank of America, N.A., and any future bank, insurance company, pension fund or other financial institution acceptable to the 2008 Certificate Insurer which provides a Liquidity Facility or Alternate Liquidity Facility for the 2008 Certificates.

“Liquidity Provider Certificates” means any 2008 Certificates purchased by a Liquidity Facility Provider with funds drawn on or advanced under the Liquidity Facility provided by such Liquidity Facility Provider.

“Mandatory Purchase Date” means (i) with respect to a Flexible Rate Certificate, the first Business Day following the last day of each Flexible Rate Period with respect to such Flexible Rate Certificate; (ii) for the 2008 Certificates in a Term Rate Mode, the first Business Day following the last day of each Term Rate Period for such 2008 Certificates; (iii) any Mode Change Date; (iv) any Substitution Date; (v) the fifth Business Day prior to an Expiration Date; (vi) the date specified by the Trustee following the occurrence of an event of default with respect to the Liquidity Facility which requires or gives the Liquidity Facility Provider the option to terminate the Liquidity Facility upon notice and requires that all Outstanding 2008 Certificates secured by such Liquidity Facility be tendered for purchase under the applicable Reimbursement Agreement, which date shall be a Business Day not less than 20 days after the Trustee’s receipt of notice of such event of default from the applicable Liquidity Facility Provider and in no event later than the Business Day preceding the termination date specified in the notice of event of default delivered to the Trustee by such Liquidity Facility Provider; and (vii) for the 2008 Certificates in a Daily Mode or a Weekly Mode, any Business Day specified by the Authority in a notice delivered to the Trustee, which Mandatory Purchase Date shall be not less than twenty (20) days after the Trustee’s receipt of such notice from the Authority.

“Master Contract” means that certain Master Installment Purchase Contract, executed and entered into as a November 1, 1997, by and between the City and the Authority, as the same may be amended or supplemented from time to time.

“Maturity Date” means, with respect to the 2008 Certificates, the maturity date specified for the 2008 Certificates in the Trust Agreement or, if Serial Certificates or more than one Term Certificates are established for the 2008 Certificates pursuant to the Trust Agreement upon a change of the 2008 Certificates to a Fixed Rate Mode, the maturity dates established for such Serial Certificates or Term Certificates.

“Maximum Rate” or “Maximum Interest Rate” means, with respect to all 2008 Certificates other than Liquidity Provider Certificates, a rate of interest of 12% per annum, and with respect to Liquidity Provider Certificates, such rate not greater than 25% as is provided for in the applicable Liquidity Facility; provided, however, that such rate will not in any event exceed the highest rate then permitted by law.

“Mode” means, as the context may require, the Daily Mode, the Weekly Mode, the Flexible Mode, the Term Rate Mode, or the Fixed Rate Mode.

“Mode Change Date” means with respect to the 2008 Certificates in a particular Mode, the day on which another Mode for the 2008 Certificates begins.

“Moody’s” means Moody’s Investors Service Inc., a corporation duly organized and existing under and by virtue of the laws of the State of Delaware, and its successors or assigns, except that if such corporation will be dissolved or liquidated or will no longer perform the services of a municipal securities rating agency, then “Moody’s” will be deemed to refer to any other nationally recognized municipal securities rating agency selected by the Authority.

“1997 Certificates” means the \$25,585,000 Refunding Revenue Certificates of Participation (1997 Water Utility System Refinancing Project), evidencing and representing and proportionate interests of the owners thereof in the 1997 Payments to be made by the City.

“1997 Payments” means the installment payments required to be made by the City to the Authority under and pursuant to the 1997 Supplemental Contract.

“1997 Supplemental Contract” means the 1997 Supplemental Installment Purchase Contract, executed and entered into as of November 1, 1997, by and between the City and the Authority, supplementing the Master Contract.

“1997 Trust Agreement” means that certain Trust Agreement, dated as of November 1, 1997, by and between the Authority and State Street Bank and Trust Company, N.A., which has been succeeded by The Bank of New York Trust Company, N.A., as trustee, pursuant to which there was executed and delivered the 1997 Certificates.

“Notice Parties” means the Authority, the City, the Trustee, the Credit Enhancement Provider, if any, the Liquidity Facility Provider, if any, the Remarketing Agent, if any, and the Fixed Rate Remarketing Agent, if any.

“Opinion of Counsel” means a written opinion of counsel of recognized standing in the field of law being addressed in such opinion retained the Authority.

“Outstanding” when used as of any particular time with reference to 2008 Certificates, means (subject to the provisions of the Trust Agreement) all 2008 Certificates except (1) 2008 Certificates theretofore cancelled by the Trustee or surrendered to the Trustee for cancellation; (2) 2008 Certificates paid or deemed to have been paid within the meaning of the Trust Agreement; and (3) 2008 Certificates in lieu of or in substitution for which other 2008 Certificates will have been executed and delivered by the Trustee pursuant to the Trust Agreement.

“Owner” means any person who will be the registered owner of any Outstanding 2008 Certificate.

“Parity Reserve Fund” means the fund by that name continued pursuant to the Trust Agreement.

“Payment Agreement Payments” has the meaning given such term in the Master Contract.

“Payment Agreement Receipts” has the meaning given such term in the Master Contract.

“Permitted Investments” means any of the following obligations if and to the extent then permitted by law:

- (1) Federal Securities;
- (2) Obligations issued by the Resolution Funding Corporation and the Student Loan Marketing Association, or obligations, participations, or other instruments of or issued by, or fully guaranteed as to interest and principal by, the Government National Mortgage Association (excluding stripped mortgage backed securities which are valued at greater than par on the unpaid principal);
- (3) Bills of exchange or time drafts drawn on and accepted by a commercial bank (including the Trustee or any of its affiliates), otherwise known as bankers acceptances, which are eligible for purchase by the Federal Reserve System and which are drawn on any bank the short-term obligations of which are rated in the highest letter and numerical rating category as provided by Moody’s and by S&P; provided, that purchases of eligible bankers acceptances may not exceed 270 days’ maturity;
- (4) Commercial paper of “prime” quality of the highest ranking or of the highest letter and numerical rating category as provided by Moody’s and by S&P, which commercial paper is limited to issuing corporations that are organized and operating within the United States of America and that have total assets in excess of \$500,000,000 and that have an “A1” or higher rating for the issuer’s unsecured debentures, other than commercial paper, as provided by Moody’s and by S&P; provided, that purchases of eligible commercial paper may not exceed 180 days’ maturity nor represent more than 10% of the outstanding commercial paper of an issuing corporation;
- (5) Non-negotiable certificates of deposit issued by a state or national bank (including the Trustee or any of its affiliates) that have maturities of not more than 365 days or deposit accounts with a state or national bank and that are fully insured by the Federal Deposit Insurance Corporation or the short-term obligations of which state or national bank are rated no lower than “A1” by Moody’s and “A+” by S&P;
- (6) Any repurchase agreement of any securities enumerated in subdivisions (1) and (2) with any state or national bank (including the Trustee or any of its affiliates) or government bond dealer reporting to, trading with, and recognized as a primary dealer by the Federal Reserve Bank of New York, which agreement is either (A) with any institution which has debt rated no lower than “A1” by Moody’s and “A+” by S&P or whose commercial paper is rated no lower than “P-1” by Moody’s and no lower than “A-1” by S&P; (B) with any corporation or other entity that falls under the jurisdiction of the Federal Bankruptcy Code; provided, that (a) the term of such repurchase agreement is less than one (1) year or due on demand; (b) the Trustee or a third party acting solely as agent for the Trustee has possession of the collateral; (c) the market value of the collateral (as determined at least once in every 14 days) exceeds the principal amount of the repurchase agreement plus accrued interest and the market value of the collateral is maintained at levels acceptable to Moody’s and to S&P; (d) failure to maintain the requisite collateral levels will require the Trustee to liquidate the collateral immediately; and (e) the repurchase agreement securities are free and clear of any third-party lien or claim; or (C) with financial institutions insured by the Federal Deposit Insurance Corporation or any broker-dealer with “retail customers” which falls under the jurisdiction

of the Securities Investors Protection Corporation; provided, that: (a) the market value of the collateral (as determined at least once in every 14 days) exceeds the principal amount of the repurchase agreement plus accrued interest and the market value of the collateral is maintained at levels acceptable to Moody's and to S&P; (b) the Trustee or a third party acting solely as agent for the Trustee has possession of the collateral; (c) the Trustee has a perfected first priority security interest in the collateral; (d) the collateral is free and clear of third-party liens and in the case of a Securities Investors Protection Corporation broker was not acquired pursuant to a repurchase agreement or reverse repurchase agreement; and (e) failure to maintain the requisite collateral percentage will require the Trustee to liquidate the collateral immediately;

(7) Certificates, notes, warrants, bonds or other evidence of indebtedness of the State or any local agencies therein which are rated in the highest short-term rating category or within one of the three highest long-term rating categories by Moody's and by S&P (excluding securities that do not have a fixed par value and/or whose terms do not promise a fixed dollar amount at maturity or call date);

(8) For amounts less than \$100,000, interest-bearing demand or time deposits (including certificates of deposit) in a nationally or state-chartered bank fully insured by the Federal Deposit Insurance Corporation, including the Trustee or any affiliate thereof, and of which an aggregate total of \$100,000 is not exceeded in any one financial institution;

(9) Investments in units of a money-market fund portfolio that is rated in the highest letter and numerical rating category by Moody's and by S&P (including funds for which the Trustee, its affiliates or subsidiaries provide investment advisory or other management services) and that is composed of obligations guaranteed by the full faith and credit of the United States of America or repurchase agreements collateralized by such obligations;

(10) A guaranteed investment contract with a financial institution or insurance company (or guaranteed by a financial institution or insurance company) which has at the date of execution thereof an outstanding issue of unsecured, uninsured and unguaranteed debt obligations or a claims paying ability rated within the two highest rating categories of any Rating Agency;

(11) Other investments approved in writing by the 2008 Certificate Insurer; and

(12) The Local Agency Investment Fund, the California Asset Management Program, or similar pooled fund operated by or on behalf of the State and which is authorized to accept investments by or on behalf of the Authority of the moneys held by the Trustee in any of the accounts or funds established pursuant to the Trust Agreement to the extent deposits and withdrawals may be made by the Trustee directly.

"Person" will mean an individual, a corporation, an association, a joint venture, a partnership, a trust, an unincorporated organization or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"Prepayment Date" means the date fixed for prepayment of any 2008 Certificate in any notice of prepayment given in accordance with the terms of the Trust Agreement.

"Purchase Date" means any Mandatory Purchase Date.

“Purchase Price” means an amount equal to the principal amount of the 2008 Certificates purchased on any Purchase Date, plus accrued interest to such Purchase Date (unless such Purchase Date is also an Interest Payment Date, in which case the Purchase Price will not include accrued interest, which will be paid in the normal course).

“Rating Agencies” means Moody’s and S&P, and their respective successors or assigns, or any other nationally recognized securities rating agency or agencies rating the 2008 Certificates at the request of the City.

“Rating Confirmation Notice” means a written notice from the Rating Agencies then rating the 2008 Certificates, confirming that the rating on the 2008 Certificates (without giving effect to any Liquidity Facility) will not be lowered or withdrawn (other than a withdrawal of a short-term rating upon a change to a Fixed Rate Mode) as a result of the action proposed to be taken.

“Record Date” means (i) with respect to the 2008 Certificates in a Short-Term Mode, the last Business Day before each Interest Payment Date; and (ii) with respect to the 2008 Certificates in a Long-Term Mode, the 15th day (whether or not a Business Day) of the month next preceding each Interest Payment Date.

“Reimbursement Agreement” means any reimbursement agreement, credit agreement, line of credit agreement, standby purchase agreement or other agreement, between a Credit Enhancement Provider or a Liquidity Facility Provider, as applicable, and the Authority and/or the City, as the same may be amended from time to time pursuant to its terms.

“Remarketing Agent” means the remarketing agent for the 2008 Certificates selected by the Authority pursuant to the Trust Agreement and approved by the 2008 Certificate Insurer.

“Reserve Funding Instruments” will have the meaning given such term in the Trust Agreement, including the 2008 Parity Reserve Fund Insurance Policy.

“Reserve Fund Requirement” will have the meaning ascribed thereto in the Contract.

“S&P” means Standard & Poor’s Ratings Services, a division of The McGraw Hill Company, and its successors or assigns, except that if such entity will be dissolved or liquidated or will no longer perform the services of a municipal securities rating agency, then “S&P” will be deemed to refer to any other nationally recognized municipal securities rating agency selected by the Authority.

“Securities Depositories” means: The Depository Trust Company, 55 Water Street, 50th Floor, New York, New York 10041-0099, Attention: Call Notification Department, Fax: (212) 855-7232; or, in accordance with then-current guidelines of the Securities and Exchange Commission, such other securities depositories as the Authority may designate in a Certificate of the Authority to the Trustee.

“Serial Certificate” means any 2008 Certificate not subject to mandatory prepayment from Sinking Fund Payments.

“Sinking Fund Payments” means the payments required under the Trust Agreement to be deposited in the 2008 Sinking Fund Subaccount.

“Special Counsel” means any firm of nationally recognized municipal bond attorneys selected by the Authority and experienced in the issuance of municipal bonds and matters relating to the exclusion of the interest thereon from gross income for federal income tax purposes.

“State” means the State of California.

“Supplemental Contract” will have the meaning given such term in the Contract.

“Supplemental Trust Agreement” means any trust agreement then in full force and effect which has been duly executed and delivered by the Authority and the Trustee amendatory of or supplemental to the Trust Agreement; but only if and to the extent that such Supplemental Trust Agreement is specifically authorized under the Trust Agreement.

“Tax Certificate” means, collectively, the Tax Certificate concerning certain matters pertaining to the use and investment of proceeds of the 2008 Certificates, executed and delivered by the City on the date of delivery of the 2008 Certificates, including any and all exhibits attached thereto.

“Term Certificates” means the 2008 Certificates subject to mandatory prepayment from Sinking Fund Payments.

“Term Rate” means the per annum interest rate for the 2008 Certificates in the Term Rate Mode determined pursuant to the Trust Agreement.

“Term Rate Mode” means the Mode during which the 2008 Certificates evidence interest at a Term Rate.

“Term Rate Period” means the period from (and including) the Mode Change Date or the date of initial conversion of the 2008 Certificates to a Term Rate Mode, as applicable, to (but excluding) the last day of the first period that 2008 Certificates will be in the Term Rate Mode as established by the Authority pursuant to the Trust Agreement and, thereafter, the period from (and including) the beginning date of each successive Interest Rate Period selected for the 2008 Certificates by the Authority pursuant to the Trust Agreement while the 2008 Certificates are in the Term Rate Mode to (but excluding) the commencement date of the next succeeding Interest Period, including another Term Rate Period. Except as otherwise provided in the Trust Agreement, an Interest Period for the 2008 Certificates in the Term Rate Mode must be at least 180 days in length.

“Trust Agreement” means that certain Trust Agreement, dated as of May 1, 2008, between the Authority and the Trustee, as originally executed and as it may from time to time be amended or supplemented by all Supplemental Trust Agreements executed pursuant to the provisions of the Trust Agreement.

“Trustee” means The Bank of New York Trust Company, N.A., or any other association or corporation which may at any time be substituted in its place as provided in the Trust Agreement.

“2008 Certificate Insurance Policy” means the financial guaranty insurance policy issued by the 2008 Certificate Insurer guaranteeing the scheduled payment of principal of and interest evidenced and represented by the 2008 Certificates.

“2008 Certificate Insurer” means Assured Guaranty Corp., its successors and assigns.

“2008 Debt Service Fund” means the fund by that name established pursuant to the Trust Agreement.

“2008 Interest Account” means the account by that name established within the 2008 Debt Service Fund pursuant to the Trust Agreement.

“2008 Interest Rate Swap Agreement” has the meaning given such term in the 2008 Supplemental Contract.

“2008 Parity Reserve Fund Insurance Policy” means the reserve fund financial guaranty insurance policy issued by the 2008 Certificate Insurer and deposited in the Parity Reserve Fund pursuant to the Trust Agreement.

“2008 Payments” means the installment payments of interest, principal, and prepayment premium, if any, payable by the City under and pursuant to the 2008 Supplemental Contract.

“2008 Prepayment Subaccount” means the subaccount by that name established within the 2008 Principal Account of the 2008 Debt Service Fund pursuant to the Trust Agreement.

“2008 Principal Account” means the account by that name established within the 2008 Debt Service Fund pursuant to the Trust Agreement.

“2008 Project” means the refinancing of improvements to the Water Utility System described in Exhibit A to the 2008 Supplemental Contract.

“2008 Sinking Fund Subaccount” means the subaccount by that name within the 2008 Principal Account of the 2008 Debt Service Fund established pursuant to the Trust Agreement.

“2008 Supplemental Contract” means that certain 2008 Supplemental Installment Purchase Contract, dated as of May 1, 2008, by and between the City and the Authority, supplementing the Master Contract.

“Weekly Mode” means the Mode during which the 2008 Certificates evidence interest at the Weekly Rate.

“Weekly Rate” means the per annum interest rate with respect to the 2008 Certificates in the Weekly Mode determined pursuant to the Trust Agreement.

“Weekly Rate Period” means the period during which the 2008 Certificates evidence interest at a Weekly Rate, which will be the period commencing on Thursday of each week to and including Wednesday of the following week, except the first Weekly Rate Period which will be from the Mode Change Date for the 2008 Certificates to and including the Wednesday of the following week and the last Weekly Rate Period which will be from and including the Thursday of the week prior to the Mode Change Date to and including the day next preceding the Mode Change Date.

“Written Request of the Authority” means an instrument in writing signed by the Auditor and Treasurer of the Authority or by any other officer of the Authority duly authorized by the Authority for that purpose.

## **Equal Security**

In consideration of the acceptance of the 2008 Certificates by the Owners thereof, the Trust Agreement will be deemed to be and will constitute a contract between the Authority and the Owners from time to time of all 2008 Certificates authorized, executed, and delivered under the Trust Agreement and then Outstanding to secure the full and final payment of the interest, principal, and prepayment premiums, if any, evidenced and represented by the 2008 Certificates which may from time to time be authorized, executed, issued and delivered under the Trust Agreement, subject to the agreements, conditions, covenants and provisions contained in the Trust Agreement; and all agreements and covenants set forth in the Trust Agreement to be performed by or on behalf of the Trustee will be for the equal and proportionate benefit, protection and security of all Owners without distinction, preference or priority as to security or otherwise of any 2008 Certificates over any other 2008 Certificates by reason of the number or date thereof or the time of authorization, sale, execution, or delivery thereof or for any cause whatsoever, except as expressly provided in the Trust Agreement or therein.

## **2008 Payments; 2008 Project**

2008 Payments Held in Trust. The 2008 Payments will be held in trust by the Trustee for the benefit of the Owners from time to time of the 2008 Certificates, but will nonetheless be disbursed, allocated and applied solely for the uses and purposes provided in the Trust Agreement.

Deposit of 2008 Payments. The Trustee agrees to establish, maintain and hold in trust a separate fund designated as the 2008 Debt Service Fund, for so long as any 2008 Certificates will be Outstanding under the Trust Agreement. All 2008 Payments (except as otherwise provided) received by the Trustee will be immediately deposited in the 2008 Debt Service Fund and will be disbursed and applied only as provided in the Trust Agreement.

Establishment and Maintenance of Accounts for Use of Money in the 2008 Debt Service Fund. All money in the 2008 Debt Service Fund will be set aside by the Trustee in the following respective special accounts within the 2008 Debt Service Fund (each of which is created by the Trust Agreement and each of which the Trustee agrees and covenants to maintain pursuant to the Trust Agreement) in the following order of priority:

- (a) 2008 Interest Account, and
- (b) 2008 Principal Account (with a 2008 Prepayment Subaccount and a 2008 Sinking Fund Subaccount therein).

All money in each of such accounts and subaccounts will be held in trust by the Trustee for the benefit of the Owners and will be applied, used and withdrawn only for the purposes authorized in the Trust Agreement.

(a) 2008 Interest Account. On the Delivery Date, the Trustee will deposit in the 2008 Interest Account any Payment Agreement Receipts relating to the 2008 Interest Rate Swap Agreement which the City has directed under the 2008 Interest Rate Swap Agreement to be transferred to the Trustee for deposit in the 2008 Interest Account and any amounts transferred to the Trustee pursuant to the 2008 Supplemental Contract for the payment of payments due under the 2008 Interest Rate Swap Agreement. On the Business Day immediately preceding each Interest Payment

Date, the Trustee will set aside from the 2008 Debt Service Fund and deposit in the 2008 Interest Account that amount of money which is equal to the amount of interest evidenced and represented by the 2008 Certificates becoming due and payable on each such Interest Payment Date. The Trustee will also apply amounts on deposit in the 2008 Fees Subaccount to pay on behalf of the City, the Payment Agreement Payments required to be paid under the 2008 Interest Rate Swap Agreement and to pay the Remarketing Agent fees as the same will become due on each due date therefor until such 2008 Fees Subaccount will be depleted (expected to be on or about November 29, 2008). Investment earnings on amounts on deposit in the 2008 Fees Subaccount will be transferred to the City for deposit in the Revenue Fund.

No deposit need be made in the 2008 Interest Account if the amount contained therein (exclusive of amounts transferred for the payment of amounts due under the 2008 Interest Rate Swap Agreement) is at least equal to the aggregate amount of interest evidenced and represented by the 2008 Certificates becoming due and payable on such Interest Payment Date.

Except as otherwise provided in the Trust Agreement, all money in the 2008 Interest Account will be used and withdrawn by the Trustee solely for the purpose of paying the interest (including accrued interest evidenced and represented by any 2008 Certificates purchased or prepaid prior to their respective Certificate Payment Date) with respect to the 2008 Certificates as it will become due and payable and paying the Payment Agreement Payments due under the 2008 Interest Rate Swap Agreement as they will become due and payable.

(b) 2008 Principal Account. On the Business Day immediately preceding each October 1, commencing on October 1, 2008, the Trustee will set aside from the 2008 Debt Service Fund and deposit in the 2008 Principal Subaccount an amount of money equal to the principal amount evidenced and represented by the Outstanding Serial Certificates with a Certificate Payment Date of such October 1, and in the 2008 Sinking Fund Subaccount in the 2008 Principal Account the amount of all Sinking Fund Payments required to be made on such October 1.

Amounts to be applied to the optional prepayment of the principal component of the 2008 Certificates pursuant to the Trust Agreement will be deposited in the 2008 Prepayment Subaccount of the 2008 Principal Account.

No deposit need be made in the 2008 Principal Account if the amount contained therein is at least equal to the aggregate amount of the principal evidenced and represented by the Outstanding Serial Certificates with a Certificate Payment Date of such October 1 and the amount contained in the 2008 Sinking Fund Subaccount therein is at least equal to the aggregate amount of all Sinking Fund Payments required to be made on such October 1.

All money in the 2008 Principal Account will be used and withdrawn by the Trustee solely for the purpose of paying the principal evidenced and represented by the Serial Certificates as they will become due and payable, whether at their respective Certificate Payment Dates or on prior prepayment, and all money in the 2008 Sinking Fund Subaccount of the 2008 Principal Account will be used and withdrawn by the Trustee only to purchase or to prepay or to pay Term Certificates, and with respect to the 2008 Sinking Fund Subaccount, on each Sinking Fund Payment date, the Trustee will apply the Sinking Fund Payment required on that date to the prepayment (or payment at Certificate Payment Date, as the case may be) of the Term Certificates upon the notice and in the manner provided in the Trust Agreement; provided, that at any time prior to giving such notice of such prepayment, the Trustee may, upon the Written Request of the Authority and receipt of moneys

sufficient therefor, purchase for cancellation Term Certificates in accordance with the Trust Agreement.

Parity Reserve Fund. The Parity Reserve Fund created pursuant to the 1997 Trust Agreement is continued by the Trust Agreement. Pursuant to the Trust Agreement, the Trustee agrees and covenants to maintain the Parity Reserve Fund so long as the Contract has not been discharged in accordance with its terms or any 2008 Certificates remain Outstanding under the Trust Agreement. Amounts on deposit in the Parity Reserve Fund are pledged to the payment of the 1997 Certificates, the 2008 Certificates and any other obligations hereafter issued in connection with a Supplemental Contract and will be applied only for such purposes as provided in the Trust Agreement. The Trustee will deposit in the Parity Reserve Fund from the proceeds of the 2008 Certificates, the amount specified in the Trust Agreement, such amount being sufficient to cause the balance on deposit in or credited to the Parity Reserve Fund, to be equal to the Reserve Fund Requirement upon delivery of the 2008 Certificates. The Trustee will deposit in the Parity Reserve Fund such other amounts transferred to the Trustee by the City pursuant to the Contract, as directed by the Authority in a Written Request of the Authority. Moneys on deposit in the Parity Reserve Fund will be transferred by the Trustee to the 2008 Debt Service Fund to pay principal and interest evidenced and represented by the 2008 Certificates on any Interest Payment Date in the event amounts on deposit therein are insufficient for such purposes. The Trustee will also, from such amounts on deposit in the Parity Reserve Fund, transfer or cause to be transferred to any applicable debt service fund established under the 1997 Trust Agreement and under any other trust agreement under which any obligations are issued in connection with a Supplemental Contract, without preference or priority between transfers made pursuant to this sentence and the preceding sentence, and in the event of any insufficiency of such moneys ratably without discrimination or preference, that sum or sums, if any, equal to the amount required to be deposited therein pursuant to such trust agreement under which any obligations are issued in connection with a Supplemental Contract. All investments in the Parity Reserve Fund will (notwithstanding anything in the 1997 Trust Agreement to the contrary) be valued on or before October 1 of each year at the lesser of the cost or market value thereof. Following such valuation, any moneys on deposit in the Parity Reserve Fund representing an excess of the Reserve Fund Requirement will be transferred by the Trustee to the City for deposit in the Revenue Fund. The Trustee may create such subaccounts in the Parity Reserve Fund as may be necessary or convenient for the purposes of the Trust Agreement.

The Reserve Fund Requirement may be provided by one or more surety bonds, insurance policies, or letters of credit as described in the definition of Reserve Fund Requirement (“Reserve Funding Instruments”) set forth in the Contract.

Notwithstanding anything to the contrary contained in the Trust Agreement, at any time one or more Reserve Funding Instruments are on deposit in the Parity Reserve Fund, the Trustee will: (i) withdraw and use all cash, if any, on deposit in the Parity Reserve Fund prior to using and withdrawing any amounts derived from payments under any Reserve Funding Instruments; and (ii) draw on all Reserve Funding Instruments on a pro rata basis based on the draw limit of each Reserve Funding Instrument. Amounts received by the Trustee from the City pursuant to the Master Contract as a replenishment of amounts withdrawn from the Parity Reserve Fund will be applied (i) first on a pro rata basis to reimburse draws on any Reserve Funding Instruments and (ii) to replenish cash withdrawn from the Parity Reserve Fund.

Establishment and Application of Costs of Issuance Fund. Pursuant to the Trust Agreement, the Trustee agrees to establish, maintain and hold in trust a separate fund designated as the Costs of

Issuance Fund, which fund is created by the Trust Agreement and which fund the Authority agrees to maintain with the Trustee until November 29, 2008. The Trustee will deposit to the Costs of Issuance Fund the amounts specified in the Trust Agreement. All money in the Costs of Issuance Fund will be used and withdrawn by the Trustee to pay the Costs of Issuance relating to the 2008 Certificates upon receipt of a Written Request of the Authority filed with the Trustee, each of which will be sequentially numbered and will state the person to whom payment is to be made, the amount to be paid, the purpose for which the obligation was incurred and that such payment is a proper charge against said fund. On November 29, 2008, or upon the earlier Written Request of the Authority, any remaining balance in the Costs of Issuance Fund will be transferred to the City for deposit in the 2008 Debt Service Fund.

Deposit and Investments of Money in Accounts and Funds. All money held by the Trustee in any of the accounts or funds established pursuant to the Trust Agreement will be invested in Permitted Investments at the Written Request of the Authority filed with the Trustee which such Permitted Investments will, as nearly as practicable, mature on or before the dates on which such money is anticipated to be needed for disbursement under the Trust Agreement, and the Trustee will have no liability or responsibility for any loss resulting from any investment made in accordance with the Trust Agreement; provided, that if no such Written Request is received by the Trustee, the Trustee will invest such money in those Permitted Investments described in clause (9) of the definition thereof. Except as otherwise provided in the Trust Agreement with respect to the Parity Reserve Fund, all interest or profits received on any money so invested will be deposited in the 2008 Debt Service Fund.

The Authority acknowledges that to the extent regulations of the Comptroller of the Currency or other applicable regulatory entity grant the Authority the right to receive brokerage confirmations of security transactions as they occur, the Authority specifically waives receipt of such confirmations to the extent permitted by law. The Trustee will furnish the Authority periodic cash transaction statements which include detail for all investment transactions made by the Trustee under the Trust Agreement.

The Trustee or any of its affiliates may act as principal or agent, sponsor, advisor or manager in connection with any investments made by the Trustee under the Trust Agreement. For investment purposes, the Trustee may commingle the funds and accounts established under the Trust Agreement, but will account for each separately.

The Trustee will not be liable for any loss from any Permitted Investment acquired, held, or disposed of at the written request of the Authority. Any Permitted Investments that are registered securities will be registered in the name of the Trustee.

#### **Assignment to Trustee; Enforcement of Obligations.**

(a) Pursuant to the Trust Agreement, the Authority transfers, assigns and sets over to the Trustee all of the 2008 Payments and any and all rights and privileges it has under the Contract, including, without limitation, the right to collect and receive directly all of the 2008 Payments, and any 2008 Payments collected or received by the Authority will be deemed to be held, and to have been collected or received, by the Authority as the agent of the Trustee, and will forthwith be paid by the Authority to the Trustee. The Trustee also will, subject to the provisions of the Trust Agreement, take all steps, actions and proceedings required to be taken as provided in any Opinion of Counsel delivered to it, reasonably necessary to maintain in force for the benefit of the Owners of the 2008

Certificates the Trustee's rights in and priority to the following security granted to it for the payment of the 2008 Certificates: the Trustee's rights as assignee of the 2008 Payments under the Contract and as beneficiary of any other rights to security for the 2008 Certificates which the Trustee may receive in the future.

(b) The Trustee may, in performing the obligations set out above, rely and will be protected in acting or refraining from acting upon an Opinion of Counsel furnished by the City.

### **Covenants of the Authority and the Trustee**

Compliance with Trust Agreement. The Trustee will not execute or deliver any 2008 Certificates in any manner other than in accordance with the provisions of the Trust Agreement; and the Authority will not suffer or permit any default by it to occur under the Trust Agreement, but will faithfully comply with, keep, observe and perform all the agreements and covenants to be observed or performed by it contained in the Trust Agreement and in the 2008 Certificates.

Observance of Laws and Regulations. The Authority and the Trustee will faithfully comply with, keep, observe and perform all valid and lawful obligations or regulations now or hereafter imposed on them by contract, or prescribed by any law of the United States of America or of the State of California, or by any officer, board or commission having jurisdiction or control, as a condition of the continued enjoyment of each and every franchise, right or privilege now owned or hereafter acquired by them, including their right to exist and carry on their respective businesses, to the end that such franchises, rights and privileges will be maintained and preserved and will not become abandoned, forfeited or in any manner impaired.

Accounting Records and Reports. The Trustee will keep or cause to be kept proper books of record and accounts in which complete and correct entries will be made of all transactions made by the Trustee relating to the receipts, disbursements, allocation and application of the 2008 Payments and the proceeds of the 2008 Certificates, and such books will be available for inspection by the Authority, at reasonable hours and under reasonable conditions. Not more than 180 days after the close of each Fiscal Year, the Trustee will furnish or cause to be furnished to the Authority and the 2008 Certificate Insurer a complete financial statement covering receipts, disbursements, allocation and application of 2008 Payments received by the Trustee for such Fiscal Year. The Authority will keep or cause to be kept such information as required under the Tax Certificate.

Prosecution and Defense of Suits. The Authority will defend against every suit, action or proceeding at any time brought against the Trustee upon any claim to the extent arising out of the receipt, application or disbursement of any of the 2008 Payments and the proceeds of the 2008 Certificates or to the extent involving the failure of the Authority to fulfill its obligations under the Trust Agreement; provided that the Trustee or any affected Owner at its election may appear in and defend any such suit, action or proceeding. The Authority will indemnify and hold harmless the Trustee against any and all liability claimed or asserted by any person to the extent arising out of such failure by the Authority, and will indemnify and hold harmless the Trustee against any attorney's fees or other expenses which it may incur in connection with any litigation to which it may become a party by reason of its actions under the Trust Agreement, except for any loss, cost, damage or expense resulting from the active or passive negligence, willful misconduct or breach of duty by the Trustee. Notwithstanding any contrary provision of the Trust Agreement, this covenant will remain in full force and effect even though all 2008 Certificates secured by the Trust Agreement may have been fully paid and satisfied.

Amendments to Contract. Except for any Supplemental Contract delivered in accordance with the terms of the Contract, the Authority will not supplement, amend, modify or terminate any of the terms of the Contract, or consent to any such supplement, amendment, modification or termination, without the prior written consent of the Trustee, which such consent will be given only if (a) such supplement, amendment, modification or termination will not materially adversely affect the interests of the Owners or result in any material impairment of the security given for the payment of the 2008 Certificates, or (b) the Trustee first obtains the written consent of the Owners of a majority in aggregate principal amount evidenced and represented by the 2008 Certificates then Outstanding to such supplement, amendment, modification or termination; provided, that no such supplement, amendment, modification or termination will reduce the amount of 2008 Payments to be made to the Authority or the Trustee by the City pursuant to the Contract, or extend the time for making such 2008 Payments in any manner that would require the amendment of the Trust Agreement in any manner not in compliance with the Trust Agreement, or permit the creation of any lien prior to or on a parity with the lien created by the Trust Agreement on the 2008 Payments without the written consent of all of the Owners of the 2008 Certificates then Outstanding.

Recording and Filing. The Trustee upon receipt of a Written Request of the Authority, at the expense of the Authority, will file, record, register, renew, refile and rerecord all such documents, including financing statements (or continuation statements in connection therewith), all in such manner, at such times and in such places as may be required and to the extent permitted by law in order to fully perfect, preserve and protect the security of the Owners and the rights and interests of the Trustee; provided, however, that the Trustee will not be required to execute a special or general consent to service of process, or to qualify as a foreign corporation in connection with any such filing, recording, registration, refile or rerecording in any jurisdiction in which it is not now so subject.

Further Assurances. Whenever and so often as reasonably requested to do so by the Trustee or any Owner, the Authority will promptly execute and deliver or cause to be executed and delivered all such other and further assurances, documents or instruments, and promptly do or cause to be done all such other and further things as may be necessary or reasonably required in order to further and more fully vest in the Trustee and the Owners all rights, interests, powers, benefits, privileges and advantages conferred or intended to be conferred upon them by the Trust Agreement.

## **The Trustee**

The Trustee. The Bank of New York Trust Company, N.A., will serve as the Trustee for the purpose of receiving all money which the Authority is required to deposit with the Trustee under the Trust Agreement and for the purpose of allocating, applying and using such money as provided in the Trust Agreement and for the purpose of paying the interest and principal and prepayment premiums, if any, evidenced and represented by the 2008 Certificates presented for payment, and for the purpose of canceling all paid or prepaid 2008 Certificates as provided in the Trust Agreement. The Authority agrees that it will at all times maintain a Trustee having a corporate trust office in either San Francisco, California or Los Angeles, California.

The Authority may at any time, unless there exists any Event of Default as defined in the Trust Agreement, remove the Trustee initially appointed and any successor thereto and may appoint a successor or successors thereto by an instrument in writing; provided that any successor appointed under the Trust Agreement will be approved by the 2008 Certificate Insurer and will be a bank with trust powers or trust company doing business and having a principal office in either San Francisco,

California or Los Angeles, California, having (or if such bank or trust company is a member of a bank holding company system, its bank holding company has) a combined capital (exclusive of borrowed capital) and surplus of at least \$50,000,000 and subject to supervision or examination by federal or state authority. If such bank or trust company publishes a report of condition at least annually, pursuant to law or to the requirements of any supervising or examining authority above referred to, then for the purpose of this provision the combined capital and surplus of such bank or trust company will be deemed to be its combined capital and surplus as set forth in its most recent report of condition so published. The Trustee may at any time resign by giving written notice of such resignation to the Authority and by mailing to the Owners notice of such resignation. Upon receiving such notice of resignation, the Authority will promptly appoint a successor Trustee by an instrument in writing. Any removal or resignation of a Trustee and appointment of a successor Trustee will become effective only upon the acceptance of appointment by the successor Trustee. If, within 30 days after notice of the removal or resignation of the Trustee no successor Trustee will have been appointed and will have accepted such appointment, the removed or resigning Trustee may petition any court of competent jurisdiction for the appointment of a successor Trustee, which court may thereupon, after such notice, if any, as it may deem proper and prescribe and as may be required by law, appoint a successor Trustee having the qualifications required by the Trust Agreement. Any successor trustee will signify its acceptance of the duties under the Trust Agreement by an instrument in writing provided to the Authority and the Notice Parties.

Liability of the Trustee. The recitals of facts, agreements and covenants in the Trust Agreement and in the 2008 Certificates will be taken as recitals of facts, agreements and covenants of the Authority, and the Trustee assumes no responsibility for the correctness of the same or makes any representation as to the sufficiency or validity of the Trust Agreement or of the 2008 Certificates, or will incur any responsibility in respect thereof other than in connection with the rights or obligations assigned to or imposed upon it in the Trust Agreement, in the 2008 Certificates or in law or equity. The Trustee will not be liable in connection with the performance of its duties under the Trust Agreement except for its own active or passive negligence or willful misconduct.

The Trustee will not be liable for any error of judgment made in good faith by a responsible officer, unless it will be proved that the Trustee was negligent in ascertaining the pertinent facts.

The Trustee will not be liable with respect to any action taken or omitted to be taken by it in good faith in accordance with the direction of the Owners of not less than a majority in aggregate principal amount of the 2008 Certificates at the time Outstanding, relating to the time, method and place of conducting any proceeding for any remedy available to the Trustee, or exercising any trust or power conferred upon the Trustee under the Trust Agreement.

The Trustee will be under no obligation to exercise any of the rights or powers vested in it by the Trust Agreement at the request, order or direction of any of the Owners pursuant to the provisions of the Trust Agreement unless such Owners will have offered to the Trustee reasonable security or indemnity against the costs, expenses and liabilities that may be incurred therein or thereby. The Trustee has no obligation or liability to the Owners for the payment of interest, principal or prepayment premium, if any, evidenced and represented by the 2008 Certificates from its own funds; but rather the Trustee's obligations will be limited to the performance of its duties under the Trust Agreement.

The Trustee will not be deemed to have knowledge of any default under the Trust Agreement or default under the Contract unless and until it will have actual knowledge thereof or will have

received written notice thereof at its Corporate Trust Office. Except as otherwise expressly provided in the Trust Agreement, the Trustee will not be bound to ascertain or inquire as to the performance or observance of any of the terms, conditions, covenants or agreements in the Trust Agreement or of any of the documents executed in connection with the 2008 Certificates or as to the existence of a default under the Trust Agreement.

The Trustee will not be considered in breach of or in default in its obligations under the Trust Agreement or progress in respect thereto in the event of enforced delay (“unavoidable delay”) in the performance of such obligations due to unforeseeable causes beyond its control and without its fault or negligence, including, but not limited to, acts of God or of the public enemy or terrorists, acts of a government, acts of the other party, fires, floods, epidemics, quarantine restrictions, strikes, freight embargoes, earthquakes, explosion, mob violence, riot, inability to procure or general sabotage or rationing of labor, equipment, facilities, sources of energy, material or supplies in the open market, litigation or arbitration involving a party or others relating to zoning or other governmental action or inaction pertaining to the project, malicious mischief, condemnation, and unusually severe weather or delays of suppliers or subcontractors due to such causes or any similar event and/or occurrences beyond the control of the Trustee.

### **Amendment of the Trust Agreement**

Amendment of the Trust Agreement. The Trust Agreement and the rights and obligations of the Authority and of the Owners may be amended at any time by a Supplemental Trust Agreement which will become binding when the written consents of the Owners of a majority in aggregate principal amount of the 2008 Certificates then Outstanding, exclusive of 2008 Certificates disqualified as provided in Trust Agreement, are filed with the Trustee; provided, that before executing any such Supplemental Trust Agreement the Trustee may first obtain at the Authority’s expense an Opinion of Counsel that such Supplemental Trust Agreement complies with the provisions of the Trust Agreement, on which opinion the Trustee may conclusively rely. No such amendment will (1) extend the Certificate Payment Date of, or change the payment dates of, or reduce the rate of interest or principal or prepayment premium, if any, evidenced and represented by any 2008 Certificate without the express written consent of the Owner of such Certificate, or (2) reduce the percentage of 2008 Certificates required for the written consent to any such amendment, or (3) modify any rights or obligations of the Trustee without its prior written assent thereto.

The Trust Agreement and the rights and obligations of the Authority and of the Owners may also be amended at any time by a Supplemental Trust Agreement which will become binding upon adoption without the consent of any Owners, but only to the extent permitted by law, for any purpose that will not materially adversely affect the interests of the Owners, including (without limitation) for any one or more of the following purposes:

(a) to add to the agreements and covenants required in the Trust Agreement to be performed by the Authority other agreements and covenants thereafter to be performed by the Authority, or to surrender any right or power reserved in the Trust Agreement to or conferred in the Trust Agreement on the Authority;

(b) to make such provisions for the purpose of curing any ambiguity or of correcting, curing or supplementing any defective provision contained in the Trust Agreement or in regard to questions arising under the Trust Agreement which the Authority may deem desirable or necessary and not inconsistent with the Trust Agreement;

(c) to add to the agreements and covenants required in the Trust Agreement, such agreements and covenants as may be necessary to qualify the Trust Agreement under the Trust Indenture Act of 1939;

(d) to make any amendments or supplements necessary or appropriate to preserve or protect the exclusion of interest evidenced and represented by the 2008 Certificates from gross income for federal income tax purposes under the Code or the exemption of such interest from State of California personal income taxes;

(e) to make such amendments or supplements as may be necessary or appropriate to maintain any then current rating on the 2008 Certificates by any of the Rating Agencies;

(f) to add to the rights of the Trustee;

(g) to modify, alter, amend or supplement the Trust Agreement in any other respect, including amendments which would otherwise be described in the Trust Agreement, if the effective date of such amendments is a date on which all 2008 Certificates affected thereby are subject to mandatory tender for purchase pursuant to the provisions of the Trust Agreement or if notice of the proposed amendments is given to Owners of the affected 2008 Certificates at least thirty (30) days before the proposed effective date of such amendments and, on or before such effective date, such Owners have the right to demand purchase of their 2008 Certificates pursuant to the provisions of the Trust Agreement; or

(h) for any other purpose that does not materially and adversely affect the interests of the Owners of the 2008 Certificates.

Amendment by Mutual Consent. Subject to certain provisions in the Trust Agreement related to the 2008 Certificate Insurance Policy, the Trust Agreement does not prevent any Owner from accepting any amendment as to the particular 2008 Certificates held by him, provided that due notation thereof is made on such 2008 Certificates.

Consent of the Liquidity Facility Provider. Notwithstanding anything to the contrary contained in the Trust Agreement, the Trust Agreement may not be amended without the prior written consent of the Liquidity Facility Provider.

Notice. The Trustee will give notice to the Rating Agencies of any amendments pursuant to the Trust Agreement.

### **Events of Default and Remedies of Owners**

Events of Default: Acceleration; Waiver of Default. If an Event of Default (as that term is defined in the Contract) will happen, then such Event of Default will constitute a default under the Trust Agreement, and in each and every such case during the continuance of such Event of Default the Trustee or the Owners of not less than a majority in aggregate principal amount of the 2008 Certificates then Outstanding will exercise the remedies provided to the Authority in the Contract; provided, that nothing contained in the Trust Agreement will affect or impact the right of action of any Owner to institute suit directly against the City to enforce payment of the obligation evidenced and represented by such Owner's 2008 Certificates. Upon the occurrence of any Event of Default, the Trustee will give notice to the Credit Enhancement Provider and the Liquidity Facility Provider.

In determining whether a payment default has occurred under the Trust Agreement or whether a payment on the 2008 Certificates has been made under the Trust Agreement, no effect will be given to payments made under the 2008 Certificate Insurance Policy.

Other Remedies of the Trustee. The Trustee will have the right:

(a) by mandamus or other action or proceeding or suit at law or in equity to enforce the Authority's rights under the Contract against the City or any director, officer or employee thereof, and to compel the City or any such director, officer or employee to perform or carry out its or his duties under law and the agreements and covenants required to be performed by it or him contained in the Contract;

(b) by suit in equity to enjoin any acts or things which are unlawful or violate the rights of the Trustee; or

(c) by suit in equity upon the happening of any Event of Default under the Trust Agreement to enforce the Authority's rights under the Contract to require the City and its directors, officers and employees to account as the trustee of an express trust.

Non-Waiver. A waiver of any default or breach of any duty or contract by the Trustee will not affect any subsequent default or breach of duty or contract or impair any rights or remedies on any such subsequent default or breach of duty or contract. No delay or omission by the Trustee to exercise any right or remedy accruing upon any default or breach of duty or contract will impair any such right or remedy or will be construed to be a waiver of any such default or breach of duty or contract or any acquiescence therein, and every right or remedy conferred upon the Trustee by law or by the Trust Agreement may be enforced and exercised from time to time and as often as will be deemed expedient by the Trustee.

If any action, proceeding or suit to enforce any right or to exercise any remedy is abandoned or determined adversely to the Trustee, the Trustee, and the City will be restored to their former positions, rights and remedies as if such action, proceeding or suit had not been brought or taken.

Remedies Not Exclusive. No remedy in the Trust Agreement conferred upon or reserved to the Trustee or the Owners is intended to be exclusive of any other remedy, and each such remedy will be cumulative and will be in addition to every other remedy given thereunder or now or hereafter existing in law or in equity or by statute or otherwise and may be exercised without exhausting and without regard to any other remedy conferred by law.

No Liability by the City to the Owners. Except for the payment when due of the 2008 Payments and the performance of the other agreements and covenants required to be performed by it contained in the Contract, the City will not have any obligation or liability to the Owners with respect to the Trust Agreement or the preparation, execution, delivery or transfer of the 2008 Certificates or the disbursement of the 2008 Payments by the Trustee to the Owners, or with respect to the performance by the Trustee of any right or obligation required to be performed by it contained in the Trust Agreement.

No Liability by the Trustee to the Owners. Except as expressly provided in the Trust Agreement, the Trustee will not have any obligation or liability to the Owners with respect to the

payment when due of the 2008 Payments by the City, or with respect to the performance by the City of the other agreements and covenants required to be performed by it contained in the Contract.

Control of Remedies by Credit Facility Provider or Liquidity Facility Provider. Provided that the Credit Facility or the Liquidity Facility remain in effect, notwithstanding anything in the Trust Agreement to the contrary, the Credit Facility Provider will have the right to direct all remedies upon the occurrence of an Event of Default. If the Credit Facility is no longer in effect or a default has occurred with respect to the Credit Facility, the Liquidity Facility Provider will have the right to direct all remedies upon the occurrence of an Event of Default.

## **Defeasance**

Discharge of Trust Agreement. When the obligations of the City under the Contract will cease pursuant to the Contract (except for the right of the Trustee and the obligation of the City to have the money and Federal Securities mentioned therein applied to the payment of 2008 Payments as therein set forth), and either (i) the 2008 Certificates are in Fixed Rate Mode at the time moneys or Federal Securities are deposited, (ii) the deposit of money and Federal Securities is sufficient to pay the 2008 Certificates at the Maximum Rate to the earlier of the first possible tender or redemption date, or (iii) the City will have received a Rating Confirmation Notice on any 2008 Certificate that will remain Outstanding following such redemption, then and in such case the obligations created by the Trust Agreement will thereupon cease, terminate and become void except for the right of the Owners and the obligation of the Trustee to apply such moneys and Federal Securities to the payment of the 2008 Certificates as set forth in the Trust Agreement and the right of the Trustee to collect any fees or expenses due thereunder and the Trustee will turn over to the City, as an overpayment of 2008 Payments, all balances remaining in any other funds or accounts other than moneys and Federal Securities held for the payment of the 2008 Certificates at maturity or on prepayment, which moneys and Federal Securities will continue to be held by the Trustee in trust for the benefit of the Owners and will be applied by the Trustee to the payment, when due, of the principal and interest and premium if any represented by the 2008 Certificates, and after such payment, the Trust Agreement will become void.

If moneys or Federal Securities are deposited with and held by the Trustee as provided in the Trust Agreement, the Trustee will mail a notice, first-class postage prepaid, to the Owners at the addresses listed on the registration books kept by the Trustee pursuant to the Trust Agreement, stating that (a) moneys or Federal Securities are so held by it, and (b) that the Trust Agreement has been released in accordance with the provisions of the Trust Agreement.

Notice of discharge of the Trust Agreement will be provided to the Rating Agencies by the Trustee.

Deposit of Money or Securities with Trustee. Whenever in the Trust Agreement or the Contract it is provided or permitted that there be deposited with or held in trust by the Trustee money or securities (certified to be sufficient by a report of an Independent Certified Public Accountant) in the necessary amount to pay or prepay any 2008 Certificates, the money or securities to be so deposited or held may include money or securities held by the Trustee in the funds and accounts established pursuant to the Trust Agreement and will be:

(a) lawful money of the United States of America in an amount equal to the principal amount represented by such 2008 Certificates and all unpaid interest represented thereby to maturity,

except that, in the case of 2008 Certificates which are to be prepaid prior to maturity and in respect of which notice of such prepayment will have been given as provided in the Trust Agreement or provision satisfactory to the Trustee will have been made for the giving of such notice, the amount to be deposited or held will be the principal amount plus accrued interest to such date of prepayment plus a prepayment premium, if any, represented by such 2008 Certificates; or

(b) Federal Securities which are not subject to redemption except by the holder thereof prior to maturity (including any such securities issued or held in book-entry form) or municipal obligations which have been defeased under irrevocable escrow instructions with Federal Securities and which are rated in the highest rating category by the Rating Agencies, the principal of and interest on which when due will provide, in its opinion of an Independent Certified Public Accountant, delivered to the Trustee, money sufficient to pay the principal plus prepayment premium, if any, plus all accrued interest to maturity or to the prepayment date, as the case may be, represented by the 2008 Certificates to be paid or prepaid, as such amounts become due, provided that, in the case of 2008 Certificates which are to be prepaid prior to the maturity thereof, notice of such prepayment will have been given as provided in the Trust Agreement or provision satisfactory to the Trustee will have been made for the giving of such notice;

provided, in each case, that the Trustee will have been irrevocably instructed (by the terms of the Trust Agreement and the Contract or by Written Request of the City) to apply such money to the payment of such principal plus prepayment premium, if any, plus interest represented by such 2008 Certificates.

Unclaimed Money. Notwithstanding anything contained in the Trust Agreement to the contrary, any money held by the Trustee in trust for the payment and discharge of any of the 2008 Certificates which remains unclaimed for two years after the date when such 2008 Certificates have become due and payable, either at their stated Certificate Payment Dates or by call for prepayment prior to Certificate Payment Date, if such money was held by the Trustee at such date, or for two years after the date of deposit of such money if deposited with the Trustee after the date when such Certificates have become due and payable, will be repaid by the Trustee to the City as its absolute property free from trust, and the Trustee will thereupon be released and discharged with respect thereto and the Owners will look only to the City for the payment of the 2008 Payments evidenced and represented by such 2008 Certificates; provided, however, that before being required to make any such payment to the City, the Trustee will, at the request of and at the expense of the City, cause to be mailed to all Owners and the Securities Depositories and the Information Services a notice that such money remains unclaimed and that, after a date named in such notice, which date will not be less than 30 days after the date of the first publication of each such notice, the balance of such money then unclaimed will be returned to the City.

#### **Additional Provisions Relating to the 2008 Certificate Insurance Policy**

(a) Notwithstanding anything in the Trust Agreement to the contrary so long as the 2008 Certificate Insurance Policy relating to the 2008 Certificates will be in full force and effect and the 2008 Certificate Insurer will not be in default of any of its obligations thereunder, the 2008 Certificate Insurer will be deemed to be sole Owner of the 2008 Certificates it insures for the purpose of exercising any voting right or privilege or giving any consent or direction or taking any other action that the 2008 Certificate Owners are entitled to take pursuant to the Trust Agreement, including any consent to any modification, amendment or supplement to the Trust Agreement pursuant to the Trust Agreement.

(b) Notwithstanding anything in the Trust Agreement to the contrary the 2008 Certificate Insurer shall be deemed to be the Owners of all of the 2008 Certificates for purposes of (a) exercising all remedies and directing the Trustee to take actions or for any other purposes following an Event of Default (as defined herein), and (b) granting any consent, direction or approval or taking any action permitted or required by the Owners of the 2008 Certificates.

(c) Notwithstanding anything in the Trust Agreement to the contrary so long as the 2008 Certificate Insurance Policy will be in full force and effect and the 2008 Certificate Insurer will not be in default of any of its obligations thereunder, upon the occurrence and continuance of an Event of Default, the Trustee may, with the consent of the 2008 Certificate Insurer, and will at the direction of the 2008 Certificate Insurer or the Bondholders with the prior written consent of the 2008 Certificate Insurer, by written notice to the Authority and the 2008 Certificate Insurer, as applicable (i) declare the principal of the 2008 Certificates immediately due and payable, whereupon that portion of the principal of the 2008 Certificates thereby coming due and the interest thereon accrued to the date of payment will, without further action, become and be immediately due and payable, anything in the Trust Agreement or the 2008 Certificates to the contrary notwithstanding or (ii) annul any declaration of acceleration.

**APPENDIX C**

**PROPOSED FORM OF OPINION OF SPECIAL COUNSEL**

[Closing Date]

City Council  
City of Modesto  
Modesto, California

\$47,625,000

CITY OF MODESTO

WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

Ladies and Gentlemen:

We have acted as special counsel to the City of Modesto (the “City”) in connection with the execution and delivery of \$47,625,000 principal amount of Water Revenue Certificates of Participation, 2008 Series A (the “Certificates”), evidencing and representing proportionate interests of the owners thereof in 2008 Payments (as that term is defined in the Trust Agreement referred to below) to be made by the City under and pursuant to that certain Master Installment Purchase Contract, dated as of November 1, 1997 (the “Master Installment Purchase Contract”), by and between the City and the Modesto Public Financing Authority (the “Authority”), as previously supplemented and as amended and supplemented by that certain 2008 Supplemental Installment Purchase Contract, dated as of May 1, 2008 (the “2008 Supplemental Installment Purchase Contract”), by and between the City and the Authority. The Master Installment Purchase Contract, as previously supplemented and as amended and supplemented by the 2008 Supplemental Installment Purchase Contract, is referred to herein as the “Installment Purchase Contract.” All of the Authority’s rights to receive such 2008 Payments have been assigned by the Authority to The Bank of New York Trust Company, N.A., as trustee (the “Trustee”), pursuant to that certain Trust Agreement, dated as of May 1, 2008 (the “Trust Agreement”), by and between the Authority and the Trustee. The Certificates have been executed by the Trustee pursuant to the terms of the Trust Agreement.

In our capacity as special counsel, we have reviewed relevant laws of the State of California, including the City Charter; executed copies of the Installment Purchase Contract and the Trust Agreement; certifications and resolutions of the City, the Authority, the Trustee, and others; opinions of counsel to the City, the Authority and the Trustee; and such other documents, opinions and instruments as we deemed necessary to render the opinions set forth herein. Our services as special counsel were limited to such examination and to rendering the opinions set forth below. We have assumed the genuineness of all documents and signatures presented to us. We have not undertaken to verify independently, and have assumed, the accuracy of the factual matters represented, warranted or certified in the documents. Furthermore, we have assumed compliance with all covenants and agreements contained in the Installment Purchase Contract and the Trust Agreement, including (without limitation) covenants and agreements compliance with which is necessary to assure that future actions, omissions or events will not cause interest represented by the Certificates to be included in gross income for federal income tax purposes.

Certain requirements and procedures contained or referred to in the Installment Purchase Contract and the Trust Agreement or other relevant documents relating to the Certificates may be changed, and certain actions may be taken (including, without limitation, defeasance of the Certificates) or omitted, under the circumstances and subject to the terms and conditions set forth in such documents, upon the advice or with the approving opinion of counsel nationally recognized in the area of municipal bonds. We express no opinion as to the effect of any change to any document pertaining to the Certificates or of any action taken or not taken where such change is made or action is taken or not taken without our approval or in reliance upon the advice of counsel other than ourselves with respect to the exclusion from gross income of the interest represented by the Certificates for federal income tax purposes.

With respect to the opinions expressed herein, the enforceability of the Installment Purchase Contract is subject to the limitations on the imposition of certain fees and charges by the City relating to the Water Utility System under Articles XIIC and XIID of the California Constitution. In addition, the rights and obligations under the Certificates, the Installment Purchase Contract and the Trust Agreement are subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting the enforcement of creditors' rights generally, to the application of equitable principles (regardless of whether such enforceability is considered in equity or at law), to the exercise of judicial discretion in appropriate cases and to the limitations on legal remedies against cities in the State of California. Furthermore, we express no opinion with respect to any indemnification, contribution, penalty, choice of forum or waiver provisions contained in the foregoing documents.

Based on and subject to the foregoing, and in reliance thereon, as of the date hereof, we are of the following opinions:

1. The Master Installment Purchase Contract, the 2008 Supplemental Installment Purchase Contract and the Trust Agreement have been duly authorized, executed and delivered by the Authority; the Master Installment Purchase Contract and the 2008 Supplemental Installment Purchase Contract have been duly authorized, executed and delivered by the City; and, assuming (in the case of the Trust Agreement) due authorization, execution and delivery by the Trustee, such agreements are valid and binding obligations of the Authority and the City (as the case may be), enforceable against the Authority and the City (as the case may be) in accordance with their respective terms.

2. The Certificates, assuming due execution and delivery by the Trustee, are entitled to the benefits of the Trust Agreement.

3. The obligation of the City to make the 2008 Payments under the Installment Purchase Contract is a special obligation of the City payable solely from Gross Revenues (as such term is defined in the Installment Purchase Agreement). The general fund of the City is not liable, and neither the credit nor taxing power of the City is pledged, for the payment of the 2008 Payments under the Installment Purchase Contract.

4. Based on existing statutes, regulations, rulings and judicial decisions and assuming compliance by the City with certain covenants in the Installment Purchase Contract and with requirements of the Internal Revenue Code of 1986, as amended, regarding the use, expenditure and investment of Certificate proceeds and the timely payment of certain investment earnings to the United States Treasury, interest represented by the Certificates is not includable in the gross income

of the owners of the Certificates for purposes of federal income taxation. Failure by the City to comply with the above covenants and requirements may cause interest represented by the Certificates to be included in gross income retroactive to the date of execution and delivery of the Certificates.

Interest represented by the Certificates will not be treated as an item of tax preference in calculating the federal alternative minimum taxable income of individuals or corporations; however, interest represented by the Certificates will be included as an adjustment in the calculation of the alternative minimum taxable income of corporations and may therefore affect the federal alternative minimum tax liability of corporations.

5. Interest represented by the Certificates is exempt from present State of California personal income taxes.

Other than as described herein, we neither addressed nor are we opining on the tax consequences to any person of the investment in, or the receipt of interest represented by, the Certificates.

The opinions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions. Such opinions may be adversely affected by actions taken or events occurring, including a change in law, regulation or ruling (or in the application or official interpretation of any law, regulation or ruling) after the date hereof. We have not undertaken to determine, or to inform any person, whether such actions are taken or such events occur, and we have no obligation to update this opinion in light of such actions or events.

This opinion is limited to the laws of the State of California and the federal laws of the United States. The opinions in this letter are expressed solely as of the date hereof for your benefit and may not be relied upon in any manner for any purposes by any other person.

Respectfully submitted,

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## APPENDIX D

### INFORMATION CONCERNING DTC

*The information in this Appendix concerning DTC and DTC's book entry only system has been obtained from sources that the Authority and the City believe to be reliable, but neither the Authority nor the City takes any responsibility for the completeness or accuracy thereof. The following description of the procedures and recordkeeping with respect to beneficial ownership in the 2008 Certificates, payment of principal, premium, if any, and interest with respect to the 2008 Certificates to all DTC Participants or to Beneficial Owners, confirmation and transfers of Beneficial Ownership interests in the 2008 Certificates and other related transactions by and between DTC, DTC Participants and Beneficial Owners is based solely on information provided by DTC.*

The Depository Trust Company ("DTC"), New York, NY, will act as securities depository for the 2008 Certificates. The 2008 Certificates will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered security certificate will be issued for each maturity of the 2008 Certificates, each in the aggregate principal amount of such maturity, and will be deposited with DTC.

DTC, the world's largest securities depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 3.5 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 100 countries that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Fixed Income Clearing Corporation, and Emerging Markets Clearing Corporation, (NSCC, FICC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission.

Purchases of 2008 Certificates under the DTC system must be made by or through Direct Participants, which will receive credit for the 2008 Certificates on DTC's records. The ownership interest of each actual purchaser of each 2008 Certificate (a "Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchases. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the 2008 Certificates are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Certificates, except in the event that use of the book-entry system for the 2008 Certificates is discontinued.

To facilitate subsequent transfers, all 2008 Certificates deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co, or such other name as may be requested by an authorized representative of DTC. The deposit of 2008 Certificates with DTC and their registration in the

name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the 2008 Certificates; DTC's records reflect only the identity of the Direct Participants to whose accounts such 2008 Certificates are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of 2008 Certificates may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the 2008 Certificates, such as redemptions, tenders, defaults, and proposed amendments to the Bond documents. For example, Beneficial Owners of 2008 Certificates may wish to ascertain that the nominee holding the 2008 Certificates for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of notices be provided directly to them.

Prepayment notices shall be sent to DTC. If less than all of the 2008 Certificates within a maturity are being prepaid, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such maturity to be prepaid.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to 2008 Certificates unless authorized by a Direct Participant in accordance with DTC's MMI Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the City as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts 2008 Certificates are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Prepayment proceeds, principal and interest payments on the 2008 Certificates will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the City or the Trustee, on the payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC, the Trustee or the City, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of prepayment proceeds, principal and interest payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the City or the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

A Beneficial Owner shall give notice to elect to have its 2008 Certificates purchased tendered, through its Participant, to the Remarketing Agent, and shall effect delivery of 2008 Certificates by causing the Direct Participant to transfer the Participant's interest in the 2008 Certificates, on DTC's records, to the Remarketing Agent. The requirement for physical delivery of 2008 Certificates in connection with an optional tender or a mandatory purchase will be deemed satisfied when ownership rights in the 2008 Certificates are transferred by Direct Participants on DTC's records followed by a book-entry credit of tendered 2008 Certificates to the Remarketing Agent's account.

DTC may discontinue providing its services as securities depository with respect to the 2008 Certificates at any time by giving reasonable notice to the City or the Trustee. Under such circumstances, in the event that a successor securities depository is not obtained, 2008 Certificates are required to be printed and delivered.

The Authority may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, 2008 Certificates will be printed and delivered.

**APPENDIX E**  
**SPECIMEN FINANCIAL GUARANTY INSURANCE POLICY**



Assured Guaranty Corp.  
1325 Avenue of the Americas  
New York, NY 10019  
t. 212.974.0100  
www.assuredguaranty.com

**Financial Guaranty Insurance Policy**

**Issuer:**

**Policy No.:**

**Obligations:**

**Premium:**

**Effective Date:**

Assured Guaranty Corp., a Maryland corporation ("**Assured Guaranty**"), in consideration of the payment of the Premium and on the terms and subject to the conditions of this Policy (which includes each endorsement hereto), hereby unconditionally and irrevocably agrees to pay to the trustee (the "**Trustee**") or the paying agent (the "**Paying Agent**") for the Obligations (as set forth in the documentation providing for the issuance of and securing the Obligations) for the benefit of the Holders that portion of the Insured Payments which shall become Due for Payment but shall be unpaid by reason of Nonpayment.

Assured Guaranty will make such Insured Payments to the Trustee or the Paying Agent on the later to occur of (i) the date applicable principal or interest becomes Due for Payment, or (ii) the Business Day next following the day on which Assured Guaranty shall have Received a completed Notice of Nonpayment. If a Notice of Nonpayment by Assured Guaranty is incomplete or does not in any instance conform to the terms and conditions of this Policy, it shall be deemed not Received, and Assured Guaranty shall promptly give notice to the Trustee or the Paying Agent. Upon receipt of such notice, the Trustee or the Paying Agent may submit an amended Notice of Nonpayment. The Trustee or the Paying Agent will disburse the Insured Payments to the Holders only upon receipt by the Trustee or the Paying Agent in form reasonably satisfactory to it of (i) evidence of the Holder's right to receive such payments, and (ii) evidence, including without limitation any appropriate instruments of assignment, that all of the Holder's rights to payment of such principal or interest Due for Payment shall thereupon vest in Assured Guaranty. Upon and to the extent of such disbursement, Assured Guaranty shall become the Holder of the Obligations, any appurtenant coupon thereto and right to receipt of payment of principal thereof or interest thereon, and shall be fully subrogated to all of the Holder's right, title and interest thereunder, including without limitation the right to receive payments in respect of the Obligations. Payment by Assured Guaranty to the Trustee or the Paying Agent for the benefit of the Holders shall discharge the obligation of Assured Guaranty under this Policy to the extent of such payment.

This Policy is non-cancelable by Assured Guaranty for any reason. The Premium on this Policy is not refundable for any reason. This Policy does not insure against loss of any prepayment premium or other acceleration payment which at any time may become due in respect of any Obligation, other than at the sole option of Assured Guaranty, nor against any risk other than Nonpayment.

Except to the extent expressly modified by any endorsement hereto, the following terms shall have the meanings specified for all purposes of this Policy. "**Avoided Payment**" means any amount previously distributed to a Holder in respect of any Insured Payment by or on behalf of the Issuer, which amount has been recovered from such Holder pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court having competent jurisdiction that such payment constitutes an avoidable preference with respect to such Holder. "**Business Day**" means any day other than (i) a Saturday or Sunday, (ii) any day on which the offices of the Trustee, the Paying Agent or Assured Guaranty are closed, or (iii) any day on which banking institutions are authorized or required by law, executive order or governmental decree to be closed in the City of New York or in the State of Maryland. "**Due for Payment**" means (i) when referring to the principal of an Obligation, the stated maturity date thereof, or the date on which such Obligation shall have been duly called for mandatory sinking fund redemption, and does not refer to any earlier date on which payment is due by reason of a call for redemption (other than by mandatory sinking fund redemption), acceleration or other advancement of maturity (unless Assured Guaranty in its sole discretion elects to make any principal payment, in whole or in part, on such earlier date) and (ii) when referring to interest on an Obligation, the stated date for payment of such interest. "**Holder**" means, in respect of any Obligation, the person or entity who, at the time of Nonpayment, is entitled under the terms of such Obligation to payment of principal or interest thereunder, except that Holder shall not include the Issuer or any person or entity whose direct or indirect obligation constitutes the underlying security for the Obligations. "**Insured Payments**" means that portion of the principal of and interest on the Obligations that shall become Due for Payment but shall be unpaid by reason of Nonpayment. Insured Payments shall not include any additional amounts owing by the Issuer solely as a result of the failure by the Trustee or the Paying Agent to pay such amount when due and payable, including without limitation any such additional amounts as may be attributable to penalties or to interest accruing at a default rate, to amounts payable in respect of indemnification, or to any other additional amounts payable by the Trustee or the Paying Agent by reason of such failure. "**Nonpayment**" means, in respect of an Obligation, the failure of the Issuer to have provided sufficient funds to the Trustee or the Paying Agent for payment in full of all principal and interest Due for Payment on such Obligation. It is further understood that the term "Nonpayment" in respect of an Obligation includes any Avoided Payment. "**Receipt**" or "**Received**" means actual receipt or notice of or, if notice is given by overnight or other delivery service, or by certified or registered United States mail, by a delivery receipt signed by a person authorized to accept delivery on behalf of the person to whom the notice was given. Notices to Assured Guaranty may be mailed by registered mail or personally delivered or telecopied to it at 1325 Avenue of the Americas, New York, New York 10019, Telephone Number: (212) 974-0100, Facsimile Number: (212) 581-3268, Attention: Risk Management Department - Public Finance Surveillance, with a copy to the General Counsel, or to such other address as shall be specified by Assured Guaranty to the Trustee or the Paying Agent in writing. A Notice of Nonpayment will be deemed to be Received by Assured Guaranty on a given Business Day if it is Received prior to 12:00 noon (New York City time) on such Business Day; otherwise it will be deemed Received on the

next Business Day. "Term" means the period from and including the Effective Date until the earlier of (i) the maturity date for the Obligations, or (ii) the date on which the Issuer has made all payments required to be made on the Obligations.

At any time during the Term of this Policy, Assured Guaranty may appoint a fiscal agent (the "Fiscal Agent") for purposes of this Policy by written notice to the Trustee or the Paying Agent, specifying the name and notice address of such Fiscal Agent. From and after the date of Receipt of such notice by the Trustee or the Paying Agent, copies of all notices and documents required to be delivered to Assured Guaranty pursuant to this Policy shall be delivered simultaneously to the Fiscal Agent and to Assured Guaranty. All payments required to be made by Assured Guaranty under this Policy may be made directly by Assured Guaranty or by the Fiscal Agent on behalf of Assured Guaranty. The Fiscal Agent is the agent of Assured Guaranty only, and the Fiscal Agent shall in no event be liable to the Trustee or the Paying Agent for any acts of the Fiscal Agent or any failure of Assured Guaranty to deposit, or cause to be deposited, sufficient funds to make payments due under this Policy.

To the fullest extent permitted by applicable law, Assured Guaranty hereby waives, in each case for the benefit of the Holders only, all rights and defenses of any kind (including, without limitation, the defense of fraud in the inducement or in fact or any other circumstance that would have the effect of discharging a surety, guarantor or any other person in law or in equity) that may be available to Assured Guaranty to deny or avoid payment of its obligations under this Policy in accordance with the express provisions hereof. Nothing in this paragraph will be construed (i) to waive, limit or otherwise impair, and Assured Guaranty expressly reserves, Assured Guaranty's rights and remedies, including, without limitation, its right to assert any claim or to pursue recoveries (based on contractual rights, securities law violations, fraud or other causes of action) against any person or entity, in each case, whether directly or acquired as a subrogee, assignee or otherwise, subsequent to making any payment to the Trustee or the Paying Agent, in accordance with the express provisions hereof, and/or (ii) to require payment by Assured Guaranty of any amounts that have been previously paid or that are not otherwise due in accordance with the express provisions of this Policy.

This Policy (which includes each endorsement hereto) sets forth in full the undertaking of Assured Guaranty with respect to the subject matter hereof, and may not be modified, altered or affected by any other agreement or instrument, including, without limitation, any modification thereto or amendment thereof. THIS POLICY IS NOT COVERED BY THE PROPERTY/CASUALTY INSURANCE SECURITY FUND SPECIFIED IN ARTICLE 76 OF THE NEW YORK INSURANCE LAW. This Policy will be governed by, and shall be construed in accordance with, the laws of the State of New York.

IN WITNESS WHEREOF, Assured Guaranty has caused this Policy to be affixed with its corporate seal, to be signed by its duly authorized officer, and to become effective and binding upon Assured Guaranty by virtue of such signature.

**ASSURED GUARANTY CORP.**

(SEAL)

By: \_\_\_\_\_  
[Insert Authorized Signatory Name]  
[Insert Authorized Signatory Title]

Signature attested to by:

\_\_\_\_\_  
Counsel

## APPENDIX F

### CERTAIN INFORMATION REGARDING THE CITY OF MODESTO

The following information with respect to the City is presented for information purposes only. The 2008 Certificates do not constitute an indebtedness of the City within the meaning of any constitutional, statutory or charter limitations and the City is not obligated to levy any ad valorem taxes therefor or to use any other funds of the City to pay the 2008 Payments or the interest thereon (other than Gross Revenues of the Water Utility System).

#### General Description

The City, which is the county seat of Stanislaus County, was incorporated in 1884. It covers approximately 36 square miles. The City operates under a council-manager form of government pursuant to a charter adopted in 1963. The City is located in central California approximately 93 miles east of the City and County of San Francisco.

The City Council (the "Council") appoints the City Clerk and Auditor, the City Attorney, and the City Manager. The City Manager heads the executive branch of government, implements Council directives and policies, and manages the administrative and operational functions through the various department heads who are appointed by the City Manager.

The City provides the full range of services normally associated with a municipality, including public safety (police and fire), highways and streets, sanitation, health and social services, culture-recreation, public improvements, planning and zoning and general administrative services. The City also provides parking and airport facilities and water, sewer and bus service. The school districts in the City are separate governmental entities which receive no funding from the City.

#### Population

The following table represents historical population statistics for the City, the County and the State.

#### CITY OF MODESTO Population Estimates<sup>(1)</sup>

<i>Calendar Year</i>	<i>City of Modesto</i>	<i>Stanislaus County</i>	<i>State of California</i>
2008	209,936	525,903	38,049,462
2007	208,150	518,938	37,559,440
2006	207,096	511,848	37,114,598
2005	207,029	503,003	36,675,346
2004	206,861	493,515	36,199,342
2003	203,813	483,705	35,652,700
2002	199,398	472,185	35,063,959
2001	193,640	458,512	34,430,970

<sup>(1)</sup> As of January 1.

Source: California State Department of Finance, Population Estimates for Cities, Counties and State, 2001-2008 with 2000 Benchmark.

## Employment

The following table summarizes the civilian labor force, employment and unemployment in the County for the calendar years 2003 through 2007. These figures are county-wide statistics and may not necessarily accurately reflect employment trends in the City.

### MODESTO METROPOLITAN STATISTICAL AREA Industry Employment and Labor Force (Annual Averages)

	2007	2006	2005	2004	2003
<u>Civilian Labor Force</u>					
Employment	231,200	227,100	210,800	204,600	201,500
Unemployment	20,300	18,100	19,000	20,700	22,000
Unemployment Rate	8.8%	8.0%	8.3%	9.2%	9.8%
<u>Wage and Salary Employment:</u>					
Total Farm	12,800	14,100	14,100	13,800	14,000
Natural Resources, Mining and Construction	11,400	13,400	13,300	12,300	11,400
Manufacturing	22,700	23,100	22,300	22,700	23,100
Wholesale Trade	6,000	5,900	6,200	6,000	5,700
Retail Trade	22,200	22,500	22,700	21,500	21,800
Transport., Warehousing, Utilities	5,600	5,200	5,200	4,700	4,600
Information	2,300	2,400	2,500	2,500	2,200
Financial Activities	6,200	6,400	6,200	6,100	6,000
Professional and Business Services	14,900	14,800	14,900	14,200	13,800
Educational and Health Services	21,100	19,600	19,500	19,200	18,900
Leisure and Hospitality	15,400	15,500	14,800	14,200	13,700
Other Services	6,000	5,900	6,100	6,200	6,200
Federal Government	1,100	1,200	1,200	1,200	1,200
State Government	1,800	1,800	1,700	1,700	1,900
Local Government	<u>23,300</u>	<u>23,300</u>	<u>22,700</u>	<u>22,100</u>	<u>21,900</u>
Total All Industries	172,800	172,500	173,300	168,500	166,300

<sup>(1)</sup> Latest available information.

Note: Totals may not add up because of rounding.

Source: Labor Division of the California State Employment Development Department.

## Effective Buying Income

“Effective Buying Income” is defined as money income less personal tax and non-tax payments, a number often referred to as “disposable” or “after-tax” income. Money income is the aggregate of wages and salaries, net farm and non-farm self-employment income, interest, dividends, net rental and royalty income, Social Security and railroad retirement income, other retirement and disability income, public assistance income, unemployment compensation, Veterans Administration payments, alimony and child support, military family allotments, net winnings from gambling and other periodic income. Deducted from this total money income are personal income taxes (federal, state and local), personal contributions to social insurance (Social Security and federal retirement payroll deductions), and taxes on owner-occupied non-business real estate.

The following table summarizes the total effective buying income for the County and the State for the period from 2002 through 2006.

**CITY OF MODESTO, STANISLAUS COUNTY AND THE STATE OF CALIFORNIA  
Total Effective Buying Income and Median Household Effective Buying Income  
2002 through 2006<sup>(1)</sup>**

<i>Year</i>	<i>Area</i>	<i>Total Effective Buying Income (000's Omitted)</i>	<i>Median Household Effective Buying Income</i>
2006	City of Modesto Stanislaus County California		
2005	City of Modesto	\$3,274,173	\$37,874
	Stanislaus County	7,416,705	37,815
	California	705,108,410	43,915
2004	City of Modesto	\$3,274,173	\$37,874
	Stanislaus County	7,416,705	37,815
	California	705,108,410	43,915
2003	City of Modesto	\$3,165,245	\$36,774
	Stanislaus County	7,078,408	36,670
	California	647,879,427	42,484
2002	City of Modesto	\$2,957,668	\$36,573
	Stanislaus County	6,679,400	36,331
	California	650,521,407	43,532

<sup>(1)</sup> In 2002, the publisher of Sales and Marketing Management, altered the methodology used in order to produce current year estimates. The 2006 edition of Sales and Marketing Management has not been published as of the date hereof, and therefore 2006 estimates are not available.

Source: Survey of Buying Power, Sales & Marketing Management Magazine, dated 2002 through 2006.

## Major Employers

The following table summarizes the largest employers in the City in fiscal year 2006-07.

**CITY OF MODESTO  
Ten Largest Employers  
2006-07**

<i>No.</i>	<i>Company Name</i>	<i>No. Employees</i>	<i>Percentage of Total City Employment</i>
1.	Stanislaus County	4,764	4.8%
2.	Modesto City Schools	3,345	3.4
3.	E&J Gallo Winery	3,311	3.3
4.	Memorial Medical Center	2,700	2.7
5.	Del Monte Foods	2,600	2.6
6.	Modesto Junior College	2,550	2.6
7.	Signature Fruit Company	2,321	2.3
8.	Stanislaus Food Products	2,000	2.0
9.	Doctors Medical Center	1,967	2.0
10.	City of Modesto	<u>1,700</u>	<u>1.7</u>
	Subtotal	27,258	27.5
	Total City Employment	99,100	

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Source: Stanislaus Economic Development and Workforce Alliance.

## Commercial Activity

The following two tables show the dollar volume of taxable transactions in the City of Modesto and County of Stanislaus from 2002 through 2006.

### CITY OF MODESTO Taxable Transactions Calendar Years 2002 through 2006 (in Thousands of Dollars)

<b>Retail Outlets</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>	<b>2002</b>
Apparel stores	\$ 163,548	\$ 165,575	\$ 148,097	\$ 126,372	\$ 129,773
General merchandise stores	543,987	550,143	538,323	518,024	507,438
Food stores	131,263	131,100	133,058	136,462	119,423
Eating and drinking places	275,393	275,550	258,357	245,609	235,337
Home furnishing and appliances	121,102	138,642	136,143	130,089	131,234
Bldg. materials and farm implements	204,034	248,287	233,124	204,427	188,388
Auto dealers and supplies	218,243	232,889	253,170	259,395	247,861
Service stations	175,359	153,008	131,695	115,317	101,551
Other retail stores	449,981	452,236	418,822	392,650	381,371
<b>Subtotal</b>	<b>\$2,282,910</b>	<b>\$2,347,430</b>	<b>\$2,250,789</b>	<b>\$2,128,345</b>	<b>\$2,042,376</b>
All Other Outlets	395,515	400,579	414,841	433,387	372,899
<b>All Outlets</b>	<b>\$2,678,425</b>	<b>\$2,748,009</b>	<b>\$2,665,630</b>	<b>\$2,561,732</b>	<b>\$2,415,275</b>

Source: State of California, Board of Equalization.

### COUNTY OF STANISLAUS Taxable Transactions Calendar Years 2002 through 2006 (in Thousands of Dollars)

<b>Retail Outlets</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>	<b>2002</b>
Apparel stores	\$224,909	\$213,850	\$192,858	\$154,867	\$154,083
General merchandise stores	956,378	927,418	846,742	803,255	784,431
Specialty stores	558,432	535,480	501,694	465,562	432,777
Food stores	320,361	308,864	291,867	282,781	260,781
Eating and drinking places	505,384	489,169	452,120	421,793	403,421
Household	192,275	210,720	198,691	187,214	181,384
Building materials	567,014	572,552	508,825	416,983	368,472
Automotive	1,573,719	1,516,702	1,396,277	1,305,986	1,248,936
Other retail stores	369,917	368,269	331,376	297,729	273,693
<b>Subtotal</b>	<b>\$5,268,389</b>	<b>\$5,143,024</b>	<b>4,720,450</b>	<b>4,336,170</b>	<b>4,107,978</b>
Business and Personal Services	240,304	253,838	240,245	224,429	233,862
All Other Outlets	<u>\$1,843,839</u>	<u>\$1,889,038</u>	<u>\$1,804,973</u>	<u>\$1,614,893</u>	<u>\$1,494,025</u>
<b>All Outlets</b>	<b>\$7,352,532</b>	<b>\$7,285,900</b>	<b>\$6,765,668</b>	<b>\$6,175,492</b>	<b>\$5,825,865</b>

Source: State of California, Board of Equalization.

## **Construction Trends**

“Single Family Housing,” includes detached, semi-detached, rowhouse and townhouse units. Rowhouses and townhouses are included when each unit is separated from the adjacent unit by an unbroken ground-to-roof party or fire wall. Condominiums are included in single-family when they are of zero-lot-line or zero-property-line construction; when units are separated by an air space; or, when units are separated by an unbroken ground-to-roof party or fire wall. “Multi-Family Housing,” includes duplexes, 3-4-unit structures and apartment-type structures with five units or more. Multi-family housing also includes condominium units in structures of more than one living unit that do not meet the above single-family housing definition. “Residential Alterations and Additions,” means alterations, additions, and conversions to residential structures, excluding special installation permits for electrical, plumbing, heating, air-conditioning, or similar mechanical work, or installation of fire escapes, elevators, signs, etc.

“New Commercial,” includes new hotels and motels, office and bank buildings, stores and other mercantile buildings, parking garages, service stations, and amusement and recreational buildings. “New Industrial,” includes manufacturing plants and affiliated buildings. “Other New Nonresidential,” includes churches and religious buildings, hospitals and institutional buildings, schools and educational buildings, residential garages, public works and utilities buildings, and miscellaneous nonresidential structures. “Nonresidential Alterations and Additions,” means alterations, additions, and conversions to nonresidential structures, excluding special installation permits for electrical, plumbing, heating, air-conditioning, or similar mechanical work, or installation of fire escapes, elevators and signs, etc.

Provided below are the building permits and valuations for the City of Modesto for calendar years 2003 through 2007.

**CITY OF MODESTO**  
**Residential and Nonresidential Building Permit Valuations**  
**and Total Residential Building Permits**

	<i>2003</i>	<i>2004</i>	<i>2005</i>	<i>2006</i>	<i>2007</i>
<b>Permit Valuation</b>					
New Single-family	\$ 169,031,342	\$ 69,285,758	\$ 168,770,716	\$ 80,245,831	\$ 55,199,615
New Multi-family	6,105,669	20,343,871	1,118,710	3,812,649	30,912,544
Res. Alterations & Additions	39,686,601	80,226,181	45,317,392	39,017,104	80,583,151
Total Residential	214,823,612	169,855,810	215,206,818	123,075,584	166,695,310
New Commercial	24,687,807	46,240,400	11,798,301	27,027,077	59,163,453
New Industrial	994,822	3,204,092	1,202,465	2,279,197	10,000
New Other	39,686,601	37,838,523	62,440,247	21,941,020	5,188,331
Non-Res. Alterations & Additions	33,473,125	36,444,721	69,587,431	36,071,154	40,412,881
Total Nonresidential	<u>98,842,355</u>	<u>123,727,736</u>	<u>145,028,444</u>	<u>87,318,448</u>	<u>104,774,665</u>
Total All Building	\$313,665,967	\$293,583,546	\$360,235,262	\$210,394,032	\$271,469,975
<b>New Dwelling Units</b>					
Single Family	838	345	868	378	288
Multiple Family	77	288	13	37	288
Total	915	633	881	415	576

Source: Building Permit Summary, City of Modesto.

**Agriculture**

The following table summarizes historical agricultural production within the County for calendar years 2002 through 2006.

**STANISLAUS COUNTY**  
**Agricultural Production**  
**2002-2006**

<i>Commodity</i>	<i>2002</i>	<i>2003</i>	<i>2004</i>	<i>2005</i>	<i>2006</i>
Fruit and Nut Crops	\$393,520,000	\$431,642,000	\$616,452,000	\$686,897,000	\$660,001,000
Vegetable Crops	105,508,000	105,667,000	125,903,000	91,454,000	93,239,000
Field Crops	132,418,000	127,329,000	137,871,000	147,744,000	167,576,000
Seed Crops	561,000	533,000	401,000	810,000	617,000
Apiary	7,323,000	7,565,000	8,865,000	12,045,000	12,745,000
Nursery Crops	85,889,000	99,164,000	111,272,000	71,240,000	87,351,000
Livestock & Poultry	242,677,000	239,990,000	403,205,000	401,244,000	628,551,000
Livestock & Poultry Products	400,075,000	443,042,000	574,465,000	566,161,000	498,072,000
<b>TOTALS</b>	<b>\$1,367,971,000</b>	<b>\$1,454,932,000</b>	<b>\$1,978,434,000</b>	<b>\$1,977,595,000</b>	<b>\$2,148,152,000</b>

Source: Stanislaus County Department of Agriculture.

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**APPENDIX B**

**FORM OF OPINION OF SPECIAL COUNSEL**

\_\_\_\_\_, 2011

City Council  
City of Modesto  
Modesto, California

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

JPMorgan Chase Bank, National Association  
New York, New York

\$47,625,000  
CITY OF MODESTO  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

Ladies and Gentlemen:

We previously acted as special counsel to the City of Modesto (the "City"), in connection with the execution and delivery of the above-referenced certificates of participation (the "Certificates"). The Certificates were executed and delivered on May 30, 2008, and evidence and represent proportionate interests of the owners thereof in 2008 Payments (as that term is defined in the Trust Agreement referred to below) to be made by the City pursuant to that certain Master Installment Purchase Contract, dated as of November 1, 1997 (the "Master Installment Purchase Contract"), by and between the City and the Modesto Public Financing Authority (the "Authority"), as amended and supplemented by that certain 2006 Supplemental Installment Purchase Contract, dated as of November 1, 2006 (the "2006 Supplemental Installment Purchase Contract"), by and between the City and the Authority and that certain 2008 Supplemental Installment Purchase Contract, dated as of May 1, 2008 (the "2008 Supplemental Installment Purchase Contract"), by and between the City and the Authority. The Master Installment Purchase Contract, as amended and supplemented by the 2006 Supplemental Installment Purchase Contract and the 2008 Supplemental Installment Purchase Contract, is referred to herein as the "Installment Purchase Contract." All of the Authority's rights to receive such 2008 Payments were assigned on May 30, 2008, the date of execution and delivery of the Certificates, by the Authority to The Bank of New York Mellon Trust Company, N.A., as trustee (the "Trustee"), pursuant to that certain Trust Agreement, dated as of May 1, 2008 (the "Trust Agreement"), by and between the Authority and the Trustee. The Certificates were executed by the Trustee pursuant to the terms of the Trust Agreement. On May 30, 2008, the date of execution and delivery of the Certificates, we rendered our opinion that, subject to certain conditions, assumptions and limitations, interest represented by the Certificates would

be excludable from gross income retroactive to the date of execution and delivery of the Certificates for federal income tax purposes (the “Original Special Counsel Opinion”). Capitalized terms not defined herein shall have the meanings ascribed to them in the Trust Agreement or in the Original Special Counsel Opinion.

This opinion is being rendered pursuant to Section 3.11(e) of the Trust Agreement in connection with the delivery by the Authority to the Trustee of an Alternate Liquidity Facility on the date hereof in substitution for the Liquidity Facility.

In connection with our rendering the opinions set forth herein, we have reviewed the Installment Purchase Contract and the Trust Agreement and such other documents, opinions and matters to the extent we deemed necessary to render the opinions set forth herein. As to questions of fact material to our opinion, we have relied upon, and have assumed the accuracy of, the certified proceedings and other certifications of public officials and officials of the Authority furnished to us without undertaking to verify the same by independent investigation.

We have assumed the genuineness of all documents and signatures presented to us (whether as originals or as copies) and the due and legal execution and delivery thereof by, and validity against, any parties other than the Authority. Further, we have assumed compliance with all covenants contained in the Installment Purchase Contract and the Trust Agreement, including (without limitation) covenants and agreements, compliance with which is necessary to assure that actions, omissions or events on and after the execution and delivery of issuance of the Certificates have not caused and will not cause interest represented by the Certificates to be included in gross income for federal income tax purposes. We have not been engaged to undertake and we have not undertaken to determine compliance with any of such covenants and agreements or any other requirements of law, and, except as expressly set forth below, we have not otherwise reviewed any actions, omissions or events occurring after the execution and delivery of the Certificates or the exclusion of interest represented by the Certificates from gross income for federal income tax purposes. Accordingly, except as expressly set forth below, no opinion is expressed herein as to whether interest represented by the Certificates is excludable from gross income for federal income tax purposes or as to any other tax consequences related to the ownership or disposition of, or the accrual or receipt of interest represented by the Certificates.

Based upon the foregoing, under existing law, we are of the opinion that the delivery to the Trustee of an Alternate Liquidity Facility in substitution for the Liquidity Facility (i) is authorized under the Trust Agreement, (ii) complies with the terms of the Trust Agreement and (iii) will not adversely affect the exclusion of interest represented by the Certificates from gross income for purposes of federal income taxation.

The opinions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and speak as of the date hereof. Such opinions may be adversely affected by actions taken or events occurring, including a change in law, regulation or ruling (or in the application or official interpretation of any law, regulation or ruling) after such date. We have not undertaken to determine, or to inform any person, whether such actions are taken or such events occur, and we have no obligation to update this opinion in light of any such actions or events.

Respectfully submitted,

**APPENDIX C**

**EXCERPTS FROM THE CITY'S FINANCIAL STATEMENTS  
FOR FISCAL YEAR ENDING 2010**

CITY OF  
**Modesto, California**

**COMPREHENSIVE ANNUAL FINANCIAL REPORT**  
**Fiscal Year Ended June 30, 2010**

**Prepared by**  
**Finance Department**

**CITY OF MODESTO**  
 June 30, 2010  
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## **INTRODUCTORY SECTION**



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*[TDD (209) 526-9211 Hearing and Speech Impaired only]*

December 20, 2010

To the Honorable Mayor, Members of the City Council, and Citizens of the City of Modesto:

The Finance Department is pleased to present to you the Comprehensive Annual Financial Report (CAFR) for the City of Modesto. The City of Modesto City Charter and Municipal Code require that a complete (CAFR) which is comprised of a financial statement and report on the finances of the City be submitted to the City Council at the end of each fiscal year. This report is being submitted to fulfill that requirement for the fiscal year ended June 30, 2010.

City management assumes full responsibility for the completeness and reliability of the information contained in this report. We believe the data fairly represent the financial position and results of operations of the City. The disclosures necessary to enable the reader to understand the City's financial affairs have been included. The City's accounting system has been developed and maintained with due consideration given to the adequacy of internal controls. Because the cost of internal controls should not exceed the anticipated benefits, the objective is to provide reasonable, rather than absolute, assurance that the financial statements are free of any material misstatements. The evaluation of the costs and benefits of particular control requires estimates and judgments by management.

The Charter also requires an annual audit by an independent certified public accountant selected by the City Council. The accounting firm of Brown and Armstrong was selected in 2009 to perform the City's annual financial audits. The auditors have issued an unqualified ("clean") opinion on the financial statements for the year ended June 30, 2010, which is presented on page 3. In addition to meeting the City Charter audit requirements, the audit was also designed to meet the requirements of the federal Single Audit Act of 1996 and related OMB Circular A-133. The auditor's reports related specifically to the Single Audit will be presented separately at a later date.

Management's discussion and analysis (MD&A) immediately follows the independent auditor's report and provides a narrative introduction, overview, and analysis of the basic financial statements. MD&A is designed to be read in conjunction with this transmittal letter.

### **City of Modesto Profile**

Modesto is a dynamic city located in the heart of California's San Joaquin Valley and is the retail, service and financial center of Stanislaus County. The City currently occupies a land area of approximately 36 square miles and serves a population of over 211,000. Periodically, as allowed by state statute, the City extends its corporate limits by annexation when deemed appropriate by the City Council.

Incorporated in 1884, Modesto adopted its City Charter on March 12, 1951, and has operated under the council-manager form of government since that date. Under this form of government, policy-making and legislative authority are vested in an elected council consisting of the Mayor and six members. Historically, the Modesto City Council has been elected on a non-partisan basis, meaning 6 members

represent the entire City rather than specific geographical areas within the City's boundaries. Beginning with the November 2009 election, the City Council are elected on the basis of district representation as Council seats become vacant or are subject to re-election. The Mayor will continue to be elected separately on a non-partisan city-wide basis. Since February 2008, the Mayor has been responsible for the preparation of the annual budget in accordance with the Accountability Measure that was enacted at that time. Together, the Mayor and City Council are responsible for passing ordinances, adopting and amending the operating and capital budgets, appointing various committee members, and hiring the City Manager, City Attorney, City Clerk and City Auditor. The City Manager of Modesto is charged with carrying out the policies and ordinances of the City Council, overseeing the day-to-day operations of the City and for appointing the Deputy City Manager and department heads, with general responsibilities for the Economic Development and Health, Safety & Culture components of the City's Vision.

The City provides services typically associated with a municipality. These include administrative services; police and fire protection; highway, street, and utility infrastructure construction and maintenance; sanitation; planning and zoning; recreational activities and cultural events. Parking, airport facilities, water, sewer, storm drainage and bus services are also provided.

The City's financial reporting entity includes all funds and activities of the City of Modesto as the primary government and its component units, which are legally separate entities that operate under the auspices of the City and provide services that supplement City services. The City's component units are blended into the City's funds because their governing boards consist of all seven members of the City Council. These component units are the Modesto Municipal Sewer District No. 1, the Redevelopment Agency of the City of Modesto, the Modesto Public Financing Authority and the City of Modesto Community Facilities Districts.

The annual operating budget serves as the foundation for Modesto's financial planning and control. The proposed budget is adopted annually prior to July 1, by passage of a resolution. The Council's legally adopted budget level is at the fund level. During the fiscal year, the budget may be modified. The City Council has also adopted fiscal policies that delegate budget control authority to the Council, City Manager and the Director of Finance.

### **Local Economy**

The local economy continues to struggle with the effects of the recession and foreclosure crisis. Primary revenue sources of the City have been directly impacted by economic influences. Specifically, sales and property taxes have decreased approximately \$1.53 million and \$1.56 million respectively, from 2009 levels. Total revenues have decreased \$11 million or 10% during this time frame. These reductions have caused a corresponding contraction in governmental services provided to the community and a reduction in the City's General Fund budget.

The Modesto area primarily employs people in the areas in government, retail and manufacturing. Stanislaus County consistently ranks among the top 10 California counties in terms of annual agricultural production values. The county's leading commodities are milk, almonds and poultry.

The unemployment rate within the Modesto Metropolitan Statistical Area has increased significantly. At June, 30 2010, the unemployment rate was 14.02% as compared to 7.9% just over 8 years ago.

Building permit activity boomed over the past decade; however, the City has experienced virtually little building activity during the last 12 months. This lack of activity can be compared to peak levels over the last two decades. In fiscal year 1996, the City issued 4,186 permits with estimated cost of construction valued at \$114 million. Permit activity peaked in 2001, when 7,155 permits with construction valued at \$477 million were issued. In 2005, the total construction was valued at \$360 million. Since that time construction values have fallen and for the calendar year 2007 they totaled \$271 million. In 2010, there were 3,733 permits issued with an estimated cost of construction of \$67.5 million.

During the past ten years, public safety costs have risen not only in amount, but also as a percentage of total expenditures. Public safety represented 73% of total General Fund expenditures in 2010, compared with 63% ten years ago. Expenses for other governmental functions have decreased compared to total fund expenses due to the reduction in the major revenue sources from the decline in the economy. Increased staffing, driven by the growth in the population, as well as higher salaries and charges for retirement, has caused the increase in public safety charges during the past ten years.

### **Long-Term Financial Planning**

In June 2010, the City Council amended its fiscal policies to require the City to maintain at least \$7 million of General Fund expenditures in reserve in fiscal year 2010-2011. At the end of Fiscal Year 2010, the General Fund unreserved and undesignated balance was \$10.1 million representing 11.0% of total General Fund outflows (expenditures). This fund balance allows the City to respond to unplanned circumstances and maintain adequate working capital to meet its cash flow needs. The long-term maintenance of a stable fund balance is a direct reflection of the Mayor's and Council's leadership and prudent fiscal management. The Mayor and Council have employed expenditure reduction strategies in direct response to declining revenues and instead of utilizing fund balance reserves to augment declining revenues. Staff commends them for their long-term vision to ensure the fiscal well-being of the City.

### **State Impacts**

Between Fiscal Years 1991 and 2005, the State of California diverted \$36.6 million in local revenues from the City of Modesto into its own coffers. In 2005 the State enacted new legislation known as the Triple-Flip. As the name implies, a series of revenue exchanges take place leaving the City with 25% less sales tax revenue and more property tax revenue in its place. A similar exchange takes place leaving the City with property tax revenue in place of 67% of the In-Lieu Vehicle License Fees. These exchanges not only affect the character and amount of the revenues received by the City but also affect the City's cash flow, because a monthly stream of payments has been replaced by semi-annual payments. Legislation in the form of Proposition 1A was enacted by the voters in the 2004-2005 Fiscal Year to protect cities and counties from recurring raids on local revenue by the State. In November 2010, voters approved Proposition 22. Proposition 22 further restricts the State's ability to divert local government revenues to the State, thus securing local revenues for local needs.

### **Important Financial Policies**

Annually, the City Council adopts a series of financial policies that direct how the City's financial business is conducted. In addition to maintaining a stable General Fund balance, these policies include direction on departmental annual budget savings, tracking of all transfers to the Redevelopment Agency for future payback, capital budgeting, interfund loan interest rates and investment pool interest allocation.

### **Local Initiatives and Accomplishments**

Despite the fiscal challenges facing the City, staff has been able to achieve several milestones. In September 2010, the Council adopted the 2010-11 Strategic Plan. This Plan contains six strategic commitments to the community with underlying initiatives from each City department. The six commitments are as follows:

*Commitment #1* – Build and promote partnerships that engage neighborhoods and create a sense of community.

*Commitment #2* – Provide a safe and inviting community in which to live, work and visit.

*Commitment #3* – Provide an innovative and accountable city government that embraces a standard of service excellence through adaptive leadership and responsive public service.

*Commitment #4* – Foster a vibrant, competitive and diverse economic environment for business.

*Commitment #5* – Champion education partnerships.

*Commitment #6* – Promote Modesto.

Staff is in the process of linking this Strategic Plan to performance measures and its budgeting processes. As part of the Strategic Plan, staff has made 9 commitments to the Council and community. These commitments are articulated in an acronym called "EMBRACE IT!" and include:

E – Exceptional Service  
M – Measurable Success  
B – Build Trust  
R – Results Oriented  
A – Accountability  
C – Community Outreach  
E – Excite Pride

I – Innovation  
T – Teamwork

In May 2010, Council awarded contracts for the upgrade and implementation of a new Finance Enterprise (ERP) system. This system will replace several obsolete existing systems and fully integrate the financial, human resources, payroll and budget processes. Implementation is scheduled for 3 waves with a targeted go-live date for the first wave in the Spring of 2011. Staff anticipates the final wave to be implemented in the Fall of 2011.

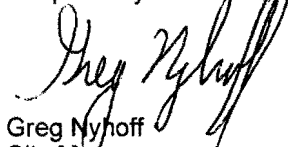
#### **Awards and Acknowledgments**

For the twenty-sixth consecutive year, the Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the City of Modesto for its comprehensive annual financial report for the fiscal year ended June 30, 2008-09. To receive this recognition, the City must publish an easily readable and efficiently organized report. The report must satisfy both generally accepted accounting principles and applicable legal requirements. The award is valid for a period of one year. We believe that the current Comprehensive Annual Financial Report continues to meet the requirements of the program, and it will be submitted to the GFOA to determine its eligibility.

The Comprehensive Annual Financial Report (CAFR) is the result of the cooperative work of many people. We wish to convey our appreciation to all members of the Finance Department team who prepared and contributed to its successful completion. In particular, we commend DeAnna Espinoza, Belinda Duerksen, and the staff of the Accounting Division responsible for the preparation of this report. Without their hard work, this report would not be possible.

In addition, we would like to express our appreciation to Mayor Jim Ridenour and the City Council. Their leadership and direction throughout the year has allowed the City to look beyond the current economic storm to strive to become something better. Thank you for your dedicated service to the residents of the City.

Respectfully submitted,

  
Greg Nyhoff  
City Manager

  
Gloriette Beck  
Director of Finance

# Certificate of Achievement for Excellence in Financial Reporting

Presented to

City of Modesto  
California

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
June 30, 2009

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



President

Executive Director

**CITIZENS OF MODESTO**

**CITY COUNCIL**  
 Jim Ridenour, Mayor  
 Dave Geer, Brad Hawn, Dave Lopez, Garrad Marsh, Joe Muratore, Kristin Olsen

*Voters Elect*

**City Manager**  
 Greg Nyhoff

**City Attorney**  
 Susana Wood

**City Clerk**  
 Stephanie Lopez

*Mayor &  
 Council Appoint*

**Acting Deputy City  
 Manager**  
 Dee Williams-Ridley

**Community &  
 Economic  
 Development**  
 Brent Sinclair  
 Director

*City Manager  
 Appoints*

**Finance**  
 Gloriette Beck  
 Director

**Police**  
 Mike Harden  
 Chief

**Information  
 Technology**  
 Kevin Harless  
 Acting CIO

**Fire**  
 Mike Kraus  
 Acting Chief

**Personnel**  
 Dee Williams-Ridley  
 Director

**Parks, Recreation  
 & Neighborhoods**  
 Julie Hannon  
 Director

**Public Works**  
 Nick Pinhey  
 Director

**CITIZENS ADVISORY BOARDS, COMMISSIONS & COMMITTEES**

- Airport Advisory Committee
- Board of Building Appeals
- Board of Zoning Adjustment
- Charter Review Committee
- Citizens Advisory Committee on Recycling
- Citizens Housing & Community Development Committee
- Citizens Redevelopment Advisory Committee
- Citizens Salary Setting Commission
- Comprehensive Fee Task Force
- Culture Commission
- Disabled Access Appeals Board
- Districting Commission

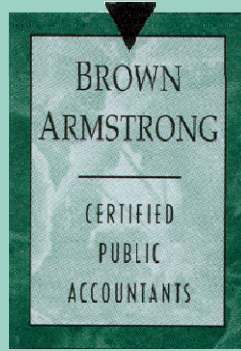
- Downtown Improvement District Advisory Board
- Entertainment Commission
- Golf Courses Advisory Committee
- Housing Rehabilitation Loan Committee
- Human Relations Commission
- Landmark Preservation Commission
- Local Cable Programming Committee
- Planning Commission
- Solid Waste Advisory Committee
- Tuolumne River Regional Park Citizens  
 Advisory Committee
- Youth Commission

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## **FINANCIAL SECTION**



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## INDEPENDENT AUDITOR'S REPORT

The Honorable City Council of the  
City of Modesto, California

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Modesto, California, as of and for the year ended June 30, 2010, which collectively comprise the City of Modesto's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City of Modesto's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the City of Modesto's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Modesto, California, as of June 30, 2010, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

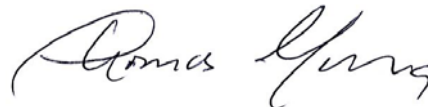
As discussed in Note 1 to the financial statements, the City of Modesto has adopted the provisions of Governmental Accounting Standards Board Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, and Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, in 2010.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 30, 2010, on our consideration of the City of Modesto's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, budgetary comparison information, and the schedule of funding progress of the City of Modesto's other postemployment benefit plan (OPEB), as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Modesto, California's financial statements as a whole. The introductory section, combining and individual nonmajor fund financial statements, and statistical section are presented for purposes of additional analysis and are not a required part of the financial statements. The combining and individual nonmajor fund financial statements are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole. The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

BROWN ARMSTRONG  
ACCOUNTANCY CORPORATION

A handwritten signature in cursive script, appearing to read "Ronald Young".

Bakersfield, California  
November 30, 2010

## Management's Discussion and Analysis

This section of the City of Modesto (City) comprehensive annual financial report presents a discussion and analysis of the City's financial performance during the fiscal year ended June 30, 2010. Please read it in conjunction with the transmittal letter at the front of this report and the basic financial statements following this section.

### FINANCIAL HIGHLIGHTS

- The assets of the City exceeded liabilities at the close of the 2010 fiscal year by \$824,207,474 (*total net assets*). Of this amount, \$162,061,296 (*unrestricted net assets*) may be used to meet ongoing obligations to citizens and creditors, \$81,528,516 is restricted for a specific purpose (*restricted net assets*), and \$580,617,662 is invested in capital assets, net of related debt.
- The City's total net assets decreased by \$5,569,973 compared to the prior year. All of this decrease is attributable to Governmental Activities.
- As of June 30, 2010, the City's governmental funds reported combined fund balances of \$113,871,596, a decrease of \$12,016,939 in comparison with the prior year. Approximately 63% of the combined fund balances, \$71,312,989 is available to meet the City's current and future needs (*unreserved fund balance*).
- At the end of the fiscal year, the General Fund balance was \$12,975,360, or 13% of total General Fund expenditures. Of this, \$2,871,715 million is reserved for encumbrances and non-current assets. The unreserved/undesignated balance of \$10,103,645 represents 11% of total General Fund outflows. The City Council has adopted a goal of maintaining an 8% unreserved fund balance amount.
- The City's total long-term liabilities showed a net increase of \$23,948,241 in comparison with the prior year. The increase is due to the derivative interest swap for both the 2008 Water Refunding Revenue Certificates of Participation and the 2008 Lease Revenue Refunding Bonds. Additionally, a \$6.4 million notes payable was reported for the Water fund due to an MID reimbursement agreement for the EIFS roofing project.

### OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis are intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements comprise three components 1) **Government-wide** financial statements; 2) **Fund** financial statements and 3) **Notes** to basic financial statements. Required Supplementary Information is included in addition to the basic financial statements.

**Government-wide Financial Statements** are designed to provide readers with a broad overview of City finances, in a manner similar to a private-sector business.

The *statement of net assets* presents information on all City assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City is improving or deteriorating.

The *statement of activities* presents information showing how net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of these government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from other functions that are intended to recover all or a portion of their costs through user fees and charges (*business-type activities*). The governmental activities of the City include general government, community development, highways and streets, public works, parks and recreation, and public safety. The business-type activities of the City include the water, sewer, parking, storm drain, airport, bus, golf and community center operations.

Component units are included in our basic financial statements and consist of legally separate entities for which the City is financially accountable and that have substantially the same board as the City Council, or provide services entirely to the City. Examples are the Redevelopment Agency of the City of Modesto and the Modesto Public Financing Authority.

**The government-wide financial statements can be found on pages 17-19 of this report.**

## Management's Discussion and Analysis (*continued*)

**Fund Financial Statements** are groupings of related accounts that are used to maintain control over resources that have been segregated for specific activities or objectives. The City, like other state and local governments, uses fund accounting to ensure and demonstrate finance-related legal compliance. All of the funds of the City can be divided into three categories: governmental funds, proprietary funds and fiduciary funds.

**Governmental funds** are used to account for essentially the same functions reported as *governmental activities* in the government-wide financial statements. However, unlike the government-wide financial statements, governmental funds financial statements focus on *near-term inflows* and *outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in evaluating the City's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental funds balance sheet and the governmental funds statement of revenues, expenditures and changes in fund balances provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

The City reports 17 individual governmental funds. Information is presented separately in the governmental funds balance sheet and in the governmental funds statement of revenues, expenditures and changes in fund balances for the General Fund, the Capital Facility Fees Fund and the Special Gas Tax Street Improvement Fund. Data from the other governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these non-major governmental funds is provided in the form of *combining statements* elsewhere in this report.

**The governmental funds financial statements can be found on pages 20-23 of this report**

**Proprietary funds** are maintained two ways. *Enterprise funds* are used to report the same functions presented as *business-type activities* in the government-wide financial statements. The City uses enterprise funds to account for its Water, Sewer, Parking, Storm Drain, Compost, Airport, Bus, Golf and Community Center operations. *Internal service funds* are an accounting device used to accumulate and allocate costs internally among the City's various functions. The City uses internal service funds to account for its Fleet Management, Central Services, Information and Technology Services, Insurance, Employee Benefits Management and Building Services functions. Because these services predominantly benefit governmental rather than business-type functions, they have been included within *governmental activities* in the government-wide financial statements. Internal services benefiting business-type functions have been allocated as "internal balances".

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The Water, Sewer and Bus funds are considered to be major funds of the City. The City's six internal service funds are combined into a single, aggregated presentation in the proprietary funds financial statements. Individual fund data for the internal service funds is provided in the form of *combining statements* elsewhere in this report.

**The proprietary funds financial statements can be found on pages 24-27 of this report.**

**Fiduciary funds** are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the City's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds except for agency funds.

**The fiduciary fund financial statements can be found on page 28 of this report.**

**Notes to Basic Financial Statements** provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes can be found on **pages 29-59** of this report.

**Required Supplementary Information** is also presented. The City adopts an annual appropriated budget. Budgetary comparison schedules for the major governmental funds have been provided to demonstrate compliance with this budget.

**Required supplementary information can be found on pages 63-67 of this report.**

## Management's Discussion and Analysis *(continued)*

The *combining and individual fund statements and schedules* referred to earlier provide information for non-major governmental, enterprise and internal service funds and are presented immediately following the required supplementary information. Combining and individual fund statements and schedules can be found on **pages 71-107** of this report.

### GOVERNMENT-WIDE FINANCIAL ANALYSIS

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the City, assets exceeded liabilities by \$824,207,474 at the close of the most recent fiscal year.

#### Net Assets

	Governmental activities		Business-type activities		Total	
	2010	2009	2010	2009	2010	2009
Current and other assets	\$220,010,362	\$215,486,724	\$183,857,214	\$197,977,889	\$403,867,576	\$413,464,613
Capital assets	398,476,708	402,097,561	372,756,536	336,708,420	771,233,244	738,805,981
Total assets	618,487,070	617,584,285	556,613,750	534,686,309	1,175,100,820	1,152,270,594
Current and other liabilities	26,219,061	21,092,495	16,793,089	17,467,696	43,012,150	\$38,560,191
Long-term liabilities	166,747,546	154,786,927	141,133,650	129,146,029	307,881,196	283,932,956
Total liabilities	192,966,607	175,879,422	157,926,739	146,613,725	350,893,346	322,493,147
Net assets:						
Invested in capital assets, net of related debt	329,592,169	347,357,492	251,025,494	218,432,739	580,617,663	\$565,790,231
Restricted net assets	81,528,516	94,819,773			81,528,516	\$94,819,773
Unrestricted net assets	14,399,778	(472,402)	147,661,517	169,639,845	162,061,295	169,167,443
Total net assets	\$425,520,463	\$441,704,863	\$398,687,011	\$388,072,584	\$824,207,474	\$829,777,447

The largest portion of the City's net assets, \$580,617,663 (71 percent), reflects its investment in capital assets (e.g. land, buildings, improvements, furnishings and equipment, buses and fare boxes, pipelines, and infrastructure), less any related debt used to acquire those assets that is still outstanding. The City uses these capital assets to provide services to citizens; consequently, these assets are *not* available for future spending. Although the City's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

Another significant portion of the City's net assets represents *unrestricted net assets* of \$162,061,295 (20 percent), which may be used to meet the City's ongoing obligations to citizens and creditors.

The remaining balance of the City's net assets of \$81,528,516 (9 percent) represents resources that are subject to external restrictions on how they may be used.

At the end of the 2010 fiscal year, the City reported positive balances in all three categories of net assets for the City as a whole.

The City's net assets decreased by \$5,569,973 during the current fiscal year.

## Management's Discussion and Analysis *(continued)*

The following table indicates the changes in net assets for governmental and business-type activities, as well as comparative data for the prior year:

	Changes in Net Assets					
	Governmental activities		Business-type activities		Total	
	2010	2009	2010	2009	2010	2009
Revenues:						
Program revenues:						
Charges for services	\$25,775,676	\$29,979,644	\$106,214,203	\$103,112,157	\$131,989,879	133,091,801
Operating grants and contributions	14,559,357	11,424,548	13,706,512	11,462,346	28,265,869	22,886,894
Capital grants and contributions	10,876,018	6,595,213	2,898,489	4,527,875	13,774,507	11,123,088
General revenues:						
Taxes	52,606,197	55,345,729	265,587	202,460	52,871,784	55,548,189
Intergovernment revenue not restricted for specific purposes	37,532,698	43,119,384			37,532,698	43,119,384
Unrestricted investment earnings	1,211,702	5,247,506	3,155,954	6,227,615	4,367,656	11,475,121
Settlements and recoveries			447,102	253,032	447,102	253,032
Miscellaneous	2,502,397	5,809,581			2,502,397	5,809,581
Total revenues	145,064,045	157,521,605	126,687,847	125,785,485	271,751,892	283,307,090
Expenses:						
General government	12,093,091	12,700,264			12,093,091	12,700,264
Community development	18,912,766	14,694,997			18,912,766	14,694,997
Highways and streets	23,668,779	23,682,253			23,668,779	23,682,253
Public works	6,759,562	9,151,786			6,759,562	9,151,786
Parks and recreation	13,268,871	15,070,007			13,268,871	15,070,007
Public safety	80,254,834	84,395,987			80,254,834	84,395,987
Interest on long-term debt	5,766,421	6,114,875			5,766,421	6,114,875
Parking			1,826,401	2,011,386	1,826,401	2,011,386
Water			43,619,704	38,190,214	43,619,704	38,190,214
Sewer			28,055,056	22,416,713	28,055,056	22,416,713
Storm drain			5,201,741	6,140,963	5,201,741	6,140,963
Compost			1,480,068	1,130,816	1,480,068	1,130,816
Airport			1,918,113	1,682,644	1,918,113	1,682,644
Bus			15,671,731	15,210,224	15,671,731	15,210,224
Golf			2,473,968	2,440,599	2,473,968	2,440,599
Community center			2,346,175	2,303,256	2,346,175	2,303,256
Total expenses	160,724,324	165,810,169	102,592,957	91,526,815	263,317,281	257,336,984
Increase in net assets before transfers	(15,660,279)	(8,288,564)	24,094,890	34,258,670	8,434,611	25,970,106
Transfers	402,303	(5,490,881)	(402,303)	5,490,881	0	
Special item			(1,326,309)	(2,211,514)	(1,326,309)	(2,211,514)
Change in net assets	(15,257,976)	(13,779,445)	22,366,278	37,538,037	7,108,302	23,758,592
Net assets - beginning, as restated	441,704,863	446,626,848	388,072,584	358,227,618	829,777,447	804,854,466
Prior year adjustments	(926,424)	8,857,460	(11,751,851)	(7,693,071)	(12,678,275)	1,164,389
Net assets - ending	\$425,520,463	\$441,704,863	\$398,687,011	\$388,072,584	\$824,207,474	\$829,777,447

**Governmental activities.** Governmental activities decreased the City's net assets by \$16,184,400. Taxes declined about \$2.7 million compared to 2009 due to the continuous reassessment of property values due to the housing crisis. Intergovernmental revenues reflect a decrease of approximately \$5.6 million, mostly due to sales tax declined by \$2.3 million and Motor Vehicle License revenue decrease by \$1.3 million due to the economic conditions. Finally, investment earnings dropped by \$4 million due to absorbing cash flows to cover the reduction in major revenue sources. Charges for services have decreased by \$4.2 million compared to the prior year, due to two divisions moving to the Water Fund. The main services provided by Utilities and Collections and Cashiering is in support of the utility funds.

## Management's Discussion and Analysis (continued)

Expenses in total were lower compared to the prior year by \$5.1 million, or 4%, due mainly to strategic spending reductions implemented by the City Council in response to lower revenue estimates and a cyclical decline in the value of construction projects undertaken.

**Business-type activities.** Business-type activities increased the City's net assets by \$10,614,427. As detailed in the schedule on **page 12**, net losses were experienced by Parking, Compost, Airport, Golf and Community Center operations. Depreciation expense, which is the major cause of these net losses, is not included in these funds' budgets or revenue-setting processes.

Charges for services increased by approximately \$3.1 million due to a 2.1% CPI rate increase for water rates and a sewer rate increase in this fiscal year.

### FINANCIAL ANALYSIS OF THE CITY'S FUNDS

As noted earlier, the City uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

**Governmental funds.** The general government functions are contained in the general, special revenue, capital projects, and debt service funds. The focus of the City's *governmental funds* is to provide information on near-term inflows, outflows, and balances of *spendable* resources. Such information is useful in assessing the City's financing requirements. In particular, *unreserved fund balance* may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

At June 30, 2010, the City's governmental funds reported combined fund balances of \$113,871,596, a decrease of \$12,016,939 from the prior year. Approximately 63% of the combined fund balances (\$71,312,989) constitute *unreserved fund balance*, which is available to meet the City's current and future needs. The remainder of fund balance is *reserved* to indicate that it is *not* available for new spending because it has been committed: 1) to pay debt service (\$6,050,302); 2) to reflect advances to other funds, loans receivable and property held for resale that are long-term and/or do not represent available spendable resources (\$22,912,438); 3) to liquidate contractual commitments of the period (\$12,540,475); and 4) to meet Redevelopment Agency low and moderate income housing set-aside requirements (\$1,055,392).

The General Fund is the chief operating fund of the City. At June 30, 2010, unreserved fund balance of the General Fund was \$10,103,645 while total fund balance was \$12,975,360. As a measure of the General Fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved fund balance represents 11.0% of total fund expenditures, while total fund balance represents 13.2% of that same amount. The prior year ratios were 10.0% and 13%, respectively. The use of the fund balance reserves was planned and budgeted during the year.

Revenues of governmental funds totaled \$144,321,053 in fiscal year 2009-10, which represents a decrease of 8.8% from fiscal year 2008-09.

Expenditures of governmental funds totaled \$155,605,865 in fiscal year 2009-10, representing a decrease of 8.4% over the prior year.

## Management's Discussion and Analysis *(continued)*

The following table presents governmental fund revenues from various sources, with comparisons to the prior year:

### Revenues Classified by Source – Governmental Funds

Revenues by Source	FY 2010		FY 2009		Increase (Decrease)	
	Amount	Percent	Amount	Percent	Amount	% Change
Taxes	\$52,606,197	36.5%	\$55,345,729	35.0%	(\$2,739,532)	-4.9%
Licenses and permits	138,811	0.1%	132,459	0.1%	6,352	4.8%
Intergovernmental	61,551,617	42.6%	63,606,634	40.2%	(2,055,017)	-3.2%
Charges for services	23,509,170	16.3%	27,051,151	17.1%	(3,541,981)	-13.1%
Special assessments	38,520	0.0%	37,299	0.0%	1,221	3.3%
Interest and rent	1,322,005	0.9%	2,909,155	1.8%	(1,587,150)	-54.6%
Net increase (decrease) in fair value	399,322	0.03%	860,820	0.5%	(461,498)	-53.6%
Fines and forfeits	2,253,014	1.6%	2,443,506	1.5%	(190,492)	-7.8%
Miscellaneous	2,502,397	1.6%	5,809,581	3.6%	(3,307,184)	-56.9%
<b>Total</b>	<b>\$144,321,053</b>	<b>100.0%</b>	<b>\$158,196,334</b>	<b>100.0%</b>	<b>(\$13,875,281)</b>	<b>-8.8%</b>

- Taxes –Property taxes and Redevelopment Agency Tax Increment (an allocation of property taxes) decreased by \$1,556,769 and \$563,560 respectively, due mainly to the drop in the sales prices of homes affecting the amount of supplemental tax payments received.
- Intergovernmental – State sales taxes and motor vehicle license fees make up over half of these revenues. Sales tax revenues were lower by \$1.5 million, and vehicle license fees decreased by \$1.3 million due mainly from a decline in consumer spending and an increase in the unemployment rate.
- Charges for services – Included in this category are the Capital Facilities and Community Facility District Fees charged to mitigate the impact of new development on City infrastructure needs. Capital Facility Fees collected during the year were down significantly due to the halt in new housing starts.
- Investment revenues decreased due to a reduction of cash balances and interest rates.

The following table presents expenditures by function compared to prior year amounts.

### Expenditures by Functions Governmental Funds

Exp by Function	FY 2010		FY 2009		Increase (Decrease)	
	Amount	Percent	Amount	Percent	Amount	% Change
General government	\$11,482,240	7.4%	\$13,715,577	8.1%	(\$2,233,337)	-16.3%
Community development	18,536,120	11.9%	14,137,095	8.3%	4,399,025	31.1%
Highways and streets	8,102,327	5.2%	9,721,445	5.7%	(1,619,118)	-16.7%
Public works	6,124,685	3.9%	7,667,125	4.5%	(1,542,440)	-20.1%
Parks and recreation	12,138,077	7.8%	13,307,764	7.8%	(1,169,687)	-8.8%
Public safety	75,081,791	48.3%	78,103,260	46.0%	(3,021,469)	-3.9%
Capital outlay	16,655,242	10.7%	27,663,037	16.3%	(11,007,795)	-39.8%
Debt Service-principal retirement	2,045,000	1.3%	1,093,000	0.6%	952,000	87.1%
Debt Service-interest charges	4,032,612	2.6%	3,033,829	1.8%	998,783	32.9%
Debt Service- other	1,408,771	0.9%	1,395,211	0.8%	13,560	1.0%
<b>Total</b>	<b>\$155,606,865</b>	<b>100.0%</b>	<b>\$169,837,343</b>	<b>100.0%</b>	<b>(\$14,230,478)</b>	<b>-8.4%</b>

The following provides an explanation of the expenditures by function that changed significantly over the prior year:

- General government –Expenditures decreased about \$2,233,337 or 16.3% over the prior year, due to the continuous budget reductions put into place due to a reduction in the major revenue sources.

## Management's Discussion and Analysis *(continued)*

- Community development – Expenditures increased \$4,399,025, or 31.1% over the prior year, due to the funding received from the Neighborhood Stabilization program and American Recovery and Reinvestment Act of 2009.
- Public Works – Expenditures decreased \$1,542,440, or 20.1% over the prior year, due to budget reductions put into place due to a reduction in gas tax revenues and General Fund subsidies.
- Public safety – Expenditures decreased \$3,021,469, or 3.9% over the prior year, due to budget reductions put into place due to a reduction in the major revenue sources.
- Capital outlay – The decreased by \$11,007,795 or 39.8% reflects the current cycle that the city is in with respect to the planning and construction of capital improvements.

Other financing sources and uses are presented below to illustrate changes from the prior year:

	FY 2010	FY 2009	Increase/(Decrease)	
			Amount	Percent
Transfers in	\$12,346,246	\$19,237,526	(\$6,891,280)	-35.8%
Transfers out	(12,402,937)	(18,149,564)	(5,749,627)	-31.7%
Issuance of loans payable		209,575	(209,575)	-100.0%
Issuance of lease revenue bonds		65,170,000)	(65,170,000)	-100.0%
Refunding of lease revenue bonds		(65,210,000)	(65,210,000)	-100.0%
Other debt issuance cost		(2,431,247)	(2,431,247)	-100.0%
Sale of assets		34,900	(34,900)	-100.0%
Net financing sources (uses)	(\$56,691)	(\$1,138,810)	(\$145,693,629)	-567.5%

Transfers - The City uses interfund transfers to: (1) move resources from a fund to other funds that will utilize them in accordance with statutory and budgetary requirements, (2) utilize unrestricted resources collected in the General Fund to help finance various programs and capital projects accounted for in other funds in accordance with budgetary authorization, and (3) move cash to pay debt service to the funds that are responsible for payment as those payments become due.

- The net transfers *from* governmental funds for 2010 were \$56,691 compared to \$1,087,962, in the prior year. This net transfer is *to* various City funds including transferring funds from the General Fund, Capital Facility Fee funds and the Redevelopment Agency to the Public Financing Authority to cover the debt service payments and various transfers to cover City grant matches.
- The annual totals for both transfers in and out vary, depending on the nature of the activities that are undertaken each year.

Debt transactions – No new debt was issued for the governmental funds. A new capital lease was reported for the new Oracle Financial system in the amount of \$893K.

## Management's Discussion and Analysis *(continued)*

The current year excess of revenues and other financing sources over expenditures and other financing uses is presented in the following table:

Statement of Revenues, Expenditures, and Changes in Fund Balances  
Governmental Funds

	Major Funds			Nonmajor Funds			
	General Fund	Capital Facility Fees Fund	Special Gas Tax Street Improvement	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	Total
Revenues	\$100,952,900	\$2,215,647	\$5,067,841	\$23,219,183	\$7,599,380	\$5,266,102	\$144,321,053
Expenditures	(99,791,303)	(7,854,573)	(8,119,412)	(20,256,046)	(10,514,640)	(9,070,891)	(155,606,865)
Other financing sources/(uses), net	(2,939,995)	(911,720)	364,814	(502,001)	139,170	3,793,041	(56,691)
Net change in fund balances	(1,778,398)	(6,550,646)	(2,686,757)	2,461,136	(2,776,090)	(11,748)	(11,342,503)
Fund balance-July 1	14,753,758	39,650,167	6,877,454	23,961,736	33,677,448	6,967,972	125,888,535
Prior year adjustment			(674,436)				(674,436)
Fund balance June 30	\$12,975,360	\$33,099,521	\$3,516,261	\$26,422,872	\$30,901,358	\$6,956,224	\$113,871,596

The fund balance of the City's General Fund decreased by \$1,778,398 during the fiscal year. This result is consistent with the City Council's budgetary direction to reduce spending and identify additional revenue sources that would allow the General Fund to retain an unrestricted reserve that meets the City Council's adopted 8% level.

Capital Facility Fee revenues, derived from impact fees on new development, decreased \$6.6 million from the prior year, due to of the overall market conditions in the housing market. Spending on capital projects decreased by \$10.9 million for major construction projects. The remaining fund balance is targeted to be spent on large, multi-year capital projects to mitigate the effects of growth on the community.

**Proprietary funds.** The City's proprietary fund disclosures provide the same type of information found in the government-wide financial statements, but in more detail.

The following table shows actual revenues, expenses and results of operations of enterprise funds for the current fiscal year:

	Major Funds			Nonmajor Funds						
	Water	Sewer	Bus	Storm			Community			Total
				Parking	Drain	Compost	Airport	Golf	Center	
Operating revenues	\$54,670,041	\$37,310,731	\$2,769,814	\$1,239,995	\$5,428,291	\$1,706,189	\$675,565	\$1,924,015	\$489,562	\$106,214,203
Operating expenses	(42,186,300)	(25,301,269)	(15,490,948)	(1,791,282)	(5,126,315)	(1,469,551)	(1,906,686)	(2,206,793)	(2,336,480)	(97,815,624)
Non-operating revenues (expenses), net	285,360	(1,249,564)	13,558,808	(19,333)	54,467	8,966	450,984	(183,414)	418,211	\$13,324,485
Income (loss) before capital contributions, transfers and special items	12,769,101	10,759,898	837,674	(570,620)	356,443	245,604	(780,137)	(466,192)	(1,428,707)	21,723,064
Contributions, transfers and special items	(951,773)	(191,455)	860,240	(59,046)	491,841	(113,902)	599,938	270,000	264,034	1,169,877
Net income (loss)	\$11,817,328	\$10,568,443	\$1,697,914	(\$629,666)	\$848,284	\$131,702	(\$180,199)	(\$196,192)	(\$1,164,673)	\$22,892,941

The Water, Sewer, Storm Drain, and Compost enterprises posted net incomes during the period. It is important to note that while the Water and Sewer funds show rather healthy operating results, capital improvement expenses and debt service principal payments incurred during the year are not reflected in the expenses totals shown above. Net losses were experienced by the other enterprise funds. Golf operations did receive an operating subsidy from the General Fund in 2010. The Community Center operation also receive its annual operating subsidy from the General Fund, the subsidy

## Management's Discussion and Analysis *(continued)*

does not cover depreciation expenses, resulting in the net loss shown. The Bus Fund, which receives capital funding from the federal government also does not budget revenues at levels sufficient to cover the annual cost of depreciation expense.

Revenues in the Water utility fund rose slightly due to the 2.1% CPI rate increase. Additionally, the Sewer utility fund had an increase in revenue due to the rate increases for this fiscal year.

### GENERAL FUND BUDGETARY HIGHLIGHTS

Budget to actual information for the major governmental funds are presented as Required Supplementary Information, beginning on **page 65** of this report.

While the City Council amended the budget several times, the differences between the original budget and the final amended budget for the General Fund were increased overall mainly due to an increase in fines and forfeitures, service credit revenues and sales in real property which was not anticipated during the original budget. The estimated revenues increased about \$.5 million (.6%), while total appropriations were increased \$2 million, or about 2%. These amendments were to adjust the actual beginning balances and carryovers after closing the prior fiscal year, and to reflect adjustments to current estimates based on the periodic monitoring of revenue and expenditures throughout the year.

Revenues came in \$2.4 million less than final estimates. Variances in Sales tax (\$780,897), Property taxes (\$163,697) and construction related revenues (\$1,141,006) were due to the effects of the sub-prime mortgage market that were being fully realized during the fiscal year.

Expenditures, overall, were \$5.4 million under budget, primarily due to efforts of departments to realize savings, and certain purchases being deferred to future periods.

### CAPITAL ASSETS AND DEBT ADMINISTRATION

#### Capital assets

The City's investment in capital assets for its governmental and business-type activities as of June 30, 2010, amounted to \$771,233,244 (net of accumulated depreciation). The total increase in the City's investment in capital assets for the current period was 4.4 percent. Capital assets net of depreciation, for the governmental and business-type activities are presented below to illustrate changes from the prior year.

	Governmental		Business type		Total		Increase (decrease) Percent Change	\$ change
	2010	2009	2010	2009	2010	2009		
Land	\$32,690,491	\$32,082,218	\$30,068,229	\$29,806,353	\$62,758,720	\$61,888,571	1.4%	\$870,149
Buildings	16,630,984	17,664,826	38,456,244	40,976,318	55,087,228	58,641,144	-6.1%	(3,553,916)
Improvements	38,115,248	24,156,102	89,562,227	69,746,335	127,677,475	93,902,437	36.0%	33,775,038
Furnishings and equipment	5,184,473	9,186,540	6,144,174	2,716,957	11,328,647	11,903,497	-4.8%	(574,850)
Intangible Assets	1,982,328		131,546		2,113,874		100.0%	2,113,874
Equipment pool	11,873,219	13,198,479			11,873,219	13,198,479	-10.0%	(1,325,260)
Streets	250,374,786	248,228,636			250,374,786	248,228,636	0.9%	2,146,150
Signalization	3,865,206	5,270,489			3,865,206	5,270,489	-26.7%	(1,405,283)
Bridges	22,718,265	23,026,849			22,718,265	23,026,849	-1.3%	(308,584)
Buses & fareboxes			5,521,707	7,098,477	5,521,707	7,098,477	-22.2%	(1,576,770)
Pipelines			118,963,188	119,580,720	118,963,188	119,580,720	-0.5%	(617,532)
Construction in progress	15,041,708	29,283,421	83,909,221	66,783,260	98,950,929	96,066,681	3.0%	2,884,248
<b>Total</b>	<b>\$398,476,708</b>	<b>\$402,097,560</b>	<b>\$372,756,536</b>	<b>\$336,708,420</b>	<b>\$771,233,244</b>	<b>\$738,805,980</b>	<b>4.4%</b>	<b>\$32,427,264</b>

Major capital asset events during the current fiscal year included the following:

- Construction in progress –Business type increases were in Water and related to both system-wide improvements and those being made in conjunction with the expansion of the surface water treatment plant. The wastewater program also had significant growth related to the Phase 1 & 2 plant improvements at the primary treatment facility that continue from the prior year.

## Management's Discussion and Analysis (continued)

The City's infrastructure assets are recorded at historical cost in the government-wide financial statements. Depreciation expense is recorded using the straight-line method, based on estimated useful life of the asset. Additional information on the City's capital assets can be found in note II.B on pages 38-39 of this report.

### Long-term debt

At June 30, 2010, the City had total long-term liabilities outstanding of \$307,881,197, net of unamortized discounts and deferred amounts on refunding, as compared to \$283,932,956 in the prior year. This amount was comprised of \$64,275,000 of lease revenue bonds, \$85,081,213 of certificates of participation, \$46,750,801 of revenue bonds payable, \$11,739,301 of estimated compensated absences, \$45,527,073 of OPEB obligation, \$21,270,905 of claims liability, \$8,722,995 of loans payable, \$1,798,431 of developer advances, \$1,221,553 of capital leases, \$3,802,436 of notes payable and \$17,691,489 of Derivative instrument SWAP. The long-term debt increase was primarily due to the requirements of GASB 53 which is to account for the Derivative instrument SWAP. Additionally, a new capital lease was reported for the new Oracle lease for the City's new financial system which is scheduled to go live in April 2011. Additional information on the City's long-term debt can be found in note II.C on pages 40-47 of this report.

Modesto maintains an Employee Benefits internal service fund (EBF) to pay a portion of retiree health benefits and other employee related expenses. The City implemented GASB Statement No. 45 related to Other Post Employment Benefits during fiscal year 2008. As of June 30, 2010, the net OPEB obligation amounts to approximately \$45.5 million. This contributes significantly to the EBF's \$40.0 million deficit net assets. Additional information on the City's EBF can be found in Notes II-H and III-G.

### Economic Factors and Next Year's Budget and Rates

- *Consumer Price Index* – Growth in the CPI has been relatively stable during the past seven years and serves as a measure for the growth in the cost for supplies and services used by the city. In the year ending June 30, 2010, the CPI-Western Urban Index increased by 1.2%.
- *Taxable Sales* – With the unemployment rate at 14.02%, sales tax revenues continue to decrease going into fiscal year 2010. The City has taken action to implement non-paid furloughs and have eliminated 50 staffing positions as part of the adoption of the Fiscal Year 2010-11 budget to maintain the affects of the reduction of the City's major revenue sources.
- *Utility Service Charges* - Water utility rates were increased by 2.1% for the annual CPI increase in this fiscal year and are currently working on rate increases for the coming years. For the Sewer utility rates, the City Council adopted a resolution approving and implementing 5 annual rate increases for Wastewater beginning with a 3% rate increase on July 1, 2010 and subsequent rate increases of 8%, 9%, 10% and 7% to take effect on July 1 of 2011 through 2014.

All of these factors were considered in preparing the City's budget for fiscal year 2010.

During the current fiscal year, unreserved fund balance in the General Fund decreased by \$1.1 million, to \$10,103,645 which represents 11% of total General Fund outflows which equals City Council's target value of 8%. The budget adopted for fiscal year 2010-2011 reflects a planned reduction in the reserve level on a temporary basis, from 8% to a flat reserve amount of \$7 million.

### Requests for Information

This financial report is designed to provide a general overview of the City's finances for all those with an interest in the City's financial condition. Questions concerning any of the information provided in this report and requests for additional financial information should be addressed to the City of Modesto, Attention: Finance Department, P.O. Box 642, Modesto, CA 95353

# **BASIC FINANCIAL STATEMENTS**



**CITY OF MODESTO**  
**STATEMENT OF NET ASSETS**  
**June 30, 2010**

	<u>Governmental</u> Activities	<u>Business-type</u> Activities	<u>Total</u>
<u>ASSETS</u>			
Cash and cash equivalents	\$ 148,843,837	\$ 162,980,156	\$ 311,823,993
Accounts receivable, net	871,502	249,321	1,120,823
Interest receivable	227,536	269,102	496,638
Utility billings receivable, net	1,458,987	11,035,210	12,494,197
Taxes receivable	8,251,141	18	8,251,159
Due from governments, net	8,430,453	2,199,199	10,629,652
Notes receivable, net	22,415,295		22,415,295
Prepaid expenses	189,000		189,000
Property held for resale	784,000	630,000	1,414,000
Internal balances	3,068,357	(3,068,357)	-
Inventories	482,315		482,315
Unamortized costs of debt issuance		2,043,688	2,043,688
Deferred outflow of resource	10,172,612	7,518,877	17,691,489
Investments in joint ventures	14,815,327		14,815,327
Capital assets:			
Land and construction in progress	47,732,199	113,977,450	161,709,649
Other capital assets, net of accumulated depreciation	<u>350,744,509</u>	<u>258,779,086</u>	<u>609,523,595</u>
<b>Total assets</b>	<u>618,487,070</u>	<u>556,613,750</u>	<u>1,175,100,820</u>
<u>LIABILITIES</u>			
Accounts payable	6,475,623	9,337,951	15,813,574
Accrued salaries and benefits	2,276,073	536,365	2,812,438
Approved loans payable	875,041		875,041
Interest payable	341,112	655,008	996,120
Due to other governments	217,997		217,997
Unearned revenues	13,490,014	4,525,966	18,015,980
Refundable deposits	2,543,200	1,737,799	4,280,999
Long-term liabilities:			
Due within one year	11,384,599	5,454,148	16,838,747
Due in more than one year	<u>155,362,948</u>	<u>135,679,502</u>	<u>291,042,450</u>
<b>Total liabilities</b>	<u>192,966,607</u>	<u>157,926,739</u>	<u>350,893,346</u>
<u>NET ASSETS</u>			
Invested in capital assets, net of related debt	329,592,168	251,025,494	580,617,662
Restricted for:			
Capital projects	22,067,062		22,067,062
Housing and community development	21,155,647		21,155,647
Redevelopment	5,449,419		5,449,419
Other purposes	32,856,388		32,856,388
Unrestricted	<u>14,399,779</u>	<u>147,661,517</u>	<u>162,061,296</u>
<b>Total net assets</b>	<u>\$ 425,520,463</u>	<u>\$ 398,687,011</u>	<u>\$ 824,207,474</u>

The notes to basic financial statements are an integral part of this statement.

**CITY OF MODESTO**  
**STATEMENT OF ACTIVITIES**  
**Year ended June 30, 2010**

FUNCTIONS/PROGRAMS:	Program Revenues			
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
Governmental activities:				
General government	\$ 12,093,091	\$ 6,323,865		
Community development	18,912,766	2,941,932	121,517	
Highways and streets	23,668,779	2,801,213	1,703,016	\$ 8,218,591
Public works	6,759,562	3,344,967	6,143	
Parks and recreation	13,268,871	6,038,468	8,817,912	2,657,427
Public safety	80,254,834	4,325,231	3,910,769	
Interest on long-term debt	5,766,421			
Total governmental activities	160,724,324	25,775,676	14,559,357	10,876,018
Business-type activities:				
Parking	1,826,401	1,239,995		
Water	43,619,704	54,670,041		652,693
Sewer	28,055,056	37,310,731	50,000	867,697
Storm Drain	5,201,741	5,428,291	(1,669)	113,862
Compost	1,480,068	1,706,189		
Airport	1,918,113	675,565		599,938
Bus	15,671,731	2,769,814	13,658,181	664,299
Golf	2,473,968	1,924,015		
Community Center	2,346,175	489,562		
Total business-type activities	102,592,957	106,214,203	13,706,512	2,898,489
<b>Total</b>	<b>\$ 263,317,281</b>	<b>\$ 131,989,879</b>	<b>\$ 28,265,869</b>	<b>\$ 13,774,507</b>

General revenues:

Taxes:

  Utility users tax

  Property taxes, levied for general purposes

  Property taxes, generated by and allocated to the airport

  Tax increments for redevelopment agency

  Transient occupancy tax

  Franchise tax

  Business license tax, levied for general purposes

  Business license tax, levied for downtown improvement district

  Sales tax

  Motor vehicle license fee

  Other

Unrestricted investment earnings

Miscellaneous

Settlements

Transfers, net

Special item - PCE legal fees

Total general revenues, transfers and special item

Change in net assets

Net assets, July 1, (as restated)

Prior year adjustments

Net assets, June 30

The notes to basic financial statements are an integral part of this statement.

Net (Expense) Revenue and Changes in Net Assets		
Governmental Activities	Business-type Activities	Total
\$ (5,769,226)		\$ (5,769,226)
(15,849,317)		(15,849,317)
(10,945,959)		(10,945,959)
(3,408,452)		(3,408,452)
4,244,936		4,244,936
(72,018,834)		(72,018,834)
(5,766,421)		(5,766,421)
<u>(109,513,273)</u>		<u>(109,513,273)</u>
	\$ (586,406)	(586,406)
	11,703,030	11,703,030
	10,173,372	10,173,372
	338,743	338,743
	226,121	226,121
	(642,610)	(642,610)
	1,420,563	1,420,563
	(549,953)	(549,953)
	<u>(1,856,613)</u>	<u>(1,856,613)</u>
	<u>20,226,247</u>	<u>20,226,247</u>
<u>(109,513,273)</u>	<u>20,226,247</u>	<u>(89,287,026)</u>
12,306,702		12,306,702
19,117,518		19,117,518
	265,587	265,587
6,521,515		6,521,515
1,460,613		1,460,613
3,962,159		3,962,159
9,068,219		9,068,219
169,471		169,471
22,301,060		22,301,060
13,945,172		13,945,172
1,286,466		1,286,466
1,211,702	3,155,954	4,367,656
2,502,397		2,502,397
	447,102	447,102
402,303	(402,303)	0
	<u>(1,326,309)</u>	<u>(1,326,309)</u>
<u>94,255,297</u>	<u>2,140,031</u>	<u>96,395,328</u>
(15,257,976)	22,366,278	7,108,302
441,704,863	388,072,584	829,777,447
<u>(926,424)</u>	<u>(11,751,851)</u>	<u>(12,678,275)</u>
<u>\$ 425,520,463</u>	<u>\$ 398,687,011</u>	<u>\$ 824,207,474</u>

**CITY OF MODESTO**  
**BALANCE SHEET - GOVERNMENTAL FUNDS**  
**June 30, 2010**

	General	Capital Facility Fees	Special Gas Tax Street Improvement	Other Governmental	Total Governmental
<b>ASSETS</b>					
Cash and cash equivalents	\$ 2,739,716	\$ 35,030,473	\$ 13,803,819	\$ 24,056,437	\$ 75,630,445
Cash and cash equivalents with fiscal agent				19,125,018	19,125,018
Receivables:					
Accounts	235,187	84	24,574	382,646	642,491
Interest	18,721	61,730	19,758	47,672	147,881
Utilities, net	995,485			463,502	1,458,987
Taxes	7,790,716		229,259	231,166	8,251,141
Due from governments	387,621	641,105	577,992	6,681,273	8,287,991
Due from other funds	3,669,777				3,669,777
Notes receivable, net				22,415,295	22,415,295
Property held for resale				784,000	784,000
Restricted assets:					
Cash and cash equivalents	1,605,352			639,616	2,244,968
Advances to other funds	2,629,429			1,249,071	3,878,500
<b>Total assets</b>	<b>\$ 20,072,004</b>	<b>\$ 35,733,392</b>	<b>\$ 14,655,402</b>	<b>\$ 76,075,696</b>	<b>\$ 146,536,494</b>
<b>LIABILITIES AND FUND BALANCES</b>					
<b>Liabilities:</b>					
Accounts payable	\$ 1,329,614	\$ 1,090,437	\$ 346,084	\$ 2,472,652	\$ 5,238,787
Accrued salaries and benefits	1,822,093		96,789	192,181	2,111,063
Accrued interest payable	62,713			32,113	94,826
Approved loans payable				875,041	875,041
Due to other governments	217,997				217,997
Due to other funds				3,407,995	3,407,995
Deferred revenues	1,761,643	484,436	10,696,268	2,679,846	15,622,193
Payable from restricted assets:					
Refundable deposits	1,902,584			640,616	2,543,200
Advances from other funds		1,058,998		1,494,798	2,553,796
<b>Total liabilities</b>	<b>7,096,644</b>	<b>2,633,871</b>	<b>11,139,141</b>	<b>11,795,242</b>	<b>32,664,898</b>
<b>Fund balances:</b>					
Reserved	2,871,715	3,863,854	19,671	35,803,367	42,558,607
Unreserved:					
Designated, reported in:					
General fund					
Special revenue funds				2,208,654	2,208,654
Capital projects funds		29,235,667		2,847,531	32,083,198
Undesignated, reported in:					
General fund	10,103,645				10,103,645
Special revenue funds			3,496,590	1,162,506	4,659,096
Capital projects funds				22,258,396	22,258,396
<b>Total fund balances</b>	<b>12,975,360</b>	<b>33,099,521</b>	<b>3,516,261</b>	<b>64,280,454</b>	<b>113,871,596</b>
<b>Total liabilities and fund balances</b>	<b>\$ 20,072,004</b>	<b>\$ 35,733,392</b>	<b>\$ 14,655,402</b>	<b>\$ 76,075,696</b>	<b>\$ 146,536,494</b>

**CITY OF MODESTO**  
**RECONCILIATION OF THE BALANCE SHEET OF GOVERNMENTAL FUNDS**  
**TO THE STATEMENT OF NET ASSETS - GOVERNMENTAL ACTIVITIES**  
**June 30, 2010**

Total fund balances - total governmental funds \$ 113,871,596

Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the governmental funds.

General capital assets:

Nondepreciable	\$ 46,156,075	
Depreciable	106,752,094	
Accumulated depreciation on general capital assets	(49,259,506)	

Infrastructure:

Depreciable	530,425,544	
Accumulated depreciation on infrastructure	<u>(253,467,287)</u>	380,606,920

Other long-term assets are not available to pay for current-period expenditures and, therefore, are:

Deferred in the governmental funds, or	\$ 2,132,178	
Investments in joint ventures	<u>14,815,327</u>	16,947,505

Internal service funds are used by management to charge the costs of activities to individual funds. The assets and liabilities of internal service funds are included in governmental activities in the statement of net assets. 1,606,949

Some liabilities are not due and payable in the current period and therefore are not reported in the funds.

Bonds payable and other long-term debt	\$ (87,269,805)	
Accrued interest	<u>(242,702)</u>	<u>(87,512,507)</u>

Net assets of governmental activities \$ 425,520,463

The notes to basic financial statements are an integral part of this statement.

**CITY OF MODESTO**  
**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES**  
**IN FUND BALANCES - GOVERNMENTAL FUNDS**  
**Year ended June 30, 2010**

	<u>General</u>	<u>Capital Facility Fees</u>	<u>Special Gas Tax Street Improvement</u>	<u>Other Governmental</u>	<u>Total Governmental</u>
<b>REVENUES:</b>					
Taxes	\$ 45,855,929		\$ 59,282	\$ 6,690,986	\$ 52,606,197
Licenses and permits	83,039		1,558	54,214	138,811
Intergovernmental	39,050,217	\$ 423,473	3,060,205	19,017,722	61,551,617
Charges for services	13,047,695	1,250,033	1,685,752	7,525,690	23,509,170
Special assessments levied				38,520	38,520
Interest and rent	290,902	329,591	113,044	588,468	1,322,005
Net increase in fair value of investments	54,744	212,505	55,888	76,185	399,322
Fines and forfeits	1,042,067			1,210,947	2,253,014
Miscellaneous	1,528,307	45	92,112	881,933	2,502,397
Total revenues	<u>100,952,900</u>	<u>2,215,647</u>	<u>5,067,841</u>	<u>36,084,665</u>	<u>144,321,053</u>
<b>EXPENDITURES:</b>					
Current:					
General government	10,112,680	537,504		832,056	11,482,240
Community development	5,145,993			13,390,127	18,536,120
Highways and streets		10,942	8,017,950	73,435	8,102,327
Public works	2,613,393			3,511,292	6,124,685
Parks and recreation	9,239,132	5,926		2,893,019	12,138,077
Public safety	72,680,105			2,401,686	75,081,791
Capital outlay		7,300,201	101,462	9,253,579	16,655,242
Debt service:					
Principal retirement				2,045,000	2,045,000
Interest				4,032,612	4,032,612
Other				1,408,771	1,408,771
Total expenditures	<u>99,791,303</u>	<u>7,854,573</u>	<u>8,119,412</u>	<u>39,841,577</u>	<u>155,606,865</u>
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	<u>1,161,597</u>	<u>(5,638,926)</u>	<u>(3,051,571)</u>	<u>(3,756,912)</u>	<u>(11,285,812)</u>
<b>OTHER FINANCING SOURCES (USES):</b>					
Transfers in	3,234,442		1,812,175	7,299,629	12,346,246
Transfers out	<u>(6,174,437)</u>	<u>(911,720)</u>	<u>(1,447,361)</u>	<u>(3,869,419)</u>	<u>(12,402,937)</u>
TOTAL OTHER FINANCING SOURCES (USES)	<u>(2,939,995)</u>	<u>(911,720)</u>	<u>364,814</u>	<u>3,430,210</u>	<u>(56,691)</u>
NET CHANGE IN FUND BALANCES	(1,778,398)	(6,550,646)	(2,686,757)	(326,702)	(11,342,503)
FUND BALANCES, July 1	14,753,758	\$ 39,650,167	\$ 6,877,454	\$ 64,607,156	\$ 125,888,535
PRIOR PERIOD ADJUSTMENT			(674,436)		(674,436)
FUND BALANCES, June 30	<u>\$ 12,975,360</u>	<u>\$ 33,099,521</u>	<u>\$ 3,516,261</u>	<u>\$ 64,280,454</u>	<u>\$ 113,871,596</u>

The notes to basic financial statements are an integral part of this statement.

**CITY OF MODESTO**  
**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND**  
**BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES -GOVERNMENTAL ACTIVITIES**  
**Year Ended June 30, 2010**

Net change in fund balances - total governmental funds \$ (11,342,503)

Amounts reported for governmental activities in the statement of activities are different because:

Governmental funds report capital outlay as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.

Capital outlay	\$ 16,655,242	
Depreciation expense	<u>(19,597,101)</u>	(2,941,859)

In the statement of activities, only the gain or loss on the sales of capital assets is reported, whereas in the governmental funds, the proceeds from such sales increase financial resources. Thus, the change in net assets differs from the change in fund balances by the cost of the assets sold. 201,400

Developer donations of infrastructure assets are not included in the fund statements. Thus, the change in net assets differs from the change in fund balance by the value of these asset donations.

Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.

Change in deferred revenue	\$ 1,252,617	
Change in investment in joint venture	<u>(1,470,927)</u>	(218,310)

The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets.

Principal retirement	2,045,000	
Capitalized interest	<u>(328,442)</u>	1,716,558

Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds.

Change in accrued interest		11,999
----------------------------	--	--------

Internal service funds are used by management to charge the costs of certain activities to individual funds. The net revenue (expense) of internal service funds is reported with governmental activities. (2,685,261)

Change in net assets of governmental activities \$ (15,257,976)

The notes to basic financial statements are an integral part of this statement.

**CITY OF MODESTO**  
**STATEMENT OF NET ASSETS - PROPRIETARY FUNDS**  
**June 30, 2010**

	Enterprise					Internal Service
	Water	Sewer	Bus	Other Enterprise	Total Enterprise	
<b>ASSETS</b>						
Current assets:						
Cash and cash equivalents	\$ 87,922,024	\$ 28,610,976	\$ 6,206,866	\$ 5,662,720	\$ 128,402,586	\$ 51,843,406
Cash and cash equivalents with fiscal agent	4,241,091	4,379,888		603,150	9,224,129	
Receivables:						
Accounts	1,954	37,949	8,951	200,467	249,321	229,011
Interest	197,957	53,866	8,721	8,558	269,102	79,655
Utilities, net	6,649,743	3,827,577		557,890	11,035,210	
Taxes				18	18	
Due from governments			1,977,491	221,708	2,199,199	142,462
Prepaid expenses						189,000
Inventories						482,315
Property held for resale				630,000	630,000	
Total current assets	<u>99,012,769</u>	<u>36,910,256</u>	<u>8,202,029</u>	<u>7,884,511</u>	<u>152,009,565</u>	<u>52,965,849</u>
Noncurrent assets:						
Notes receivable, net						
Restricted assets-cash and cash equivalents	24,661,375	692,066			25,353,441	
Unamortized costs of issuance	1,289,452	754,236			2,043,688	
Deffered outflow of resource	7,518,877				7,518,877	
Land and construction in progress	32,033,873	66,560,563	4,735,511	10,647,503	113,977,450	1,576,124
Other capital assets, net of accumulated depreciation	78,843,723	120,335,987	16,342,395	43,256,981	258,779,086	16,293,664
Total noncurrent assets	<u>144,347,300</u>	<u>188,342,852</u>	<u>21,077,906</u>	<u>53,904,484</u>	<u>407,672,542</u>	<u>17,869,788</u>
Total assets	<u>243,360,069</u>	<u>225,253,108</u>	<u>29,279,935</u>	<u>61,788,995</u>	<u>559,682,107</u>	<u>70,835,637</u>
<b>LIABILITIES</b>						
Current liabilities:						
Accounts payable	\$ 5,406,699	\$ 2,660,259	\$ 807,493	\$ 463,500	\$ 9,337,951	\$ 1,236,836
Accrued salaries and benefits	210,195	202,729	33,317	90,124	536,365	165,010
Interest payable	228,723	382,406	40	43,839	655,008	3,584
Due to other funds				261,782	261,782	
Current portion - compensated absences						4,808,016
Current portion - claims liability						4,880,570
Current portion - capital lease						187,135
Current portion - long-term debt	2,621,785	1,765,000		250,000	4,636,785	33,778
Current portion - developer advances						
Deferred revenues			4,319,518	206,448	4,525,966	
Total current liabilities	<u>8,467,402</u>	<u>5,010,394</u>	<u>5,160,368</u>	<u>1,315,693</u>	<u>19,953,857</u>	<u>11,314,929</u>
Noncurrent liabilities:						
Payable from restricted assets - refundable deposits	1,045,139	692,660			1,737,799	
Compensated absences						6,931,285
Net OPEB obligation						45,527,073
Claims liability						16,390,335
Long-term debt:						
Revenue bonds payable		43,606,475			43,606,475	
Derivative instrument SWAP	7,518,877				7,518,877	
Loan payable	6,522,243				6,522,243	
Notes payable						20,658
Obligations under capital leases						705,974
Certificates of participation	60,861,213	1,379,326		4,725,000	66,965,539	
Developer advances	1,704,036				1,704,036	
Advances from other funds				1,324,704	1,324,704	
Total noncurrent liabilities	<u>77,651,508</u>	<u>45,678,461</u>	<u>5,160,368</u>	<u>6,049,704</u>	<u>129,379,673</u>	<u>69,575,325</u>
Total liabilities	<u>86,118,910</u>	<u>50,688,855</u>	<u>5,160,368</u>	<u>7,365,397</u>	<u>149,333,530</u>	<u>80,890,254</u>
Invested in capital assets, net of related debt	64,488,591	140,145,155	21,077,906	48,929,484	251,025,494	17,130,036
Unrestricted	<u>92,752,568</u>	<u>34,419,098</u>	<u>3,041,661</u>	<u>5,494,114</u>	<u>159,323,083</u>	<u>(27,184,653)</u>
Total net assets	<u>\$ 157,241,159</u>	<u>\$ 174,564,253</u>	<u>\$ 24,119,567</u>	<u>\$ 54,423,598</u>	<u>410,348,577</u>	<u>\$ (10,054,617)</u>
Adjustment to reflect the consolidation of internal service fund activities related to enterprise funds.					<u>(11,661,566)</u>	
Net assets of business-type activities					<u>\$ 398,687,011</u>	

The notes to basic financial statements are an integral part of this statement.

**CITY OF MODESTO**  
**STATEMENT OF REVENUES, EXPENSES, AND CHANGES**  
**IN FUND NET ASSETS - PROPRIETARY FUNDS**  
**Year ended June 30, 2010**

	Enterprise					Internal Service
	Water	Sewer	Bus	Other Enterprise	Total Enterprise	
<b>OPERATING REVENUES:</b>						
Charges for services	\$ 54,208,363	\$ 37,305,248	2,527,562	\$ 11,378,327	\$ 105,419,500	\$ 42,069,111
Sales						4,289,240
Cost of sales						(3,733,953)
Miscellaneous	461,678	5,483	242,252	85,290	794,703	
Total operating revenues	<u>54,670,041</u>	<u>37,310,731</u>	<u>2,769,814</u>	<u>11,463,617</u>	<u>106,214,203</u>	<u>42,624,398</u>
<b>OPERATING EXPENSES:</b>						
Salaries and wages	5,898,699	5,366,829	907,694	2,725,151	14,898,373	4,081,136
Contractual services	2,183,483	2,558,668	9,273,118	3,286,462	17,301,731	1,826,064
Utilities	2,148,457	1,249,450	89,216	499,216	3,986,339	437,737
Maintenance and supplies	6,963,690	2,813,088	2,025,828	1,867,849	13,670,455	3,938,198
Water purchases	14,074,872				14,074,872	
Insurance	267,203	584,612	51,764	280,412	1,183,991	15,142,530
Claims expense						6,541,335
Employee benefits	2,824,135	2,699,697	448,655	1,116,785	7,089,272	9,532,783
Administration services	1,640,807	1,411,022	653,726	1,505,961	5,211,516	1,728,417
Allocated indirect administrative costs	1,426,375	1,319,021	105,391	220,244	3,071,031	308,280
Other	496,318	92,905	94,151	154,555	837,929	54,946
Depreciation	4,262,261	7,205,977	1,841,405	3,180,472	16,490,115	3,408,724
Total operating expenses	<u>42,186,300</u>	<u>25,301,269</u>	<u>15,490,948</u>	<u>14,837,107</u>	<u>97,815,624</u>	<u>47,000,150</u>
OPERATING INCOME (LOSS)	<u>12,483,741</u>	<u>12,009,462</u>	<u>(12,721,134)</u>	<u>(3,373,490)</u>	<u>8,398,579</u>	<u>(4,375,752)</u>
<b>NONOPERATING REVENUES (EXPENSES)</b>						
Operating grants		50,000	13,658,181	(1,669)	13,706,512	142,462
Gain (Loss) on disposition of capital assets	(19,875)	(711,469)	(161,557)		(892,901)	(396,902)
Tax revenue				265,587	265,587	
Tax expense	(92,291)	(101,056)		(290,386)	(483,733)	
Interest income	849,474	512,503	31,128	55,384	1,448,489	674,961
Net increase in fair value of investments	638,055	234,583	31,056	27,208	930,902	286,341
Rental income	39,300	60,706		676,557	776,563	
Settlements and recoveries		447,102			447,102	
Interest expense	(1,038,823)	(1,810,816)			(2,849,639)	(8,595)
Trustee fees	(1,500)			(2,800)	(4,300)	
Amortization of costs of issuance	(88,980)	68,883			(20,097)	
Total nonoperating revenues (expenses)	<u>285,360</u>	<u>(1,249,564)</u>	<u>13,558,808</u>	<u>729,881</u>	<u>13,324,485</u>	<u>698,267</u>
INCOME (LOSS) BEFORE CAPITAL CONTRIBUTIONS AND TRANSFERS	<u>12,769,101</u>	<u>10,759,898</u>	<u>837,674</u>	<u>(2,643,609)</u>	<u>21,723,064</u>	<u>(3,677,485)</u>
Capital contributions	652,693	867,697	664,299	713,800	2,898,489	6,566
Transfers in	264,000		204,341	1,175,281	1,643,622	1,414,206
Transfers out	(1,197,325)	(403,984)	(8,400)	(436,216)	(2,045,925)	(955,212)
Special item	(671,141)	(655,168)			(1,326,309)	
CHANGE IN NET ASSETS	<u>11,817,328</u>	<u>10,568,443</u>	<u>1,697,914</u>	<u>(1,190,744)</u>	<u>22,892,941</u>	<u>(3,211,925)</u>
NET ASSETS, July 1 (as restated)	<u>155,507,731</u>	<u>165,658,760</u>	<u>22,421,653</u>	<u>55,619,342</u>		<u>(6,809,150)</u>
PRIOR YEAR ADJUSTMENTS	<u>(10,083,900)</u>	<u>(1,662,950)</u>		<u>(5,000)</u>		<u>(33,542)</u>
NET ASSETS, June 30	<u>\$ 157,241,159</u>	<u>\$ 174,564,253</u>	<u>\$ 24,119,567</u>	<u>\$ 54,423,598</u>		<u>\$ (10,054,617)</u>
Adjustment to reflect the consolidation of internal service fund					<u>(526,663)</u>	
Change in net assets of business-type activities					<u>\$ 22,366,278</u>	

The notes to basic financial statements are an integral part of this statement.

**CITY OF MODESTO**  
**STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS**  
Year ended June 30, 2010

	Enterprise					Internal Service
	Water	Sewer	Bus	Other Enterprise	Total Enterprise	
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>						
Receipts from customers and users	\$ 54,352,528	\$ 37,409,151	\$ 2,804,211	\$ 12,163,243	\$ 106,729,133	\$ 1,937,046
Receipts from interfund services provided	339,138	41,608		1,839	382,585	40,435,055
Payments to suppliers	(24,025,394)	(5,888,426)	(11,490,536)	2,665,883	(38,738,473)	(21,568,965)
Payment of insurance claims						(6,695,983)
Payments to employees	(8,660,684)	(8,023,389)	(1,352,958)	(3,836,359)	(21,873,390)	(9,125,882)
Payments for interfund services used	(5,542,397)	(4,961,767)	(851,892)	(10,507,459)	(21,863,515)	(2,659,818)
Net cash provided (used) by operating activities	<u>16,463,191</u>	<u>18,577,177</u>	<u>(10,891,175)</u>	<u>487,147</u>	<u>24,636,340</u>	<u>2,321,453</u>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>						
Operating grants received		50,000	16,144,448	(1,669)	16,192,779	146,046
Taxes received				265,587	265,587	
Settlements and recoveries		447,102			447,102	
Transfers in	264,000		204,341	1,175,281	1,643,622	1,414,206
Transfers out	(1,197,325)	(403,984)	(8,400)	(436,216)	(2,045,925)	(955,212)
Due from other funds						101,576
Net cash provided (used) by noncapital financing activities	<u>(933,325)</u>	<u>93,118</u>	<u>16,340,389</u>	<u>1,002,983</u>	<u>16,503,165</u>	<u>706,616</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>						
Acquisition and construction of capital assets	(10,471,123)	(36,202,415)	(3,606,838)	(916,566)	(51,196,942)	(3,123,895)
Proceeds of sale of capital assets						(396,902)
Proceeds of debt issues						
Costs of issuance paid	56,308	46,220			102,528	
Principal repayments	5,122,883	(1,621,312)		(235,000)	3,266,571	790,577
Interest paid	(1,129,534)	(1,750,483)		992	(2,879,025)	(8,595)
Trustee fees	(1,500)			(2,800)	(4,300)	
Capital grants received			664,299	61,805	726,104	
Net cash used by capital and related financing activities	<u>(6,422,966)</u>	<u>(39,527,990)</u>	<u>(2,942,539)</u>	<u>(1,091,569)</u>	<u>(49,985,064)</u>	<u>(2,738,815)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>						
Interest received	1,050,237	637,858	37,068	58,997	1,784,160	734,337
Net increase in the fair value of investments	638,055	234,583	31,056	27,208	930,902	286,341
Net cash provided by investing activities	<u>1,688,292</u>	<u>872,441</u>	<u>68,124</u>	<u>86,205</u>	<u>2,715,062</u>	<u>1,020,678</u>
Net increase (decrease) in cash and cash equivalents	10,795,192	(19,985,254)	2,574,799	484,766	(6,130,497)	1,309,932
CASH AND CASH EQUIVALENTS, JULY 1	116,113,198	55,331,134	3,632,067	5,786,104	180,862,503	50,567,016
PRIOR PERIOD ADJUSTMENT	<u>(10,083,900)</u>	<u>(1,662,950)</u>		<u>(5,000)</u>	<u>(11,751,850)</u>	<u>(33,542)</u>
CASH AND CASH EQUIVALENTS, JUNE 30	<u>\$ 116,824,490</u>	<u>\$ 33,682,930</u>	<u>\$ 6,206,866</u>	<u>\$ 6,265,870</u>	<u>\$ 162,980,156</u>	<u>\$ 51,843,406</u>
<b>RECONCILIATION TO STATEMENT OF NET ASSETS:</b>						
Cash and cash equivalents	\$ 87,922,024	\$ 28,610,976	\$ 6,206,866	\$ 5,662,720	\$ 128,402,586	\$ 51,843,406
Cash and cash equivalents with fiscal agent	4,241,091	4,379,888		603,150	9,224,129	
Restricted assets-cash and cash equivalents	<u>24,661,375</u>	<u>692,066</u>			<u>25,353,441</u>	
TOTAL CASH AND CASH EQUIVALENTS	<u>\$ 116,824,490</u>	<u>\$ 33,682,930</u>	<u>\$ 6,206,866</u>	<u>\$ 6,265,870</u>	<u>\$ 162,980,156</u>	<u>\$ 51,843,406</u>

(continued)

The notes to basic financial statements are an integral part of this statement.

**CITY OF MODESTO**  
**STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS (Continued)**  
**Year ended June 30, 2010**

	Enterprise					Internal Service
	Water	Sewer	Bus	Other Enterprise	Total Enterprise	
<b>RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:</b>						
Operating income (loss)	\$ 12,483,741	\$ 12,009,462	\$ (12,721,134)	\$ (3,373,490)	\$ 8,398,579	\$ (4,375,752)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:						
Depreciation	4,262,261	7,205,977	1,841,405	3,180,472	16,490,115	3,408,723
Rental income	39,300	60,706		676,557	776,563	
Taxes paid	(92,291)	(101,056)		(290,386)	(483,733)	
Special item	(671,141)	(655,168)			(1,326,309)	
Change in assets and liabilities:						
(Increase) in accounts receivable	(1,954)	(20,553)	57,796	36,731	72,020	(109,834)
(Increase) in utilities receivable	(118,590)	46,420		(12,840)	(85,010)	
(Increase) in taxes receivable	6,151				6,151	
Decrease in due from governments			(23,399)		(23,399)	(142,462)
(Increase) decrease in prepaid expenses						(189,000)
(Increase) in inventories						429,747
(Decrease) in accounts payable and accrued expenses	401,212	(52,629)	(49,234)	145,233	444,582	(1,033,357)
Increase in accrued salaries and benefits	62,150	43,137	3,391	5,577	114,255	33,543
Increase in compensated absences and OPEB						4,454,493
(Decrease) in claims liability						(154,648)
Increase in due to other governments		(12,574)		(22,398)	(34,972)	
Increase in due to other funds	(4,366)			140,674	136,308	
Increase in deferred revenues				1,017	1,017	
Increase (decrease) in refundable deposits	96,718	53,455			150,173	
Total adjustments	<u>3,979,450</u>	<u>6,567,715</u>	<u>1,829,959</u>	<u>3,860,637</u>	<u>16,237,761</u>	<u>6,697,205</u>
Net cash provided (used) by operating activities	<u>\$ 16,463,191</u>	<u>\$ 18,577,177</u>	<u>(10,891,175)</u>	<u>\$ 487,147</u>	<u>\$ 24,636,340</u>	<u>\$ 2,321,453</u>
<b>NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES:</b>						
Capital assets transferred in	\$ 652,693	\$ 867,697				\$ 6,566
Developer infrastructure contributions						
Amortization of bonds discount and deferred amount on refunding						

The notes to basic financial statements are an integral part of this statement.

**CITY OF MODESTO**  
**STATEMENT OF FIDUCIARY NET ASSETS -AGENCY FUNDS**  
**June 30, 2010**

	<u>Agency Funds</u>
<u>ASSETS</u>	
Cash and cash equivalents	\$ 8,855,649
Cash and cash equivalents held with fiscal agent	<u>3,924,436</u>
	<u>\$ 12,780,085</u>
 <u>LIABILITIES</u>	
Due to special district bondholders	\$ 8,046,312
Deposits held as agent for others	<u>4,733,773</u>
	<u>\$ 12,780,085</u>

The notes to basic financial statements are an integral part of this statement.

**CITY OF MODESTO  
NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2010**

**I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**A. THE FINANCIAL REPORTING ENTITY**

The City of Modesto (the City) was incorporated in 1884 and operates under a Council-Manager form of government as authorized by its charter adopted in 1951. The City Council consists of seven elected members. The following services are provided by the City to its citizens: public safety (police and fire), highways and streets, drinking water, wastewater collection and treatment, storm drainage, public transit, recreation and social services, public improvements, community development, planning and zoning, and general administrative services.

These financial statements present the financial status of the City and its component units. The component units discussed in the following paragraphs are included in the City's reporting entity because the City is financially accountable for their operations.

1. The Redevelopment Agency of the City of Modesto (the Agency) was established by the City as a separate legal entity in accordance with state law. The purpose of the Agency is to encourage new investment and reinvestment within legally designated redevelopment areas in partnership with property owners.
2. The Modesto Public Financing Authority was established as a separate legal entity whose sole purpose is to provide financing for various City capital projects.
1. The Modesto Municipal Sewer District is a separate legal entity formed under the Municipal Sewer and Water Facilities Law of 1911. The purpose of the District is to provide financing for needed sewerage facilities in the Modesto urban area.
4. The City of Modesto has established several Community Facilities Districts to provide funding and reimbursement mechanisms for public facilities and services required by each District Specific Plan. These Districts are the vehicles used to ensure that all landowners in the Districts contribute to the cost of public improvements. There are currently ten active Districts, which are combined for presentation in these financial statements. Individual component unit financial statements are prepared for each District.

Although these component units are legally separate from the City, they are reported on a blended basis as part of the primary government because their boards consist of all seven members of the City Council. Component unit financial statements may be obtained from the City's Finance Department.

The joint ventures and jointly governed organization described in Note III - E are not considered part of the reporting entity because the City is not financially accountable for their operations.

**B. GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS**

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the non-fiduciary activities of the primary government and its component units. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segments are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions

restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

### C. BASIS OF PRESENTATION, BASIS OF ACCOUNTING, AND MEASUREMENT FOCUS

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund statements. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. Agency funds have no measurement focus. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the City considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, principal and interest expenditures are recorded as fund liabilities when due or when amounts have been accumulated in the debt service funds for payments to be made early in the following year.

Substantially all property taxes, taxpayer-assessed taxes (such as sales and use, utility users, business license, transient occupancy, franchise fees, and gas taxes), interest, special assessments levied, state and federal grants, and charges for current services are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. Revenues from licenses, permits, and fines and forfeits are considered to be measurable and available only when cash is received by the City.

The City reports the following major governmental funds:

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

The Capital Facility Fees Fund accounts for special fees collected on new building permits to be used for construction of growth related projects, including police department expansion, fire department expansion, expressway loop, street lights, parks, new traffic signals, city hall expansion, wastewater treatment, streets, public transportation, and air quality improvements.

The Special Gas Tax Street Improvement Fund accounts for funds received from the State under the provisions of the Streets and Highway Code for the acquisition of real property, construction, maintenance or improvements of streets or highways. The fund also tracks the expenditures for the purposes of the allowable expenses for these state revenues.

The City reports the following major proprietary funds:

The Water Fund accounts for all revenues collected by the City for the purpose of financing the construction, operation, and maintenance of the City water distribution system. Revenues are derived from water service charges and various installation fees.

The Sewer Fund accounts for revenues collected by the City for the purpose of financing the construction, operation, and maintenance of the City sewer system. Revenues include, but are not limited to, sewer service charges and sewer lateral charges.

The Bus Fund accounts for operations, maintenance, and capital expenditures of the City's mass transportation service. This system operates pursuant to the terms of a Federal grant agreement. Buses are operated by a private contractor under the terms of a supervisory agreement with the City. A separate contract provides Dial-a-Ride service for the elderly and handicapped.

Additionally, the City reports the following fund types:

Internal service funds account for fleet management, central services, technology and information services, insurance, employee benefits management, and building services provided to other departments or agencies of the City on a cost-reimbursement basis. Agency funds account for cash and investments held by the City as agent for various assessment districts, governmental entities and non-public organizations. Agency funds cannot be major funds.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in both the government-wide – business-type activities and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The City has elected not to follow subsequent private-sector guidance.

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are exchange or exchange-like transactions between functions of the government. Eliminations of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Amounts reported as program revenues include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the enterprise and internal service funds are charges to customers for sales and services. The Water and Sewer Funds also recognize as operating revenue the portion of tap fees intended to recover the cost of connecting new customers to the systems. Operating expenses for enterprise and internal service funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the City's policy to use restricted resources first, then unrestricted resources as they are needed.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

#### D. ASSETS, LIABILITIES, AND NET ASSETS OR EQUITY

##### 1. Cash and Cash Equivalents

Cash and investments (including restricted assets) held in the City's investment pool are reported as cash and cash equivalents on the statement of net assets and balance sheet because funds can spend cash at any time without prior notice or penalty. All investments with fiscal agents are also considered cash equivalents because they are highly liquid and have maturities of 3 months or less at the time of purchase. Investments are stated at fair value. Valuations are obtained by using quotations obtained from independent published sources.

## 2. Restricted Assets - Cash and Cash Equivalents

Refundable deposits of the General Fund and the Community Facilities Districts Capital Projects Fund are classified as restricted assets – cash and cash equivalents on the governmental funds balance sheet because their use is restricted for repayment of those refundable deposits. Refundable deposits in the Water and Sewer funds are also reported as restricted assets on the proprietary funds statement of net assets. In addition, certain proceeds of Water certificates of participation and Sewer revenue bonds are considered restricted assets because their use is limited by applicable debt covenants. These proceeds are reported as part of “restricted assets – cash and cash equivalents” on the proprietary funds statement of net assets.

## 3. Receivables and Payables

Balances representing lending/borrowing transactions between funds outstanding at the end of the fiscal year are reported as either "due from/due to other funds" (amounts due within one year), or "advances to/from other funds" (non-current portions of interfund lending/borrowing transactions). Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as “internal balances.” Advances to other funds are offset by a fund balance reserve in applicable governmental funds to indicate they are not available for appropriation and are not expendable available financial resources.

All property taxes are collected and allocated by the County of Stanislaus to the various taxing entities. Property taxes are determined annually as of March 1 and attach as an enforceable lien on real property as of January 1. Taxes are due November 1 and February 1 and are delinquent if not paid by December 10 and April 10, respectively. The City participates in the County "Teeter Plan" method of property tax distribution. Under the Teeter Plan, the County remits property taxes to the City based on assessments, not on collections, according to the following schedule: 55 percent in December, 40 percent in April, and 5 percent at the end of the fiscal year. Property tax is recognized when it is available and measurable. The City considers property tax as available if it is received within 60 days after year-end.

Revenue from taxpayer-assessed taxes (sales and use, business license, transient occupancy, utility users, gas, and franchise fees) are accrued in the governmental funds when they are both measurable and available. The City considers these revenues available if they are received during the period when settlement of prior fiscal year accounts payable occurs. Historically, the majority of these taxes are received within 60 days of the fiscal year end; therefore, revenue from taxpayer-assessed taxes is accrued if it is received by August 31.

Grant and entitlement revenues are recorded as receivables in the funds when they are susceptible to accrual (i.e., when all eligibility requirements have been met). The corresponding governmental fund revenues are recorded when they become available, with the differences recorded as deferred revenue. The corresponding proprietary fund revenues are recorded as non-operating revenues when the receivables are recorded. Some grant and entitlement revenues are not susceptible to accrual, in which case the corresponding revenues are recorded when received. The total amount due from governments for grants, entitlements, and shared receivables and revenues at June 30, 2010 is \$24,994,619.

Utility service accounts receivable are reported net of \$1,458,987 allowance for doubtful collections and include unbilled receivables using actual amounts billed in July for June services for governmental funds. Accounts receivable are reported net of \$642,491 allowance for doubtful collections, and are based on miscellaneous receivables from the City's invoice system as well as other receivables accrued at year end.

## 4. Inventories

Inventories of material and supplies held by proprietary funds are stated at average cost.

## 5. Capital Assets

Capital assets which include property, plant and equipment, intangible assets and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items) are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets are defined by the government as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair value at the date of donation.

In the case of the initial capitalization of infrastructure assets reported by governmental activities, the City chose to include them regardless of their acquisition date or amount. Historical values were estimated.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets of business-type activities is included as part of the capitalized value of the assets constructed. The amount of interest capitalized is determined by offsetting interest expense incurred from the date of borrowing until completion of the project, against interest earned on invested proceeds over the same period. During the fiscal year ended June 30, 2010, \$672,978 net interest expense on tax-exempt debt of the City's Sewer Fund, and \$1,271,398 of the Water fund, was capitalized.

Depreciation is recorded using the straight line method over the estimated useful lives of the assets, which are 75 years for pipelines, 30 years for buildings, 20 years for improvements, 12 years for buses, 10 years for furnishings and equipment, 2 to 10 years for vehicles, 5 to 15 years for intangible assets, 30 to 50 years for streets, 20 years for signalization, and 50 years for bridges. Operating expenses include depreciation on all depreciable capital assets.

Capital leases are recorded as an asset and an obligation at an amount equal to the present value at the beginning of the lease term of minimum lease payments during the lease term.

## 6. Compensated Absences

All earned vacation, holiday, and compensating time, and a portion of accumulated sick leave payable upon termination or retirement, are accrued in the Employee Benefits Management Internal Service Fund as compensated absences. Estimated sick leave termination payments have been calculated using the Governmental Accounting Standards Board Statement 16 vesting method. Under this method, a liability is accrued for a portion of the sick leave balances of all employees who are currently eligible, or are assumed to become eligible in the future, to receive a payment for sick leave upon termination. As of June 30, 2010, the total estimated liability for all compensated absences, including sick leave, is \$11,739,301.

## 7. Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

# E. OTHER SIGNIFICANT ACCOUNTING POLICIES

## 1. Employee Benefits

The City established the Employee Benefits Management Internal Service Fund to account for all compensated absences and non-insurance benefits. Insurance benefits for current employees are paid from the Insurance Internal Service Fund. The Employee Benefits Management Fund is reimbursed based on actual benefits paid and leave taken, through payroll charges to the City's operating funds. Leave earned but not taken is being funded over time by budgeted charges to the operating funds.

## 2. Interfund Transactions

The City transfers resources among funds in the course of normal operations. Interfund service provided and used, such as equipment pool rental, are accounted for as revenues and expenditures or expenses. Transactions to reimburse a fund for expenditures/expenses initially made from it that are applicable to another fund are recorded as expenditures/expenses in the correct fund and as reductions of expenditures/expenses in the original fund. All other interfund transactions are reported as transfers.

## 2. Proposition 1A Borrowing by the State of California

Under the provisions of Proposition 1A and as part of the 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. After repayment of this initial borrowing, the California legislature may consider only on additional borrowing within a ten-year period. The amount of this borrowing pertaining to the City of Modesto was \$2,749,159.

Authorized with the 2009-10 State budget package, 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 with 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.

## F. NEW ACCOUNTING STANDARDS

The Governmental Accounting Standards Board (GASB) issued Statement #51, "Accounting and Financial Reporting for Intangible Assets." This statement establishes accounting and financial reporting requirements for intangible assets including easements, water rights, and computer software. The City has implemented this requirement as part of the City's financial statement for June 30, 2010.

The GASB also issued Statement #53, "Accounting and Financial Reporting for Derivative Instruments." This statement establishes accounting and financial reporting requirements for derivative instruments entered into by state and local governments. The City has implemented this requirement as part of the City's financial statement for June 30, 2010.

## II. DETAILED NOTES

### A. CASH AND INVESTMENTS

The City maintains a cash and investment pool that is used by all funds. Each fund's portion of the City's cash and investment pool is displayed on the balance sheet and proprietary and fiduciary fund statements of net assets as "cash and cash equivalents." Each fund is allocated interest on average monthly cash balances held by the funds throughout the year. A majority of the interest from the Fleet Management Internal Service Fund is credited to the General Fund in accordance with the City's policy. Certain deposits held in trust are displayed on the governmental funds balance sheet and the proprietary funds statement of net assets as "restricted assets - cash and cash equivalents." The City also maintains "cash and cash equivalents with fiscal agent" which represent monies held by fiscal agents for payment of various City debt and capital projects costs.

## Investments Authorized by the California Government Code and the City's Investment Policy

The City's investment policy and the California Government Code allow the City to invest in the following types of instruments, and the table also identifies certain provisions of the California Government Code, or the City's investment policy where it is more restrictive:

<u>Authorized Investment Type</u>	<u>Maximum Maturity</u>	<u>Minimum Credit Quality</u>	<u>Maximum Percentage Of Portfolio</u>	<u>Maximum Investment in One Issuer</u>
City of Modesto Bonds	5 years	N/A	None	None
U.S. Treasury Obligations	5 years	N/A	None	None
State of California Securities	5 years	AAA	None	None
California Municipal Securities	5 years	AAA	None	None
Federal Agency Securities	5 years	N/A	None	None
Bankers' Acceptances	180 days	N/A	40%	10% or \$1 million
Commercial Paper	270 days	Top rating category	25%	10%
Certificates of Deposit	1 year	N/A	20% of surplus	None
Negotiable Certificates of Deposit	5 years	AA	30%	None
Repurchase Agreements	90 days	Top rating category	None	None
Reverse Repurchase Agreements	92 days	N/A	20%	None
Medium Term Corporate Notes	5 years	AA -	30%	None
Money Market Funds	N/A	Top rating category	None	None
California Local Agency Investment Fund	N/A	N/A	\$40 million per account	None
Mortgage and Asset-Backed Securities	5 years	AA	20% of surplus	None
California Asset Management Program	N/A	N/A	None	None

The City is a voluntary participant in the California Asset Management Program (CAMP). CAMP is an investment pool offered by the California Asset Management Trust (the Trust). The Trust is a joint powers authority and public agency created by the Declaration of Trust and established under the provisions of the California Joint Exercise of Powers Act (California Government Code Sections 6500 et seq., or the "Act") for the purpose of exercising the common power of its participants to invest certain proceeds of debt issues and surplus funds. The Pool's investments are limited to investments permitted by subdivisions (a) to (n), inclusive, of Section 53601 of the California Government Code. At June 30, 2010 the fair value approximated the City's Cost. At June 30, 2010, these investments have an average maturity of 402 days. The City reports its investments in CAMP at the fair value amounts provided by CAMP, which is the same as the value of the pool share.

## Investments Authorized by Debt Agreements

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

## Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. The following table summarizes the City's interest rate risk, based on maturity dates of various investments:

Investment Type	Remaining Time to Maturity				
	Total	Less Than 1 Year	1 – 2 Years	2 – 3 Years	Over 5 Years
U.S. Treasury Notes	\$37,395,233	0	\$37,395,233	0	
Federal agency securities					
Bonds	22,958,108	6,061,017	7,778,608	9,118,483	
Notes	117,159,775	37,996,454	41,214,278	37,949,043	
Discount Notes	7,708,055	7,708,055			
U.S. Treasury Bills	2,624,409	2,624,409			
CAMP	106,264,506	106,264,506			
Cash in banks	193,162	193,162			
Held by trustee:					
Money market funds	5,648,815	5,648,815			
Federal agency discount notes					
Federal agency securities notes	5,379,466	5,379,466			
CAMP	18,510,304	18,510,304			
Total	\$323,841,833	\$190,386,188	\$86,388,119	\$47,067,526	

Maturity dates for callable notes are based on call dates.

### Disclosures Related to 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 measured by the assignment of a rating by a nationally recognized statistical rating organization. Presented below is the rating as of June 30, 2010 for each investment type:

Investment Type	Total	Exempt from Disclosure	AAA and A-1+	Not Rated
U.S. Treasury Notes	\$37,395,233	\$37,395,233		
Federal agency securities	147,825,938		147,825,938	
U.S. Treasury Bills	2,624,409		2,624,409	
CAMP	106,264,506		106,264,506	
Held by trustee:				
Money market funds	5,648,815		5,648,815	
Federal agency discount notes				
Federal agency securities notes	5,379,466		5,379,466	
CAMP	18,510,304		18,510,304	
Guaranteed investment contracts				
Total	\$323,648,671	\$37,395,233	\$286,523,438	

On May 27, 1993 the City entered into a 20 year Repurchase Agreement with Lehman Government Securities Inc. to fulfill its "reserve requirement" for the 1993 Community Center Refinancing Refunding Certificates of Participation. The minimum credit rating allowable according the Repurchase Agreement was a rating of "A-" by Standard and Poors. On September 16, 2008, Standard and Poors downgraded Lehman Brothers Holdings Inc. to a "D" credit rating. The downgrade triggered a required "transaction reduction," and on October 1, 2008 the City contacted Lehman Government Securities Inc. and Lehman Brothers Holdings Inc. to request payment of the purchase price of the Repurchase Agreement plus additional amounts required under the Agreement. The City received payment of the Repurchase Agreement in April 2009. The reserve fund is now invested in Federal Agencies.

### Concentration of Credit Risk

The City's investment policy contains no limitations on the amount that can be invested in any one issuer beyond that stipulated by the California Government Code. Investments in any one issuer, other than U. S. Treasury securities, mutual funds, and external investment pools that represent 5% or more of total entity-wide investments are as follows at June 30, 2010:

<u>Issuer</u>	<u>Investment Type</u>	<u>Reported Amount</u>	<u>Percent of Portfolio</u>
Freddie Mac (FHLMC)	Federal agency securities	\$62,095,533	19.2%
Federal Home Loan Bank	Federal agency securities	38,686,163	11.9%
Fannie Mae (FNMA)	Federal agency securities	50,439,544	15.6%

Investments in any one issuer, other than U. S. Treasury securities, mutual funds, and external investment pools, that represent 5% or more of enterprise funds were for the Sewer Enterprise Fund as follows at June 30, 2009:

<u>Issuer</u>	<u>Investment Type</u>	<u>Reported Amount</u>
Federal Home Loan Bank	Federal agency securities	\$3,395,302

### Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the City will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. Under California Government Code Section 53651, depending on specific types of eligible securities, a bank must deposit eligible securities posted as collateral with its Agent having a fair value of 105% to 150% of the City's cash on deposit. All of the City's deposits are either insured by the Federal Depository Insurance Corporation (FDIC) or collateralized with pledged securities held in the trust department of the financial institution in the City's name.

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

## B. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2010 was as follows:

			<u>Beginning Balance</u>	<u>Additions</u>	<u>Deletions</u>	<u>Ending Balance</u>
Governmental activities:						
Capital assets, not being depreciated:						
Land			32,082,218	809,126	200,853	32,690,491
Construction in Progress			29,283,421	2,470,212	16,711,925	15,041,708
Total capital assets, not being depreciated:			\$ 61,365,639	\$ 3,279,338	\$ 16,912,778	\$ 47,732,199
Capital assets being depreciated:						
Building			31,714,964	254,673	-	31,969,637
Improvements other than buildings			49,450,895	16,942,092	85,841	66,307,146
Furnishings & equipment			21,227,231	1,325,487	7,169,939	15,382,779
Intangible Assets			-	2,416,213	-	2,416,213
Equipment pool			28,371,714	1,993,014	2,045,431	28,319,297
Infrastructure						
	Streets		473,038,088	14,295,449	-	487,333,537
	Signals		16,587,096	297,704	-	16,884,800
	Bridges		25,972,368	234,839	-	26,207,207
Total capital assets, being depreciated:			\$ 646,362,356	\$ 37,759,471	\$ 9,301,211	\$ 674,820,616
Less accumulated depreciation for:						
			<u>Beginning Balance</u>	<u>Additions</u>	<u>Deletions</u>	<u>Ending Balance</u>
Buildings			(14,050,138)	(1,288,515)	-	(15,338,653)
Improvements			(25,294,793)	(2,913,037)	15,932	(28,191,898)
Furnishings & equipment			(12,040,691)	(1,282,675)	3,125,060	(10,198,306)
Intangible Assets			-	(433,885)		(433,885)
Equipment pool			(15,173,235)	(2,798,402)	1,525,559	(16,446,078)
Infrastructure						
	Streets		(224,809,452)	(12,149,299)	-	(236,958,751)
	Signals		(11,316,607)	(1,702,987)	-	(13,019,594)
	Bridges		(2,945,519)	(543,423)	-	(3,488,942)
Total accumulated depreciation			\$ (305,630,435)	\$ (23,112,223)	\$ 4,666,551	\$ (324,076,107)
Total capital assets being depreciated, net			\$ 340,731,921	\$ 14,647,248	\$ 4,634,660	\$ 350,744,509
Governmental activities capital assets, net			\$ 402,097,560	\$ 17,926,586	\$ 21,547,438	\$ 398,476,708

	Beginning Balance	Additions	Deletions	Ending Balance
Business-type activities:				
Capital Assets not being depreciated:				
Land	29,806,353	261,876		30,068,229
Construction in Progress	66,783,259	44,690,090	27,564,128	83,909,221
Total capital assets, not being depreciated:	\$ 96,589,612	\$ 44,951,966	\$ 27,564,128	\$ 113,977,450
Capital Assets being depreciated:				
Building	83,160,909	-	-	83,160,909
Improvements other than buildings	163,514,656	28,914,307	-	192,428,963
Furnishings & equipment	6,342,945	4,255,754	672,687	9,926,012
Intangible Asset	-	149,098	-	149,098
Buses and Fareboxes	18,496,423	-	3,161,910	15,334,513
Pipelines	146,472,520	1,251,469	-	147,723,989
Total capital assets, being depreciated:	\$ 417,987,453	\$ 34,570,628	\$ 3,834,597	\$ 448,723,484
Less accumulated depreciation for:				
Buildings	(42,184,591)	(2,520,074)		(44,704,665)
Improvements	(93,768,321)	(9,098,415)		(102,866,736)
Furnishings & equipment	(3,646,267)	(677,595)	542,024	(3,781,838)
Intangible Asset		(17,552)		(17,552)
Buses and Fareboxes	(11,377,666)	(1,320,917)	2,885,777	(9,812,806)
Pipelines	(26,891,800)	(1,869,001)		(28,760,801)
Total accumulated depreciation	\$ (177,868,645)	\$ (15,503,554)	\$ 3,427,801	\$ (189,944,398)
Total capital assets being depreciated, net	\$ 240,118,808	\$ 19,067,074	\$ 7,262,398	\$ 258,779,086
Business-type activities capital assets, net	\$ 336,708,420	\$ 64,019,040	\$ 34,826,526	\$ 372,756,536

Depreciation expense was charged to functions/programs as follows:

Governmental activities:	
General government	446,208
Community development	142,054
Highways and streets, including depreciation of general infrastructure assets	14,717,700
Public works	892,300
Parks and recreation	933,484
Public safety	2,683,801
Capital assets held by the government's internal service funds are charged to the various functions based on their usage of the assets	3,296,676
Total depreciation expense – governmental activities	<u>\$23,112,223</u>
Business-type activities:	
Parking	396,668
Water	4,262,262
Sewer	7,205,977
Storm Drain	619,269
Compost	281,908
Airport	810,924
Bus	1,841,402
Golf	310,227
Community center	761,478
Total depreciation expense – business-type activities	<u>\$16,490,115</u>

**C. LONG-TERM DEBT**

Loans Payable

Governmental activities:

No-interest loan payable to the Stanislaus County Economic Development Bank loan program, to pay master plan costs incurred by the City's Redevelopment Agency for the Kansas Avenue Business Park Project; no obligation to begin repayments until project is complete and revenue stream begins; final payment due in 2016 if not repaid sooner. \$405,000

No-interest loan payable to the Stanislaus County Economic Development Bank loan program, to pay costs incurred by the City for the Kiernan Business Park East Project; loan intended to be repaid within five years of project completion, provided funds are available from revenue stream; project completion estimated to be March 1, 2009; authorized loan amount up to \$500,000, with a current balance of \$498,362; outstanding amount will increase as more eligible costs are incurred and more loan proceeds are borrowed. 498,362

Total principal balances – governmental activities \$903,362

Business-type activities:

Water Enterprise Fund:

Loan payable to the State of California Department of Water Resources, assumed from Del Este Water Company at acquisition, for purposes of upgrading the water delivery system; interest at 3.2%; semi-annual installments on April 1 and October 1 of \$132,360, including interest, through October 1, 2015. \$1,326,174

Loan payable to Modesto Irrigation District for the purposes of certain repairs and maintenance for the Exterior Insulation Finish System ("EIFS") and gutter systems, and certain low sloped roofing replacement, collectively referred to for convenience as "Project", and are necessary for the Modesto Regional Water Treatment Plant facilities. Payments are to be made in five annual installments due no later than July 31, 2014. \$6,493,459

Annual debt service requirements to maturity for loans payable are as follows:

<u>Year Ending June 30,</u>	<u>Governmental Activities</u>		<u>Business-type Activities</u>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2011			1,297,390	40,377
2012			1,586,566	33,256
2013			1,594,099	25,723
2014			1,601,698	18,124
2015			1,609,596	10,226
2016	<u>\$903,362</u>		<u>130,284</u>	<u>2,076</u>
Total	<u>\$903,362</u>	<u>\$0</u>	<u>\$7,819,633</u>	<u>\$129,782</u>

## Certificates of Participation

### Governmental activities:

1993 Refunding Certificates of Participation issued to refund earlier certificates for the Modesto Centre Plaza Community Center capital project; serial certificates with annual maturities on November 1, in amounts from \$935,000 to \$1,040,000; interest rates from 5.5% - 5.6%; term certificates at 5.6% in the amount of \$4,740,000 maturing November 1, 2014, and in the amount of \$12,235,000 at 5.0% maturing November 1, 2023, with annual payments of \$1,090,000 to \$1,610,000 beginning in 2011. The certificates are repayable from any source of available funds of the City. \$ 18,015,000

### Business-type activities:

#### Golf Enterprise Fund:

1993 Refunding Certificates of Participation issued to refund earlier certificates for the Creekside Golf Course capital project; serial certificates with annual maturities on November 1, in amounts from \$225,000 to \$235,000; interest rate of 5.5%; term certificates at 5.6% in the amount of \$1,390,000 due November 1, 2014, and in the amount of \$3,585,000 at 5.0% due November 1, 2023, with annual payments ranging from \$250,000 to \$480,000 beginning in 2010. The certificates are repayable from any source of available funds of the City. However, the City has elected to repay the certificates from revenues of the Golf enterprise fund. \$ 4,975,000

#### Water Enterprise Fund:

1997 Refunding Certificates of Participation issued to refund earlier certificates for various Water Enterprise Fund capital projects; serial certificates with annual maturities on October 1, in amounts from \$855,000 to \$1,050,000; interest rates from 4.80% to 5.0%; term certificates at 5.4% in the amount of \$6,145,000 maturing on October 1, 2017, and in the amount of \$7,965,000 at 5.43% maturing on October 1, 2022, with annual payments from \$1,015,000 to \$1,765,000 beginning in 2013. 17,100,000

2008 Water Refunding Revenue Certificates of Participation issued to refund the 2006 issue, to provide funding for construction of new downstream water facilities and various water distribution system improvements in connection with Modesto Irrigation District's expansion of the regional water treatment plant; variable rate securities maturing October 1, 2036, with interest initially calculated weekly, fluctuating according to market conditions. The Certificates may be converted to a daily, term, flexible, or fixed rate.

The City entered into a 30 year interest rate swap agreement as discussed below. The combination of the variable rate 2008 COPs and the floating rate swap creates a synthetic fixed-rate debt for the City. The synthetic fixed rate was 3.48% at June 30, 2009. 47,050,000

Total principal balances – business-type activities 69,125,000

Less:

Unamortized bond discount – 1997 Water Certificates of Participation	(296,851)
Unamortized bond discount – 2008 Water Refunding Certificates of Participation	(142,927)
Deferred amount on refunding – 1997 Water Certificates of Participation	(1,000,427)
Deferred amount on refunding – 2008 Water Refunding Certificates of Participation	<u>(618,582)</u>

Total business-type activities certificates of participation \$67,066,213

The City has pledged future Water Enterprise Fund revenues, net of specified operating expenses, to repay the 1997 and 2008 Certificates of Participation, and the loan from the State of California Department of Water Resources, along with the its commitments to the Modesto Irrigation District via its Treatment and Delivery Agreement discussed in Note III F, through 2036. The Water Fund's total principal and interest remaining to be paid on the certificates and loan is \$109,967,340. The Water Fund's principal and interest paid on certificates and loan for the current year, along with payments to Modesto Irrigation District under the Treatment and Delivery Agreement, totaled \$11,665,079, and net revenues of the Fund were \$23,122,152, which represented coverage of 211%.

Annual debt service requirements to maturity for certificates of participation are as follows:

Year Ending June 30,	Governmental Activities		Business-type Activities	
	Principal	Interest	Principal	Interest
2011	1,040,000	906,310	1,480,000	3,085,136
2012	1,090,000	846,670	1,545,000	3,010,706
2013	1,150,000	783,950	1,635,000	2,930,983
2014	1,215,000	717,730	1,705,000	2,847,511
2015	1,285,000	647,730	1,815,000	2,758,480
2016-2020	6,250,000	2,281,750	10,470,000	12,319,863
2021-2025	5,985,000	617,375	12,795,000	9,395,733
2026-2030			13,570,000	6,467,153
2031-2035			16,535,000	3,256,657
2036-2037			7,575,000	253,256
<b>Total</b>	<b>\$18,015,000</b>	<b>\$6,801,515</b>	<b>\$69,125,000</b>	<b>\$46,325,478</b>

Lease Revenue Bonds – Governmental activities:

2008 Lease Revenue Refunding Bonds in the amount of \$65,170,000 issued to refund the balance of the 1998 Lease Revenue Bonds and the 2007 Lease Revenue Refunding and Capital Improvement Bonds; variable rate securities maturing September 1, 2033, with interest initially calculated weekly, fluctuating according to market conditions. The bonds may be converted to a daily, term, flexible, or fixed rate. The combination of the variable rate bonds and a floating swap rate creates a synthetic fixed-rate debt for the City. The synthetic fixed rate was 3.61% at June 30, 2010.

\$64,275,000

Annual debt service requirements to maturity for lease revenue bonds are as follows:

Year Ending June 30,	Principal	Interest
2011	1,020,000	2,947,130
2012	1,125,000	2,897,330
2013	1,260,000	2,839,194
2014	1,395,000	2,776,079
2015	1,505,000	2,707,519
2016-2020	9,055,000	12,329,015
2021-2025	12,920,000	9,795,811
2026-2030	18,225,000	6,110,341
2031-2034	17,770,000	1,488,959
<b>Total</b>	<b>\$64,275,000</b>	<b>\$43,891,378</b>

Revenue Bonds – Business-type activities:

Sewer Enterprise Fund:

Wastewater Treatment Facility Revenue Bonds, Series 2005 Series A and B; Series A (non-taxable) interest payable on November 1 and May 1; serial certificates with annual maturities on November 1, in amounts from \$1,660,000 to \$3,230,000, with interest rates from 3.0% to 5.25%; Series B (taxable) paid in full during 2008 fiscal year.	\$ 31,515,000
Wastewater Revenue Bonds, Series 2006A; interest payable on November 1 and May 1; serial certificates with annual maturities on November 1, in amounts from \$880,000 to \$1,005,000, with interest rates from 4.2% to 4.5%; term certificates in the amount of \$5,710,000 maturing in 2031 and \$7,060,000 maturing in 2036, bearing interest at 4.25%, with annual payments beginning in 2024.	<u>16,535,000</u>
Total principal balances – business-type activities	48,050,000
Plus: Unamortized bond premium - 2005 Bonds	1,661,405
Less:	
Unamortized bond discount – 2006 Bonds	(282,079)
Deferred amount on refunding – 2005 Bonds	<u>(2,678,525)</u>
Total business-type activities revenue bonds	<u>\$ 46,750,801</u>

The 2005 and 2006 bonds were issued to fund a variety of Sewer Enterprise Fund wastewater capital improvements.

The City has pledged future Sewer Enterprise Fund revenues, net of specified operating expenses, to repay the 2005 and 2006 bonds through 2036. The Sewer Fund's total principal and interest remaining to be paid on the bonds is \$74,195,651. The Sewer Fund's principal and interest paid for the current year and total customer net revenues were \$4,110,221 and \$20,925,212 respectively.

Annual debt service requirements to maturity for revenue bonds are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2011	1,765,000	2,250,308
2012	1,855,000	2,159,808
2013	1,955,000	2,064,558
2014	2,050,000	1,964,432
2015	2,160,000	1,859,183
2016-2020	12,530,000	7,579,260
2021-2025	11,000,000	4,195,247
2026-2030	5,245,000	2,592,793
2031-2035	6,485,000	1,350,968
2036-2037	<u>3,005,000</u>	<u>129,094</u>
Total	<u>\$48,050,000</u>	<u>\$26,145,651</u>

Notes Payable – Governmental activities:

Note payable to the Federal Housing and Urban Development Department for the purpose of constructing the Neighborhood Center at Marshall Park and the expansion of the Maddux Youth Center; to be repaid using future Community Development Block Grant revenue; interest rates from 4.0% to 6.01%; semi-annual installments on August 1 and February 1 through August 2024.

\$3,748,000

Fleet Management Internal Service Fund:

Note payable for the acquisition of property related to the Police Fleet Shop; variable interest rate with a minimum of 6% and a maximum of 9%; monthly payments of \$3,010, including interest, through February 2012.

54,436

Total notes payable

\$3,802,436

Annual debt service requirements to maturity for these notes payable are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2011	207,778	206,685
2012	202,658	196,417
2013	191,000	186,906
2014	201,000	177,064
2015	211,000	166,483
2016-2020	1,224,000	643,247
2021-2025	1,565,000	242,387
Total	<u>\$3,802,436</u>	<u>\$1,819,189</u>

Interest Rate Swap Agreements

Objective of the swaps – The primary objective of the swaps is to mitigate the effect of fluctuations in variable interest rates by paying a fixed rate and receiving a floating rate on the swap. Combining a pay-fixed receive-variable rate swap with variable debt results in what is termed “synthetic” fixed rate debt. It is called synthetic because the economics are similar to fixed rate debt, but another instrument is involved unlike regular fixed rate debt. Each time the City created synthetic fixed rate debt a comparison and determination was made that the fixed rate on regular dept would have been higher than the fixed rate on the swap.

During fiscal year 2007, the City entered into an interest swap agreement in connection with the 2006 Water Revenue Certificates of Participation. This transaction was updated due to the refunding of the 2006 Certificates by the 2008 Water Refunding Revenue Certificates of Participation. The swap agreement allows the City to create a synthetic fixed rate on the COPs, protecting it against increases in short-term interest rates. During fiscal year 2008, the City entered into an interest swap agreement in connection with the 1998 and 2007 Lease Revenue Bonds. The swap agreement allows the City to create a synthetic fixed rate on the Lease Revenue Bonds, protecting it against increases in short-term interest rates. The terms, fair value and credit risk of these swap agreements are disclosed below.

Terms - The terms, including the counterparty credit rating of the outstanding swaps, as of June 30, 2010 are shown in the table below. The swap agreements contain scheduled reductions to the outstanding notional amounts that are expected to follow scheduled principal reductions in the associated debt issues.

<u>Related Debt Issue</u>	<u>Notional Amount</u>	<u>Effective Date</u>	<u>Counterparty</u>	<u>Credit Rating (S&amp;P)</u>	<u>Fixed Rate Paid</u>	<u>Variable Rate Received</u>	<u>Termination Date</u>
2008 Water Refunding Revenue COPs	\$47,335,000	5/30/2008	Bank of America	AA+	3.48%	63.7% of 30-day LIBOR, plus .154%	10/1/2036
2008 Lease Revenue Refunding and Capital Improvement	65,170,000	8/28/2008	Bank of America	AA+	3.61%	63.7% of 30-day LIBOR, plus .154%	9/1/2033

Based on the swap agreement the City owes interest calculated at a fixed rate to the counterparty (Bank of America). In return, the counterparty owes the City interest based on the variable rate that approximates the rate required by the associated COPs and lease revenue bonds. Debt principal is not exchanged; it is only the basis on which the swap receipts and payments are calculated.

In June 2008 the GASB issued Statement 53 Accounting and financial Reporting for Derivative Instruments (GASB 53). GASB53 addresses the recognition measurement and disclosure of information regarding derivative instruments entered into by state and local governments. The requirements of this Statement are effective for financial statements for periods beginning after June 15, 2009. The City adopted GASB 53 in Fiscal Year 2010. All derivatives are to be reported on the statement of net assets at fair value and all hedges must be tested for effectiveness to qualify for hedge accounting. The tests are outlined in GASB 53. Depending on the test results, the changes in fair value are either reported on the statement of net assets as a deferral or in the statement of activities as investment revenue or loss.

Fair value – Fair value takes into consideration the prevailing interest rate environment, the specific terms and conditions of each transaction and any upfront payments that may have been received. Fair value was estimated using the zero-coupon discounting method, which calculates the future payments required by the swap, assuming that the current forward rates implied by the LIBOR swap yield curve are the market’s best estimate of future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for a hypothetical zero-coupon rate bond due on the date of each future net settlement on the swaps. As of June 30, 2010, the fair value of the swaps were in favor of the counter party as shown in the following table:

<u>Bond Issue</u>	<u>Fair Value</u>
2008 Water Refunding Revenue Certificates of Participation	(\$10,152,755)
2008 Lease Revenue Bonds	(\$7,507,442)

Credit risk - As of June 30, 2010, the City was not exposed to credit risk on the swaps because the swaps had negative fair value. However, if interest rates increase and the fair value becomes positive, the City would be exposed to credit risk. The City will be exposed to interest rate risk only if the counterparty to the swap defaults or if the swap is terminated.

Basis risk - Basis risk is the risk that the interest rate paid by the City to the bondholders on the underlying variable rate bonds temporarily differs from the variable swap rates received from the counterparty. The swaps have basis risk since the City receives a percentage of the LIBOR Index to offset the actual variable bond rates the City pays on the underlying certificates of participation. The City is exposed to basis risk should the floating rate that it receives on the swap be less than the actual variable rate the City pays on the bonds. Depending on the magnitude and duration of any basis risk shortfall, the expected cost of the basis risk may vary.

A portion of this basis risk is tax risk. The City is exposed to tax risk when the relationship between the taxable LIBOR based swaps and tax-exempt variable rate bonds changes as a result of a reduction in federal and state income tax rates. Should the relationship between LIBOR and the underlying tax-exempt variable rate bonds converge the City is exposed to this basis risk.

**Termination risk** - The City may terminate the swap contracts if the other party fails to perform under the terms of the contracts. The City will be exposed to variable rates if the counterparty defaults or if the swap contract is terminated. A termination of the swap contract may also result in the City's making or receiving a termination payment based on market interest rates at the time of the termination. If at the time of termination the swap has a negative fair value, the City would be liable to the counterparty for a payment equal to the swap's fair value.

**Swap payments and associated debt** – Using rates as of June 30, 2010, debt service requirements of the 2008 Water Refunding Revenue Certificates of Participation and the 2008 Lease Revenue Refunding Bonds including net swap payments and broker fees, are as shown in the following table assuming current interest rates remain the same for their term. These payments are also included in the tables of debt service requirements accompanying the Certificates of Participation and Lease Revenue Bonds disclosures above. The bond interest payments and net swap payments will vary as interest rates vary.

Year Ending June 30	Variable-Rate Bonds		Interest Rate Swap, Net, and Broker Fees	Total
	Principal	Interest		
2011	1,305,000	1,655,194	3,277,970	6,238,164
2012	1,410,000	1,634,438	3,237,416	6,281,854
2013	1,570,000	1,611,488	3,188,751	6,370,239
2014	1,705,000	1,586,419	3,137,619	6,429,038
2015	1,845,000	1,559,269	3,082,147	6,486,416
2016-2020	10,915,000	7,324,031	14,446,753	32,685,784
2021-2025	18,900,000	6,282,600	12,328,919	37,511,519
2026-2030	31,795,000	4,257,282	8,320,214	44,372,496
2031-2035	34,305,000	1,626,469	3,119,147	39,050,616
2036-2037	7,575,000	86,456	166,800	7,828,256
<b>Total</b>	<b>\$111,325,000</b>	<b>\$27,623,646</b>	<b>\$54,305,736</b>	<b>\$193,254,382</b>

### Changes in Long-Term Liabilities

Long-term liability activity for the year ended June 30, 2010, was as follows:

	Beginning Balance (restated)	Additions	Reductions	Ending Balance	Due Within One Year
<b>Governmental activities:</b>					
Loans payable	\$ 903,362			\$ 903,362	
Certificates of participation	19,000,000		\$ 985,000	18,015,000	\$ 1,040,000
Derivative instrument SWAP	0	\$10,172,612		10,172,612	
Lease revenue bonds	65,170,000		895,000	64,275,000	1,020,000
Notes payable	3,999,252		196,816	3,802,436	207,778
Obligations under capital leases	454,401	893,110	125,958	1,221,553	245,598
Compensated absences	9,630,691	9,077,806	9,409,289	9,299,208	3,990,653
Net OPEB obligation	34,203,668	3,583,803		37,787,471	
Claims liability	21,425,553	6,386,687	6,541,335	21,270,905	4,880,570
Governmental activities long-term liabilities	<u>\$154,786,927</u>	<u>\$30,114,018</u>	<u>\$18,153,398</u>	<u>\$166,747,547</u>	<u>\$11,384,599</u>
<b>Business-type activities:</b>					
Loan payable	\$ 1,543,554	6,493,459	\$217,380	\$ 7,819,633	\$1,297,390
Compensated absences	1,971,952	1,859,310	1,391,169	2,440,093	817,363
Net OPEB obligation	7,005,570	734,032		7,739,602	
Derivative instrument SWAP	0	7,518,877		7,518,877	
Certificates of participation	70,545,000		1,420,000	69,125,000	1,480,000
Unamortized discounts	(467,450)		(27,672)	(495,122)	
Deferred amount on refunding	(1,717,536)		(98,527)	(1,816,063)	
Revenue bonds	49,760,000		1,710,000	48,050,000	1,765,000
Unamortized premium	1,789,205		127,800	1,661,405	
Unamortized discount	(292,526)		(10,447)	(302,973)	
Deferred amount on refunding	(2,884,566)		(206,041)	(3,090,607)	
Developer advances	1,892,826		94,395	1,798,431	94,395
Business-type activities long-term liabilities	<u>\$129,146,029</u>	<u>\$16,605,678</u>	<u>\$4,618,057</u>	<u>\$141,133,650</u>	<u>\$5,454,148</u>

Principal balances are reported on the government-wide and enterprise funds statements of net assets net of unamortized issuance discounts and premiums, and deferred amounts on refunding. Internal service funds predominantly serve the governmental funds. Accordingly, long-term liabilities for them are included as part of the above totals for governmental activities. At year end \$54,436 of internal service funds obligations under notes payable, and \$893,110 in capital leases are included in the above amounts. Also, the compensated absences and claims liability balances relate to the internal service funds, and as such they are liquidated by the internal service funds.

Prior year defeasance of debt

In 2005, the City issued refunding Wastewater Revenue Bonds to refund 1993, 1996 and 1997 Wastewater Revenue Bonds. The proceeds were used to purchase U.S. government securities, which were deposited in an irrevocable trust to provide for all future debt service requirements of the three refunded issues. Both the 1993 and 1996 Bonds have been fully redeemed. As of June 30, 2010 \$3,770,000 of 1997 revenue bonds are considered defeased and are not included in the Sewer Fund.

D. OBLIGATIONS UNDER CAPITAL LEASES

Internal Service Funds

A software license valued at \$893,110, less \$0 accumulated depreciation, is being leased under a capital lease arrangement. The following is a schedule of the future minimum lease payments on this capital lease as of June 30, 2010:

Year Ending June 30,	
2011	189,000
2012	189,000
2013	189,000
2014	190,674
2015	190,674
Total minimum lease payments	<u>948,348</u>
Less: amount representing interest	<u>(55,238)</u>
Present value of minimum lease payments	<u>\$893,110</u>

Governmental Funds

One Pierce Quantum 1500GPM Fire Apparatus valued at \$422,524 less \$71,799 accumulated depreciation, is being leased under a capital lease arrangement. The following is a schedule of the future minimum lease payments on this capital lease as of June 30, 2010:

Year Ending June 30,	
2011	77,611
2012	77,611
2013	77,611
2014	77,611
2015	77,611
Total minimum lease payments	388,055
Less: amount representing interest	<u>(59,612)</u>
Present value of minimum lease payments	<u>\$328,443</u>

E. DEVELOPER ADVANCES

The Del Este Water Company (Del Este) entered into various agreements with developers under which infrastructure components were either constructed on behalf of Del Este or cash was advanced to the company to construct the infrastructure. Agreements in existence at the time of the City's acquisition of Del Este were assumed by the City. The terms of repayment call for no interest, with principal paid over a 40-year period. As of June 30, 2010, the total outstanding balance due under the agreements is \$1,798,431. The total annual payments fluctuate depending on the ending date of each agreement. At June 30, 2010, the amount of \$94,395 due during fiscal year 2011 has been reported as "current portion-developer advances" on the Proprietary Funds statement of net assets. The remaining \$1,704,036 of outstanding principal has been reported under noncurrent liabilities, as "developer advances."

F. INTERFUND BALANCES

Interfund balances as of June 30, 2010 consist of the following:

<u>Due to General Fund from:</u>	
Other governmental funds – total due to/due from	\$3,407,995
Other enterprise funds – total due to/ due from	\$261,782
Total Due to from General Fund	<u>\$3,669,777</u>
Total Due to/Due from	<u>\$3,669,777</u>
<u>Advances from General Fund to:</u>	
Capital Facility Fees Fund	\$1,058,998
Other governmental funds	\$245,727
Other enterprise funds	\$1,324,704
Total advances from General Fund	<u>\$2,629,429</u>
<u>Advances from Governmental Funds to:</u>	
Other governmental funds	\$1,249,071
Total advances from Governmental Funds	<u>\$1,249,071</u>
Total Advances from/Advances to	<u>\$3,878,500</u>

All balances reported as "due to/due from" are short-term loans to cover temporary fund cash shortages as of June 30, 2010, and were repaid early in fiscal year 2015. Balances reported as "advance to/advance from" were for capital projects expenditures and are either in the process of being repaid or have scheduled repayments in future years.

G. RESERVES AND DESIGNATIONS OF FUND BALANCES

The City's reserves and designations at June 30, 2010 are comprised of the following:

	<u>General</u>	<u>Capital Facility Fees</u>	<u>Special Gas Tax Street Improvement</u>	<u>Other Governmental</u>
<u>Reserved for:</u>				
Encumbrances	\$2,629,429	\$3,863,854	\$19,671	\$6,027,521
Loan programs				21,886,152
Interfund advances	242,286			
Set-aside requirement				1,055,392
Property held for resale				784,000
Debt service				<u>6,050,302</u>
 Total reserved	 <u>\$2,871,715</u>	 <u>\$3,863,854</u>	 <u>\$19,671</u>	 <u>\$35,803,367</u>
<u>Designated for:</u>				
Pending projects		<u>29,235,667</u>		<u>\$5,056,185</u>
 Total designated	 <u>\$0</u>	 <u>\$29,235,667</u>	 <u>\$0</u>	 <u>\$5,056,185</u>

1. Reserve for encumbrances - Amounts reserved for encumbrances represent the total of outstanding purchase orders and contracts which are scheduled for reappropriation in the next fiscal year.
2. Reserve for loan programs - Amounts equal to the outstanding housing program and small business notes receivable are reserved in the Housing and Community Development Fund Special Revenue Fund and the Redevelopment Agency Capital Projects Fund.
3. Reserve for interfund advances - The City reserves an amount in each fund equal to the advances to other funds.
3. Reserve for Redevelopment Agency set-aside requirement - The portion of fund balance relating to State required low-to-moderate income housing set-aside, has been reserved in the Redevelopment Agency Capital Projects Fund.
5. Reserve for property held for resale - The City reserves an amount equal to the property held for resale by the Redevelopment Agency, since it is not an available spendable resource.
6. Reserve for debt service - The total fund balances of the debt service funds are reserved for future debt service requirements.
7. Designation for pending projects - Designations for pending projects are established to fund projects approved but not yet appropriated.

H. DEFICIT FUND EQUITY

The Special Fund for Capital Outlays and Capital Grants Capital Projects Fund has a deficit fund balance of \$37,111 and \$472,370. The future recognition of currently deferred revenue is expected to resolve this deficit and the negative balance for the Special Fund for Capital Outlays is generated from the fair market value adjustment.

The Golf Enterprise Fund has a net assets deficit of \$2,274,548, due to a change in accounting policy several years ago, as well as revenues not keeping up with expenses. The City originally classified the 1993 Refunding Certificates of Participation as debt of the governmental funds, with construction proceeds transferred to the Golf Enterprise Fund when the certificates were issued. However, since the Golf Fund is paying, and is expected to continue paying, the entire debt service cost, it was decided that the balance of the debt should be recorded in the Golf Fund. The Golf Fund also has struggled due to competition and lagging revenues. Depreciation expense further contributes to the deficit. The City is looking at various options to resolve this funding deficit.

The Employee Benefits Management Internal Service Fund has a net assets deficit of \$40,035,802. It exists partially because the total compensated absences balance previously classified as debt of the governmental funds was included in this fund at its inception several years ago, and has never been fully funded. The City is continuing to charge a higher benefit rate to help reduce this deficit. In addition, one-time revenues having to do with employee benefits are deposited to this fund.

The Insurance Funds have a net assets deficit of \$2,321,503, due mainly to the recognition of settlements that were reached in the prior fiscal year which have been reported as liabilities of the Liability Insurance Fund. Both settlements involved matters that represented city-wide policies and practices and therefore are allocable to all of the funds that make annual contributions to the liability insurance program. The Liability Insurance program will recover the full amount of the settlement from charges to the funds that participate in the liability insurance program over a period of 5 years.

I. INTERFUND TRANSFERS

The following is a schedule of interfund transfers.

Transfers from:

	General Fund	Capital Facilities Fees	Special Gas Tax Street Improvements	Other Govern-mental	Water	Sewer	Bus	Other Enterprise Funds	Internal Service	Total
General Fund		678,000	852,200	\$1,100,148	\$65,000	\$66,000	\$8,400	\$70,000	\$394,694	\$3,234,442
Special Gas Tax St	1,812,175									1,812,175
Other Governmental	3,562,435	233,720	287,450	2,828,317	15,015	15,015			357,677	7,299,629
Water	264,000									264,000
Bus	1,500								202,841	204,341
Other Enterprise	534,327			(59,046)	700,000					1,175,281
Internal Service			307,711		417,310	322,969		366,216		1,414,206
<b>Grand Total</b>	<b>\$6,174,437</b>	<b>\$911,720</b>	<b>\$1,447,361</b>	<b>\$3,869,419</b>	<b>\$1,197,325</b>	<b>\$403,984</b>	<b>\$8,400</b>	<b>\$436,216</b>	<b>\$955,212</b>	<b>\$15,404,074</b>

In general, the City uses interfund transfers to (1) move revenues from the funds that collect them to the funds that statute or budget requires to expend them, (2) use unrestricted revenues collected in the General Fund to help finance various programs and capital projects accounted for in other funds in accordance with budgetary authorization, and (3) move cash to debt service funds from the funds responsible for payment as debt service payments become due.

J. NOTES RECEIVABLE

The notes receivable in the Other Governmental Funds of \$22,415,295 net of \$806,617 allowance for doubtful accounts, consist of loans made for low-income housing rehabilitation, property improvement and small business origination. The loans are collateralized by deeds of trust on the improved properties, are generally interest free with the exception of a small number of direct loans bearing annual interest at 3 or 5 percent and, with a few exceptions, require no repayment of principal until the loans reach maturity.

## K. APPROVED LOANS PAYABLE

The approved loans payable in the Housing and Community Development Special Revenue Fund of \$300,041 consist of amounts being held for rehabilitation of properties using funds provided by federal grants. The liability is expected to be liquidated within one year.

The approved loans payable in the Redevelopment Agency Capital Projects Fund of \$575,000 consists of amounts being held for affordable housing. The liability is expected to be liquidated within a couple years.

## L. SPECIAL ITEMS

These expenses in the Water and Sewer Enterprise funds represent legal costs incurred in pursuit of mitigating damages from the manufacturers of perchlorethylene, or PCE, a common chemical used in the dry cleaning industry. This chemical has seeped into the groundwater through sewer lines when improperly disposed, and threatens the City's groundwater supplies. Modesto has been proactive in attempting to recover damages and future cleanup costs from the dry cleaners and their insurers, and has also initiated litigation with the manufacturers. In the current year the City received payments related to insurance settlements that were deposited to the Sewer fund in the amount of \$412,069.

## III. OTHER INFORMATION

### A. RISK MANAGEMENT

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to and illnesses of employees; and natural disasters. The City maintains the Insurance Internal Service Fund to account for and finance its risks of loss. Under this program, the City is self-insured for the following risks up to the maximum amount per claim/occurrence as follows: workers' compensation \$500,000; liability \$1,000,000. The City purchases commercial insurance for property loss, airport liability, and for claims in excess of the preceding self-insured coverage amounts.

For liability claims, the City is one of twelve members of the Authority for California Cities Excess Liability (ACCEL) risk pool. This pool covers City claims between \$1,000,000 and \$5,000,000. The purpose of the pool is to spread the adverse effect of losses among the member agencies. The City contributes its pro rata share of anticipated losses to the pool. Should actual losses among participants be greater than anticipated, the City will be assessed its pro rata share of that deficiency. Conversely, if the actual losses are less than anticipated, the City will be refunded its pro rata share of the excess. Commercial insurance covers claims over \$5,000,000 in three excess layers, of \$10,000,000 each; for additional coverage of \$35,000,000 per claim. Settled claims have not exceeded this commercial coverage in any of the past five fiscal years.

All operating funds participate in the program and make payments to the Insurance Fund based on historical cost and/or actuarial estimates of the amounts needed to pay prior and current year claims, and to allow accrual of estimated incurred but not reported claims and allocated loss adjustment expenses. Insurance premiums to commercial insurers are also processed through the Insurance Fund. The total claims liability at June 30, 2010 is \$21,270,905 consisting of \$18,239,000 workers' compensation, \$2,647,000 general liability, \$298,619 dental, and \$86,286 vision. Workers' compensation and general liability claims liabilities are estimated on an actuarial basis, and are reported at their net present value using an expected future investment yield assumption of 4.0%. The undiscounted worker's compensation and liability claims totaled \$22,985,000 and \$2,622,000 respectively.

The current portion of the total claims liability is estimated to be \$4,880,570 and the balance of \$16,390,335 is reported as a long-term liability on the statement of net assets. These claim estimates are based on the requirements of Governmental Accounting Standards Board Statement 10, and include estimated claims incurred but not yet reported and allocated loss adjustment expenses as of June 30, 2010. Changes in the Insurance Fund claims liability during the fiscal years ended June 30, 2009 and June 30, 2010 were:

	Claims Liability July 1	Current-Year Claims and Changes in Estimates	Current-Year Claim Payments	Claims Liability June 30
2008-09	22,949,872	2,057,837	(3,582,156)	21,425,553
2009-10	21,425,553	6,386,687	(6,541,335)	21,270,905

**B. COMMUNITY FACILITIES DEBT WITHOUT CITY COMMITMENT**

Special assessment and community facilities districts have been established in various areas of the City to provide improvements to properties located in those districts. Properties are assessed for the cost of the improvements; these assessments are payable solely by the property owners over the term of the debt issued to finance the improvements. The City is not legally obligated to pay these debts or be the purchaser of last resort of foreclosed properties in the special assessment districts, nor is it obligated to advance City funds to repay this debt in the event of default by any property owners. The City functions as an agent for the property owners by collecting assessments and forwarding collections to trustees for payment to bond holders. At June 30, 2010, the balance of these districts' outstanding debt was as follows:

Issue	Outstanding Amount
Village One #2 Community Facilities District	\$30,825,000
Fairview Village Community Facilities District	4,900,000

**C. CONDUIT DEBT OBLIGATIONS**

From time to time, the City has issued revenue bonds to provide financial assistance to private-sector entities for the acquisition and construction of industrial, commercial, health care, and multiple-family housing facilities deemed to be in the public interest. The bonds are secured by the property financed and are payable solely from developer payments on the underlying mortgage loans. Upon repayment of the bonds, ownership of the acquired facilities transfers to the private-sector entity served by the bond issuance. Neither the City, the State, nor any political subdivision thereof is obligated in any manner for repayment of the bonds. Accordingly, the bonds are considered conduit debt obligations and are not reported as liabilities in the accompanying financial statements.

As of June 30, 2010 there were six series of conduit revenue bonds outstanding. The aggregate principal amount payable for these multiple-family housing and health care facility bond issues, issued between 1993 and 2002, was \$34,960,000.

**D. COMMITMENTS AND CONTINGENCIES**

The City is involved in litigation relating to tort claims, workers' compensation claims and other claims such as contract actions and inverse condemnation actions for which the City is self-insured. The City is a defendant in various matters of litigation. On one such matter, there is the possibility the City may incur losses over \$100 million. Of the remaining matters, management and the City legal counsel do not anticipate any material effect on the June 30, 2010 financial statements. However, the outcome of the litigation is not known and no liability has been accrued on the financial statements.

In the 1950's and 1960's, the City operated a landfill facility outside the city limits. This facility was closed in 1968, to the standards in effect at that time. State and federal laws and regulations require that the City perform certain maintenance and monitoring functions. Testing performed during fiscal year 2007 indicated that methane emissions in the area had exceeded State standards, however, quarterly groundwater monitoring at the site has determined that the landfill has experienced a "release" that measurably affects groundwater. The City has to develop a plan to monitor the release and determine the nature and extent of impacts. An engineering feasibility study must be completed to determine if the City should remove/treat the release, or just continue to monitor the release. To conclude, depending on the results of the engineering feasibility study, the City will need to implement the recommended action, which could involve construction and operation of a groundwater treatment system. If additional post closure care requirements are determined (due to changes in technology or applicable laws or regulations, for example), these costs may result in increased charges to future landfill users. As of June 30, 2010, the future post closure care cost of monitoring the landfill was calculated to be immaterial for presentation purposes which include the agreement cost for the study.

The City receives funding from a number of federal, state and local grant programs, principally the Federal Highway Administration, Community Development Block Grants, and Federal Transit Administration grants. These programs are subject to financial and compliance review by the grantors. Accordingly, the City's compliance with applicable grant requirements will be determined at some future date. Expenditures, if any, which may be disallowed by the granting agencies, cannot be determined at this time. The City does not expect the undeterminable amounts of disallowed expenditures, if any, to materially affect the basic financial statements. Receipt of these federal, state and local grant revenues is not assured in the future.

The City has commitments of \$29,860,252 as of June 30, 2010 for contracts awarded but not completed and other outstanding purchase orders. This amount consists of \$242,286 in the General Fund, \$3,863,854 in the Capital Facility Fees Fund, \$19,671 in the Special Gas Tax Street Improvements, \$6,018,268 in other governmental funds, \$17,990,658 in the enterprise funds, and \$1,700,281 in the internal service funds. Commitments of the governmental funds are recorded as fund balance reserves for encumbrances on the balance sheet. As of June 30, 2010, there are major contracts and other purchase orders outstanding for water and sewer system improvements, vehicle purchases, new financial system, construction of a new bus maintenance facility, comprehensive update to the City's general plan, major street improvements, and the purchase of buses.

#### E. JOINT VENTURES AND JOINTLY GOVERNED ORGANIZATION

##### Tuolumne River Regional Park

The City participates with Stanislaus County and the City of Ceres in the operation and development of the Tuolumne River Regional Park (TRRP). The governing body consists of 2 members from the County Board of Supervisors, 2 members from the Modesto City Council, and 1 member from the Ceres City Council. The TRRP board prepares the annual budget, which must be approved by both cities' councils and the board of supervisors. Each participant has an equity interest in the capital assets of TRRP based on the percentage of cumulative contributions paid. The City's contribution to TRRP was \$132,721 for the fiscal year ended June 30, 2010. As of June 30, 2010 the City's investment in this joint venture was \$1,795,115, and is included in governmental activities on the statement of net assets. Financial statements for TRRP are prepared by the City of Modesto Finance Department.

##### Stanislaus Drug Enforcement Agency

Stanislaus County (County) and the cities of Modesto, Oakdale, Ceres, Patterson, Turlock, Riverbank and Newman are the participants in the Stanislaus Drug Enforcement Agency (SDEA). The purpose of the SDEA is to maintain a specially trained police unit to assist each of the participating agencies in the enforcement of drug control laws, and to study, plan, and set priorities for effective enforcement of such laws throughout Stanislaus County. The governing board consists of the sheriff of Stanislaus County and the chief of police of each participating city. All participants contribute to the funding of the SDEA budgeted expenditures, based on population and assessed property value. The City's cash contribution to the SDEA for the fiscal year ended June 30, 2010 was \$673,358. The City's investment in this joint venture was estimated to be \$381,905 as of June 30, 2010, based on the most recent available information. This amount is reported in governmental activities in the statement of net assets. Financial statements of the SDEA are prepared by the City of Modesto Finance Department.

##### City-County Capital Improvements and Financing Agency

The City and Stanislaus County formed the City-County Capital Improvements and Financing Agency (Agency) to provide for the design, construction, ownership, operation, management and financing of a City-County administration center located in Modesto's downtown redevelopment area. The governing body is a commission consisting of 2 members of the City Council, 2 members of the County Board of Supervisors, the County Chief Executive Officer, and the City Manager. The commission is responsible for developing an annual budget and determining the annual contribution rates, subject to approval by both the City and the County. The Stanislaus County Auditor Controller was the fiscal administrator during the construction phase, which was finalized at the end

of June 2003. Since then, the City of Modesto has been the fiscal administrator through fiscal year 2010. For the fiscal year ended June 30, 2010, the City's payments to the Agency were \$668,972 for operations and capital reserve. The City's equity interest in the Agency is \$11,719,961, equal to its capital asset contributions to date net of depreciation, and is reported in governmental activities as investments in joint ventures in the Statement of Net Assets. Financial statements of the Agency will be available from the Agency after the initial audit of the Agency's books has been completed.

#### Stanislaus Waste-to-Energy Financing Agency

The City participates with Stanislaus County in the Stanislaus Waste-to-Energy Financing Agency (Agency). The Agency was created to provide financing for a facility that generates power from solid waste. The costs of operating the Agency, if any, are shared equally by the participants. The governing body consists of 2 members each from the County Board of Supervisors and the Modesto City Council. As of June 30, 2010, the City has no equity interest. Stanislaus County Treasurer's office prepares the Agency's financial statements.

#### Regional Fire Training Center

The City has entered into an agreement with the Yosemite Community College District (YCCD) and Stanislaus County for the use and management of the regional fire training center at Modesto Junior College. The executive board consists of the YCCD Chancellor, the President of Modesto Junior College, the City Manager of the City of Modesto, and the Chief Executive Officer of Stanislaus County. The YCCD is responsible for accounting and for monitoring the center's budget. All three entities share in the operating costs. Initial construction costs were paid by the YCCD from borrowed funds, with the City and County reimbursing a portion of these costs in exchange for future use of the center. The City has paid its share of the construction costs in full. Title to the constructed asset is held by the YCCD; therefore, the City has no equity interest.

### F. TREATMENT AND DELIVERY AGREEMENT

In 1992, the City entered into a treatment and delivery agreement with the Modesto Irrigation District (MID) and the Del Este Water Company (Del Este). The City assumed Del Este's interest and obligations under the agreement when it acquired Del Este in July 1995. Under the agreement, MID built and operates a surface water treatment plant on the Tuolumne River for the purpose of providing a long-term source of domestic treated water for the City. MID is the sole owner of the project, and has all management and operations responsibility. In exchange for the treated water, the City has agreed to pay: all debt service on bonds issued by MID for the construction of the project; a raw water charge as set forth in the agreement; project operation, administration, and maintenance costs; and insurance on the project. Gross revenues of the City's Water Fund are irrevocably pledged for the punctual payment of the MID debt service and all obligations of the City under any parity debt. Current parity debt of the City consists of the 2008 Water Revenue Certificates of Participation, 1997 Water System Improvement Project Refunding Certificates of Participation, and the California Safe Drinking Water Act loan (Note II-C). The minimum annual amount payable to MID, consisting of the debt service component only, is \$7,369,086. The treatment plant completed all tests and began commercial operations on May 15, 1995, at which time the City began paying for raw water and operations. The total cash paid to MID during the fiscal year ended June 30, 2010 was \$13,058,482 which is reported as "water purchases" expense on the proprietary funds statement of revenues, expenses and changes in net assets.

The City and MID have agreed upon an expansion of the initial Domestic Water Project facilities beyond the existing design capacity of 36 million gallons per day ("mgd") to a design capacity of 72 mgd. In June 2007, the MID issued \$93,190,000 Domestic Water Project revenue bonds pursuant to the terms of the existing treatment and delivery agreement. As of June 30, 2010, the total outstanding on the MID bonds is: \$63,995,000 for the 1998 bonds, and \$93,190,000 for the 2007 bonds for a total of \$157,185,000.

G. POST-RETIREMENT HEALTH CARE DEFINED BENEFIT PLAN

Plan Description

In addition to the pension benefits described below in Note III-H, the City provides health care benefits to employees who retire from the City, under contractual agreements with all employee groups. All full-time employees, except firefighters who receive a cash payout, are eligible to set aside a percentage of accumulated sick leave upon retirement to be used for payment of future health care premiums to a choice of four insurance plans. The City has no obligation to pay the health insurance allowance for retirees with no accumulated sick leave. As of June 30, 2010 there were 435 participants receiving these health care benefits.

The OPEB Plan provisions and benefits in effect at June 30, 2010, are summarized as follows:

	Police (including Management)	General Employees	Management	Fire	Fire Management
Benefit Types Provided	Medical, dental and vision	Medical, dental and vision	Medical, dental and vision	Medical only	Medical, dental and vision
Duration of Benefits	One month per eight hours of converted sick leave	One month per eight hours of converted sick leave	One month per eight hours of converted sick leave	Lifetime	One month per eight hours of converted sick leave
City Health Allowance per month	\$535.00 for single  \$1,050.00 with dependents	\$535.00 for single  \$1,050.00 with dependents	\$540.88 for single  \$1,050.00 with dependents	\$97.00	\$540.88 for single  \$1,050.00 with dependents

Except for the Fire group, the City health allowance amounts may increase each year based on the health allowance for active employees. For the Fire group, the City health allowance amounts increase each year in accordance with Government Code Section 22825.

Funding Policy and Actuarial Assumptions

The City's funding policy for the Plan is to fund benefits on a pay-as-you-go basis. The annual required contribution was determined as part of the December 1, 2008 actuarial valuation using the entry age normal actuarial cost method. This is a projected benefit cost method, which takes into account those benefits that are expected to be earned in the future as well as those already accrued. The actuarial assumptions included (a) 5% investment rate of return, (b) 3% projected annual salary increase, and (c) 4% health inflation increases. The actuarial methods and assumptions used include techniques that are designed to reduce the short-term volatility in actuarial accrued liabilities. Actuarial calculations reflect a long-term perspective and actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Actuarially determined amounts are subject to continual revision as results are compared to past expectations and new estimates are made about the future. The City's OPEB unfunded actuarial accrued liability is being amortized as a level percentage of projected payroll on a closed basis. The remaining amortization period at June 30, 2010 was 30 years.

The City has set aside \$17,200,599 of Employee Benefits Management Internal Service Fund cash and investments to be used to fund the above benefits. Generally accepted accounting principles permit assets to be treated as OPEB assets and deducted from the Actuarial Accrued Liability when such assets are placed in an irrevocable trust or equivalent arrangement. Since the City's Internal Service Fund does not meet this requirement, the assets have been excluded from the actuarial study and calculation. This funding policy means that the City contributions are considered to be on a pay-as-you-go basis. As a result, the City has calculated and recorded the Net OPEB Obligation, representing the difference between the ARC and the pay-as-you-go contributions, as presented below.

In prior years, the City estimated and recorded an accrued liability representing unfunded retiree pension costs in its Employee Benefits Management Internal Service Fund. In accordance with GASB 45, municipalities are permitted to retain an estimated liability for prior years unfunded OPEB costs (liability at transition), so long as it is calculated in a manner consistent with GASB Statement 27, which employed methodologies consistent with those now required under GASB 45.

This liability is now reflected as part of the Net OPEB Obligation below:

Annual required contribution	\$ 5,627,617
Adjustment to annual required contribution	<u>1,263,290</u>
Annual pension cost	6,890,907
Contributions made	<u>(2,573,072)</u>
(Decrease) increase in net pensions obligations	4,317,835
Net pension obligation (asset) June 30, 2009	<u>41,209,238</u>
Net OPEB obligation (asset) June 30, 2010	<u><u>\$45,527,073</u></u>

The Plan annual required contributions and actual contributions for the year ended June 30, 2010 is set forth below:

Fiscal Year	Annual Required Contribution (ARC)	Actual Contribution	Percentage of ARC Contributed	Net OPEB Obligation
6/30/2008	\$5,752,966	\$2,125,269	36.9%	\$37,180,914
6/30/2009	\$5,627,617	\$2,862,583	50.8%	\$41,209,238
6/30/2010	\$5,627,617	\$2,573,072	45.7%	\$45,527,073

The Schedule of Funding Progress presents multi-year trend information about whether the actuarial accrued liabilities are increasing or decreasing over time.

Actuarial Valuation Date	Actuarial Value of Assets (A)	Entry Age Actuarial Accrued Liability (B)	Overfunded (Underfunded) Actuarial Accrued Liability (A-B)	Funded Ratio (A/B)	Covered Payroll (C)	Overfunded (Underfunded) Actuarial Liability as Percentage of Covered Payroll [(A-B)/C]
12/1/2006	\$0	\$58,780,482	(\$58,780,482)	0.00%	\$75,994,853	-77.35%
12/1/2008	\$0	\$53,361,991	(\$53,361,991)	0.00%	\$82,049,847	-65.00%

#### H. DEFINED BENEFIT PENSION PLAN

##### Plan Description

The City contributes to the California Public Employees Retirement System (CalPERS), an agent multiple-employer public employee defined benefit pension plan, which acts as a common investment and administrative agent for participating public entities in California. CalPERS provides retirement and disability benefits, and death benefits to plan members and beneficiaries. 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: 400 P Street, Sacramento, CA 95814. An annual financial report for the City's portion of the plan is not available.

##### Funding Policy

Participants are required to contribute 7% (9% for safety employees) of their annual covered salary, of which the City pays the majority on behalf of the employees. The City is required to contribute at an actuarially determined rate; the current rate is 9.192% of annual covered payroll for non-safety employees and 23.494% for safety employees. The contribution requirements of plan members and the City are established and may be amended by CalPERS.

## Annual Pension Cost

For 2010, the City's annual pension cost of \$11,938,820 for CalPERS was equal to the City's required and actual contributions. The required contribution was determined as part of the June 30, 2009 actuarial valuation using the entry age normal actuarial cost method. This is a projected benefit cost method, which takes into account those benefits that are expected to be earned in the future as well as those already accrued. The actuarial assumptions included (a) 7.75% investment rate of return (net of administrative expenses), (b) projected annual merit or seniority salary increases that vary by length of service, and (c) no post-retirement benefit increases. Both (a) and (b) included an inflation component of 3.0%. The actuarial value of the City's CalPERS assets was determined using techniques that smooth the effects of short-term volatility in the market value of investments over a three-year period (smoothed market value). The City's CalPERS unfunded actuarial accrued liability is being amortized as a level percentage of projected payroll on a closed basis. The remaining amortization period at June 30, 2010 was 30 years for both the miscellaneous and safety plans. The schedule of funding progress presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

### **THREE-YEAR TREND INFORMATION FOR PERS – MISCELLANEOUS PLAN**

<u>Fiscal Year</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
6/30/08	4,338,969	100%	-
6/30/09	4,534,013	100%	-
6/30/10	3,975,302	100%	-

### **THREE-YEAR TREND INFORMATION FOR PERS – SAFETY PLAN**

<u>Fiscal Year</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
6/30/08	8,333,064	100%	-
6/30/09	8,227,551	100%	-
6/30/10	7,963,518	100%	-

### **SCHEDULE OF FUNDING PROGRESS FOR PERS**

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets (A)</u>	<u>Entry Age Actuarial Liability (B)</u>	<u>Overfunded (Underfunded) Actuarial Accrued Liability (A – B)</u>	<u>Funded Ratio (A/B)</u>	<u>Covered Payroll (C)</u>	<u>Unfunded Actuarial Liability as Percentage of Covered Payroll [(A – B)/C]</u>
<b>6/30/06:</b>						
Misc.	\$234,337,099	\$248,371,895	\$(14,034,796)	94.3%	\$43,582,742	32.2%
Safety	258,762,829	293,433,828	(34,670,999)	88.2%	32,412,111	107.0%
<b>6/30/07:</b>						
Misc.	\$253,412,785	\$266,796,934	\$(13,384,149)	95.0%	\$45,986,674	29.1%
Safety	281,892,523	317,040,705	(35,148,182)	88.9%	34,438,667	102.1%
<b>6/30/08:</b>						
Misc.	\$273,210,580	\$288,300,448	\$(15,089,868)	95.8%	47,469,554	31.8%
Safety	303,140,879	343,910,847	(40,769,968)	88.1%	34,990,413	116.5%
<b>6/30/09:</b>						
Misc.	\$285,106,834	\$313,072,676	\$(27,965,842)	91.1%	45,995,050	60.8%
Safety	317,429,425	373,587,194	(56,157,769)	85.0%	33,646,382	166.9%

## I. PRIOR YEAR ADJUSTMENTS

### Governmental Activities

Various state revenues had been collected in advance in FY 08-09 which have not yet been expended. A prior year adjustment has been reported in the Special Gas Tax Street Improvement to account for this correction in the amount of (\$674,436). A prior year adjustment has been reported in the Fleet Management Fund in the amount of (\$33,542) to correct a capital asset that was reported twice in error. For the governmental funds capital assets, an error in the amount of (\$218,446) was identified when assets were being retired for joint power agencies. The total amount of the prior period adjustment for governmental activities was a reduction of net assets in the amount of (\$926,424).

### Business-type Activities

The Water Fund and Sewer Fund reported a prior year adjustment in the amount of (\$3,590,442) and (\$1,662,950) to correct several capital improvement projects that were capitalized in error and should have been reported as operating expenses. Additionally, a few Sewer Fund construction projects when completed and transferred to improvements were not assigned the correct completion date but the original date of when construction began. The correction for this error was \$986,561.

In the Water Fund the City entered into a Memorandum of Understanding in July 2008 with the Modesto Irrigation District related to the EIFS repair and roof replacement project for the Modesto Regional Water Treatment Plant facilities. The City reimbursement for these repairs is (\$6,493,458) and the payments will begin in FY 2010-11 and spread over five annual installments. This reimbursement has been reported as a loans payable on the Water Fund statements.

A prior year adjustment was reported in the Golf Fund in the amount of \$5,000 to adjust a prior year accrual accounted for twice. The total amount of the prior period adjustment for business-type activities was a reduction of net assets in the amount of (\$6,244,954).

## J. SUBSEQUENT EVENTS

### 1) ARRA (American Recovery and Reinvestment Act) Funding

On June 2009, the Council authorized the City submit an application for the Energy Efficiency and Conservation Block Grant. In FY 2010-11, the City was awarded \$1,952,900 in grant funds for this grant to fund new capital improvement projects will include upgrading HVAC units at City buildings, installing foam roofs and solar panels on City buildings, replacing high pressure sodium lights with LED lights and replacing inefficient light fixtures at the Transportation Center with more energy efficiency fixtures.

### 2) Bond Disclosure Information

The City of Modesto, Wastewater Revenue Refunding Bonds, Series 2005A, Wastewater Revenue Bonds, Series 2006A, and Water Refunding Revenue Certificates of Participation, 2008 Series A had to report a specified event to SEC due to on October 25, 2010, Standards & Poor's changed the insured rating on these bonds identified above to AA+ from AAA as a result of the downgrading of Assured Guaranty the insurer of these bonds.

In October 2010, the City of Modesto received a confirmed AA- rating from Fitch on the City's Wastewater Revenue Bonds, Series 2005 and 2006.

In August 2010, the City placed a \$9 million collateral posting deposit with JP Morgan in order to secure a \$29 million negative position under the 2007 Swap Agreement for the 2007 Modesto Irrigation District (MID) Revenue Bonds based on the termination value and the Pledgor's Threshold. In May 2007, the Council adopted Resolution 2007-275 approved the issuance of revenue bonds by the Modesto Irrigation District Financing Authority related to the financing of Phase 2 of the Treatment and Delivery Agreement with MID. This debt issued included an interest rate swap agreement with Bear Sterns Capital Markets, and is being assigned to JP Morgan Chase Bank. Under the existing

Swap Agreement if three conditions exist, then the City can be required to post collateral with an independent trustee to assure JP Morgan Chase Bank's financial interests in the event the agreement is terminated. These conditions include: 1) the credit rating of the bond and swap payment insurer (MBIA) must fall below A-. Currently, the credit rating for MBIA is in the BBB category. 2) The lowest credit rating for the Modesto Irrigation District revenue bonds is below AA-. These bonds have a credit rating of AA-/A+. 3) The Swap Agreement Pledgor's Threshold against the City is greater than \$20 million. Currently, it is approximately \$18 million. The termination value is calculated daily and could increase or decrease from its current level in response to changing interest rates. If these three conditions exist, then the City is responsible under the terms of the agreement to post collateral with a third-party trustee. The ownership of this collateral resides with the City, including any interest earnings, and is used in case the Swap Agreement is terminated and the City failed to pay the termination payment. In July 2010, the City's assignment agreement raised the Pledgor's Threshold from \$5 million to \$20 million which reduced the amount of collateral posted to the trustee.

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## **REQUIRED SUPPLEMENTARY INFORMATION**



**SCHEDULE 1 - SCHEDULE OF FUNDING PROGRESS FOR PERS**

Actuarial Valuation Date**	Actuarial Value of Assets (A)	Entry Age Actuarial Accrued Liability (B)	Overfunded (Underfunded) Actuarial Accrued Liability (A - B)	Funded Ratio (A/B)	Covered Payroll (C)	Unfunded Actuarial Liability as Percentage of Covered Payroll [(A - B)/C]
<b>6/30/04:</b>						
Misc.	\$204,261,809	\$212,669,957	\$(8,408,148)	96.0%	\$41,083,600	20.5%
Safety	221,621,121	257,554,567	(35,933,446)	86.0%	29,085,514	123.5%
<b>6/30/05:</b>						
Misc.	\$218,307,677	\$231,079,054	\$(12,771,377)	94.5%	\$42,221,273	30.2%
Safety	239,178,942	273,741,974	(34,563,032)	87.4%	30,117,501	114.8%
<b>6/30/06:</b>						
Misc.	\$234,337,099	\$248,371,895	\$(14,034,796)	94.3%	\$43,582,742	32.2%
Safety	258,762,829	293,433,828	(34,670,999)	88.2%	32,412,111	107.0%
<b>6/30/07:</b>						
Misc.	\$253,412,785	\$266,796,934	\$(13,384,149)	95.0%	\$45,986,674	29.1%
Safety	281,892,523	317,040,705	(35,148,182)	88.9%	34,438,667	102.1%
<b>6/30/08:</b>						
Misc.	\$273,210,580	\$288,300,448	\$(15,089,868)	95.8%	47,469,554	31.8%
Safety	303,140,879	343,910,847	(40,769,968)	88.1%	34,990,413	116.5%
<b>6/30/09:</b>						
Misc.	\$285,106,834	\$313,072,676	\$(27,965,842)	91.1%	45,995,050	60.8%
Safety	317,429,425	373,587,194	(56,157,769)	85.0%	33,646,382	166.9%

\*\* Most recent actuarial dated information is for June 30, 2009.

**SUMMARY ACTUARIAL INFORMATION FOR PENSION PLAN**

Valuation Date	June 30, 2009
Actuarial Cost Method	Entry Age Normal Cost Method
Amortization Method	Level percent of Payroll
Average Remaining Period	32 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)
Overall Payroll Growth employment	3.25% to 14.45% depending on Age, Service, and type of employment
Inflation Rate	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%.

**SCHEDULE 2 - SCHEDULE OF FUNDING PROGRESS FOR OPEB**

Actuarial Valuation Date**	Actuarial Value of Assets (A)	Entry Age Actuarial Accrued Liability (B)	Overfunded (Underfunded) Actuarial Accrued Liability (A-B)	Funded Ratio (A/B)	Covered Payroll (C)	Overfunded (Underfunded) Actuarial Liability as Percentage of Covered Payroll [(A-B)/C]
12/1/2006	\$0	\$58,780,482	(\$58,780,482)	0.00%	\$75,994,853	-77.35%
12/1/2008	\$0	\$53,361,991	(\$53,361,991)	0.00%	\$82,049,847	-65.00%

\*\* The valuation date available is through 2008.

**SCHEDULE 3- EMPLOYER CONTRIBUTIONS (OPEB)**

Fiscal Year	Annual Required Contribution (ARC)	Actual Contribution	Percentage of ARC Contributed
6/30/2008	\$5,752,966	\$2,125,269	36.9%
6/30/2009	\$5,627,617	\$2,862,583	50.8%
6/30/2010	\$5,627,617	\$2,573,072	45.7%

**SUMMARY ACTUARIAL INFORMATION FOR OPEB**

Valuation Date	June 30, 2008
Actuarial Cost Method	Entry Age Normal
Amortization Method	Level percent of Payroll
Amortization Period	10 Year for initial unfunded liability; 30 year for open period for remaining liability

**ACTUARIAL ASSUMPTIONS**

Investment Rate of Return	5.00%
Health Trend Rate	4.00%
Inflation Rate	3.00%
Payroll Growth	3.00%

**CITY OF MODESTO**  
**SCHEDULE OF REVENUES - BUDGET (GAAP BASIS)**  
**AND ACTUAL - GENERAL FUND**  
**Year ended June 30, 2010**

	Budget		Actual	Variance with Final Budget - Positive (Negative)
	Original	Final		
<b><u>TAXES:</u></b>				
Utility users tax	\$ 19,000,000	\$ 19,000,000	\$ 19,117,518	\$ 117,518
Property tax	12,470,099	12,470,099	12,306,702	(163,397)
Transient occupancy tax	2,050,000	2,050,000	1,460,613	(589,387)
Franchise tax	4,021,306	4,021,306	3,902,877	(118,429)
Business license tax	8,947,462	8,947,462	9,068,219	120,757
<b>Total taxes</b>	<b>46,488,867</b>	<b>46,488,867</b>	<b>45,855,929</b>	<b>(632,938)</b>
<b><u>LICENSES AND PERMITS</u></b>	<b>77,862</b>	<b>95,312</b>	<b>83,039</b>	<b>(12,273)</b>
<b><u>INTERGOVERNMENTAL:</u></b>				
Sales tax	17,469,619	17,469,619	16,688,722	(780,897)
In-lieu sales tax	6,047,636	6,047,636	5,612,338	(435,298)
Motor vehicle license fees	13,874,508	13,874,508	13,945,172	70,664
State	960,000	980,700	917,672	(63,028)
County	851,000	991,000	1,081,512	90,512
Federal	576,593	174,943	191,459	16,516
Other intergovernmental	665,570	705,570	613,342	(92,228)
<b>Total intergovernmental</b>	<b>40,444,926</b>	<b>40,243,976</b>	<b>39,050,217</b>	<b>(1,193,759)</b>
<b><u>CHARGES FOR SERVICES:</u></b>				
General government	2,088,232	2,157,042	2,324,955	167,913
Community development	3,183,149	3,589,799	2,448,693	(1,141,106)
Public works	7,075	7,075	3,213	(3,862)
Parks and recreation	2,355,313	2,394,165	2,677,297	283,132
Public safety	2,174,260	2,089,824	1,815,077	(274,747)
Other current charges for services	132,176	132,176	56,955	(75,221)
Indirect cost recovery	3,689,416	3,689,416	3,721,505	32,089
<b>Total charges for services</b>	<b>13,629,621</b>	<b>14,059,497</b>	<b>13,047,695</b>	<b>(1,011,802)</b>
<b><u>INTEREST AND RENT</u></b>	<b>251,788</b>	<b>241,300</b>	<b>290,902</b>	<b>49,602</b>
<b><u>NET INCREASE (DECREASE) IN FAIR VALUE OF INVESTMENTS</u></b>			<b>54,744</b>	<b>54,744</b>
<b><u>FINES AND FORFEITURES</u></b>	<b>970,000</b>	<b>1,002,981</b>	<b>1,042,067</b>	<b>39,086</b>
<b><u>MISCELLANEOUS:</u></b>				
Mandated cost recovery			129,046	129,046
Other	910,053	1,201,731	1,399,261	197,530
<b>Total miscellaneous</b>	<b>910,053</b>	<b>1,201,731</b>	<b>1,528,307</b>	<b>326,576</b>
<b>Total revenues</b>	<b>\$ 102,773,117</b>	<b>\$ 103,333,664</b>	<b>\$ 100,952,900</b>	<b>\$ (2,380,764)</b>

The notes to required supplementary information are an integral part of this schedule

**CITY OF MODESTO**  
**SCHEDULE OF EXPENDITURES BY FUNCTION - BUDGET**  
**(GAAP BASIS) AND ACTUAL - GENERAL FUND**  
**Year ended June 30, 2010**

	Budget		Actual	Variance with Final Budget - Positive (Negative)
	Original	Final		
General government:				
City council	\$ 442,776	\$ 427,776	\$ 338,875	\$ 88,901
Personnel/training	1,105,418	1,336,433	1,316,033	20,400
City manager	1,188,775	1,247,883	1,127,256	120,627
City attorney	1,868,062	1,915,081	1,707,579	207,502
City clerk/auditor	670,452	670,452	650,784	19,668
Finance	4,418,581	4,675,375	4,101,400	573,975
Other	673,991	920,939	870,753	50,186
Total general government	<u>10,368,055</u>	<u>11,193,939</u>	<u>10,112,680</u>	<u>1,081,259</u>
Community development	<u>5,050,444</u>	<u>5,287,783</u>	<u>5,145,993</u>	<u>141,790</u>
Public works:				
Engineering and Transportation Dept:				
Engineering administration	32,833	32,833	31,491	1,342
Operations and Maintenance Dept:				
Service and maintenance	2,296,958	2,384,498	2,325,747	58,751
Graffiti abatement	277,948	277,948	256,155	21,793
Total public works	<u>2,607,739</u>	<u>2,695,279</u>	<u>2,613,393</u>	<u>81,886</u>
Parks and recreation:				
Operations and Maintenance Dept:				
Service and maintenance	5,083,076	5,196,928	4,727,604	469,324
Community Services & Neighborhood Connection:				
Administration	672,601	908,385	898,476	9,909
Planning and development	236,251	239,851	238,412	1,439
Culture	1,247,476	1,277,889	1,210,697	67,192
Recreation division	1,816,673	1,816,838	1,753,560	63,278
Facilities	488,101	508,011	410,383	97,628
Total parks and recreation	<u>9,544,178</u>	<u>9,947,902</u>	<u>9,239,132</u>	<u>708,770</u>
Public safety:				
Fire protection	24,284,040	25,711,717	24,934,719	776,998
Police protection	51,347,585	50,359,389	47,745,386	2,614,003
Total public safety	<u>75,631,625</u>	<u>76,071,106</u>	<u>72,680,105</u>	<u>3,391,001</u>
Total expenditures by department	<u>103,202,041</u>	<u>105,196,009</u>	<u>99,791,303</u>	<u>5,404,706</u>
Total expenditures	<u>\$ 103,202,041</u>	<u>\$ 105,196,009</u>	<u>\$ 99,791,303</u>	<u>\$ 5,404,706</u>

The notes to required supplementary information are an integral part of this schedule

**CITY OF MODESTO**  
**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION**  
**YEAR ENDED JUNE 30, 2010**

BUDGETARY INFORMATION - The City follows these procedures annually in establishing the budgetary data reflected in the budgetary comparison schedules:

1. The City Manager submits to the City Council a proposed budget for the fiscal year commencing the following July 1. The budget includes proposed expenditures and the means of financing them.
2. The City Council reviews the proposed budget at specially scheduled sessions, which are open to the public. The Council also conducts a public hearing on the proposed budget to obtain comments from interested persons.
3. Prior to July 1, the budget is legally adopted through passage of an ordinance. This budget is reported as the Original Budget in the budgetary comparison schedules.
4. During the fiscal year, changes to the adopted budget may be authorized, as follows:
  - a. Items requiring City Council action - appropriation of fund balance reserves; transfers of appropriations between funds; appropriation of any non-departmental revenue; new interfund loans or advances; and creation of new capital projects or increases to existing capital projects.
  - b. Items delegated to the City Manager - transfers between departments within funds; appropriation of unbudgeted departmental revenues; and approval of transfers that increase salary and benefit appropriations.
  - c. Items delegated to the Finance Director - approval authority over any changes in or transfers from budgeted allocations for Internal Service Fund charges.
  - d. Items delegated to Department Heads - allocation of departmental appropriations to line item level.
5. Formal budgetary accounting is employed as a management tool for all funds. Annual budgets are legally adopted and amended as required for the general, special revenue, enterprise and internal service funds. Project length budgets are adopted for the capital projects funds. All budgets are prepared on a basis consistent with generally accepted accounting principles (GAAP), and budgetary comparisons for the general and major special revenue funds are presented on this basis in the required supplementary information. A debt service payment schedule for the debt service funds is also approved as part of the budget process.
6. Budget amounts are reflected after all authorized amendments and revisions. This budget is reported as the Final Budget in the budgetary comparison schedules.
7. For each legally adopted operating budget, expenditures may not exceed budgeted appropriations at the activity level. The legal appropriation basis is at the level called "department". A "department" for legal appropriation purposes may be a single organization (e.g., City Attorney), or an entire department having multiple organizations within the same fund (e.g., Operations and Maintenance), or an entire fund (e.g., Downtown Improvement District). All departments and funds completed the year within their legally authorized expenditures. Encumbrance accounting, under which purchase orders, contracts and other commitments are recorded to reserve the applicable appropriations, is employed in the governmental funds.

The City does, however, honor the contracts represented by year-end encumbrances and the subsequent year's appropriations provide authority to complete these transactions.

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**COMBINING AND INDIVIDUAL FUND  
STATEMENTS AND SCHEDULES**



## Nonmajor Governmental Funds

### Nonmajor Special Revenue Funds

Special Revenue Funds include funds which are restricted as to use by the Federal or State governments, and special purpose funds established by authority of the City Council. Nonmajor Special Revenue Funds include:

**OPERATING GRANTS FUND** – To account for a variety of governmental fund operating grants, including law enforcement grants.

**LOCAL TRANSPORTATION FUND** – To account for revenues and expenditures of Local Transportation Fund allocations for streets, urban trails, and non-motorized facilities. Allocations for the City bus system are reported directly in the Bus Enterprise Fund.

**TRAFFIC SAFETY FUND** – To account for receipts and expenditures of traffic safety fines.

**DOWNTOWN IMPROVEMENT DISTRICT FUND** – To account for the fiscal activities of Business Improvement Area A of the City of Modesto.

**HOUSING AND COMMUNITY DEVELOPMENT FUND** – To account for grants and other monies received and disbursed for projects developed and administered under the Housing and Community Development Act of 1974.

**STRATEGIC PLANNING AND DEVELOPMENT FUND** – Established to provide a funding source for future village planning, general plan update and other large expenses related to planning and development. This fund was originally financed with an apportionment of the PERS rebate related to AB702. Subsequent funding has been provided by transfers from the General Fund. Future funding will be provided by fees imposed on private development.

### Nonmajor Capital Projects Funds

Capital Projects Funds are used to account for financial resources to be used for the acquisition or construction of major capital facilities other than those financed by proprietary funds. Nonmajor Capital Projects Funds include:

**SPECIAL FUND FOR CAPITAL OUTLAYS** – To account for capital outlay authorized by the City Council. No monies placed in this fund are to be disbursed except for this purpose unless authorized by a vote of the people.

**PARKS FUND** – To account for a discretionary transfer of General Fund property tax revenue to provide for the development of parks within the City, as directed by the City Council.

**McHENRY MANSION RESTORATION FUND** – To account for donations and other revenues received and appropriated for the purpose of restoring the McHenry Mansion.

**CAPITAL GRANTS FUND** – To account for receipts and disbursements of a variety of Governmental Fund capital grants.

**COMMUNITY FACILITIES DISTRICTS FUND** – To account for the construction of public improvements deemed to benefit properties against which special taxes are levied.

**REDEVELOPMENT AGENCY FUND** – To account for the construction of capital projects financed by the Redevelopment Agency of the City of Modesto.

**PUBLIC FINANCING AUTHORITY FUND** – To account for the financing of various projects authorized by the Modesto Public Financing Authority.

### **Nonmajor Debt Service Funds**

Debt Service Funds are used to account for the accumulation of resources for, and the payment of, general long-term debt principal and interest. Nonmajor Debt Service Funds include:

**REDEVELOPMENT AGENCY FUND** – To account for certificates of participation issued to finance the acquisitions and construction of the Modesto Centre Plaza.

**PUBLIC FINANCING AUTHORITY FUND** – To account for payment of debt issued to finance projects authorized by the Modesto Public Financing Authority.

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**CITY OF MODESTO**  
**COMBINING BALANCE SHEET - NONMAJOR GOVERNMENTAL FUNDS**  
**June 30, 2010**

	Special Revenue				
	Operating Grants	Local Transportation	Traffic Safety	Downtown Improvement District	Housing and Community Development
<u>ASSETS</u>					
Cash and cash equivalents	\$ 3,182,642	\$ 462,020	\$ 521,911	\$ 16,651	\$ 86,262
Cash and cash equivalents with fiscal agent					
Receivables:					
Accounts	371,070				9,729
Interest	5,027	813		23	2,861
Utilities, net	463,502				
Taxes					
Due from governments	1,770,362	317,451			3,105,224
Notes receivable, net	229,102				19,975,193
Property held for resale					
Restricted assets:					
Cash and cash equivalents					
Advances to other funds					
 Total assets	<u>\$ 6,021,705</u>	<u>\$ 780,284</u>	<u>\$ 521,911</u>	<u>\$ 16,674</u>	<u>\$ 23,179,269</u>
 <u>LIABILITIES AND FUND BALANCES</u>					
Liabilities:					
Accounts payable	\$ 1,126,145		\$ 22,807		\$ 85,655
Accrued salaries and benefits	148,666		8,959		27,510
Interest Payable					26,380
Due to other funds	232,374				1,584,036
Approved loans payable					300,041
Deferred revenues	199,443	\$ 777,395			
Refundable deposits					
Advances from other funds					
 Total liabilities	<u>1,706,628</u>	<u>777,395</u>	<u>31,766</u>	<u>16,674</u>	<u>2,023,622</u>
Fund balances:					
Reserved for:					
Encumbrances	1,645,084	1,510,376			45,278
Loan programs and prepaids					19,675,152
Property held for resale					
Set-aside requirement					
Debt service					
Unreserved/designated for:					
Pending projects			490,145	\$ 16,674	1,435,217
Unreserved/undesignated	2,669,993	(1,507,487)			
 Total fund balances	<u>4,315,077</u>	<u>2,889</u>	<u>490,145</u>	<u>16,674</u>	<u>21,155,647</u>
 Total liabilities and fund balances	<u>\$ 6,021,705</u>	<u>\$ 780,284</u>	<u>\$ 521,911</u>	<u>\$ 16,674</u>	<u>\$ 23,179,269</u>

Capital Projects						
Strategic Planning and Development	Special Fund for Capital Outlays	Parks	McHenry Mansion Restoration	Capital Grants	Community Facilities Districts	Redevelopment Agency
\$ 411,745	\$ (36,264)	\$ 14,591	\$ 7,387	\$ 811,077	\$ 15,501,307	\$ 2,052,068
		2,218,011			9,991,058	
695	1,847		13		31,296	1,991
		27,832		1,460,404		2,211,000
						784,000
					639,616	
						1,249,071
<u>\$ 412,440</u>	<u>\$ (34,417)</u>	<u>\$ 2,260,434</u>	<u>\$ 7,400</u>	<u>\$ 2,271,481</u>	<u>\$ 26,163,277</u>	<u>\$ 6,298,130</u>
	\$ 294	\$ 55,468		\$ 381,009	\$ 92,301	\$ 2,732
		1,238			7,046	
	2,400	705,948		687,665	4,321	174
		27,831		1,675,177		575,000
					639,616	1,000
						269,805
	2,694	790,485		2,743,851	743,284	848,711
\$ 145,822		19,592		2,038,298	613,818	9,253
						2,211,000
						784,000
						1,055,392
266,618	(37,111)	1,450,357	\$ 7,400	(2,510,668)	24,806,175	1,389,774
<u>412,440</u>	<u>(37,111)</u>	<u>1,469,949</u>	<u>7,400</u>	<u>(472,370)</u>	<u>25,419,993</u>	<u>5,449,419</u>
<u>\$ 412,440</u>	<u>\$ (34,417)</u>	<u>\$ 2,260,434</u>	<u>\$ 7,400</u>	<u>\$ 2,271,481</u>	<u>\$ 26,163,277</u>	<u>\$ 6,298,130</u>

**CITY OF MODESTO**  
**COMBINING BALANCE SHEET - NONMAJOR GOVERNMENTAL FUNDS (Continued)**  
**June 30, 2010**

	Debt Service		
	Redevelopment Agency	Public Financing Authority	Total
<u>ASSETS</u>			
Cash and cash equivalents	\$ 1,023,416	1,624	\$ 24,056,437
Cash and cash equivalents with fiscal agent	2,082,453	\$ 4,833,496	19,125,018
Receivables:			
Accounts			382,646
Interest	4,953		47,672
Utilities, net			463,502
Taxes	231,166		231,166
Due from governments			6,681,273
Notes receivable, net			22,415,295
Property held for resale			784,000
Restricted assets:			
Cash and cash equivalents			639,616
Advances to other funds			1,249,071
Total assets	<u>\$ 3,341,988</u>	<u>\$ 4,835,120</u>	<u>\$ 76,075,696</u>
<u>LIABILITIES AND FUND BALANCES</u>			
Liabilities:			
Accounts payable	\$ 706,241		\$ 2,472,652
Accrued salaries and benefits			192,181
Interest payable			32,113
Due to other funds		\$ 195,572	3,407,995
Approved loans payable			875,041
Deferred revenues			2,679,846
Refundable deposits			640,616
Advances from other funds	1,224,993		1,494,798
Total liabilities	<u>1,931,234</u>	<u>195,572</u>	<u>11,795,242</u>
Fund balances:			
Reserved for:			
Encumbrances			6,027,521
Loan programs			21,886,152
Property held for resale			784,000
Set-aside requirement			1,055,392
Debt service	1,410,754	4,639,548	6,050,302
Unreserved/designated for:			
Pending projects			5,056,185
Unreserved/undesignated			23,420,902
Total fund balances	<u>1,410,754</u>	<u>4,639,548</u>	<u>64,280,454</u>
Total liabilities and fund balances	<u>\$ 3,341,988</u>	<u>\$ 4,835,120</u>	<u>\$ 76,075,696</u>

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**CITY OF MODESTO**  
**COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES**  
**IN FUND BALANCES - NONMAJOR GOVERNMENTAL FUNDS**  
**Year ended June 30, 2010**

	Special Revenue				
	Operating Grants	Local Transportation	Traffic Safety	Downtown Improvement District	Housing and Community Development
REVENUES:					
Taxes				\$ 169,471	
Licenses and permits	\$ 54,214				
Intergovernmental	3,558,214	\$ 52,552			\$ 10,604,583
Charges for services	6,209,239		\$ 309,770		350,619
Special assessments levied	38,520				
Interest and rent	29,796	1,897		96	149,408
Net increase (decrease) in fair value of investments	15,369	2,889		127	166
Fines and forfeits	3,047		1,207,900		
Miscellaneous	441,259				13,067
Total revenues	<u>10,349,658</u>	<u>57,338</u>	<u>1,517,670</u>	<u>169,694</u>	<u>11,117,843</u>
EXPENDITURES:					
Current:					
General government	832,056				
Community development				198,924	8,416,074
Highways and streets		2,103			
Public works	3,511,292				
Parks and recreation	2,735,391				
Public safety	1,879,274		522,412		
Capital outlay:					
Community development					31,245
Highways and streets		24,309			
Public works	1,518,259				
Parks and recreation					
Public safety	15,372				
Debt service:					
Principal retirement					165,000
Interest					343,189
Other					
Total expenditures	<u>10,491,644</u>	<u>26,412</u>	<u>522,412</u>	<u>198,924</u>	<u>8,955,508</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>(141,986)</u>	<u>30,926</u>	<u>995,258</u>	<u>(29,230)</u>	<u>2,162,335</u>
OTHER FINANCING SOURCES (USES):					
Transfers in	1,035,890				
Transfers out	(266,069)	(28,037)	(742,000)		(501,785)
TOTAL OTHER FINANCING SOURCES (USES)	<u>769,821</u>	<u>(28,037)</u>	<u>(742,000)</u>		<u>(501,785)</u>
NET CHANGE IN FUND BALANCES	627,835	2,889	253,258	(29,230)	1,660,550
FUND BALANCES, July 1	3,687,242		236,887	45,904	19,525,097
PRIOR PERIOD ADJUSTMENT					(30,000)
FUND BALANCES, June 30	<u>\$ 4,315,077</u>	<u>\$ 2,889</u>	<u>\$ 490,145</u>	<u>\$ 16,674</u>	<u>\$ 21,155,647</u>

Strategic Planning and Development	Capital Projects					
	Special Fund for Capital Outlays	Parks	McHenry Mansion Restoration	Capital Grants	Community Facilities Districts	Redevelop- ment Agency
						\$ 1,569,236
	\$	16,000 15,802		\$ 4,494,148	\$ 292,225 469,142	
2,998	\$ (2,448)	(7,022)	\$ 41		225,253	35,834
2,344	(974)	(2,646)	72		51,440	17,308
<u>1,638</u>		<u>120,717</u>			<u>278,852</u>	<u>26,400</u>
<u>6,980</u>	<u>(3,422)</u>	<u>142,851</u>	<u>113</u>	<u>4,494,148</u>	<u>1,316,912</u>	<u>1,648,778</u>
61,146					2,108,935	512,351
				71,332		
		157,628				
						743,781
				5,741,542	385,760	
	193,200 76,426	523,685				
<u>61,146</u>	<u>269,626</u>	<u>681,313</u>		<u>5,812,874</u>	<u>2,494,695</u>	<u>1,256,132</u>
<u>(54,166)</u>	<u>(273,048)</u>	<u>(538,462)</u>	<u>113</u>	<u>(1,318,726)</u>	<u>(1,177,783)</u>	<u>392,646</u>
	129,863 59,046	(6,258)		970,992 (5,821)		170,000 (1,178,652)
	<u>188,909</u>	<u>(6,258)</u>		<u>965,171</u>		<u>(1,008,652)</u>
(54,166)	(84,139)	(544,720)	113	(353,555)	(1,177,783)	(616,006)
466,606	47,028	2,014,669	7,287	(148,815)	26,597,776	5,159,503
				30,000		905,922
<u>412,440</u>	<u>\$ (37,111)</u>	<u>\$ 1,469,949</u>	<u>\$ 7,400</u>	<u>\$ (472,370)</u>	<u>\$ 25,419,993</u>	<u>\$ 5,449,419</u>

**CITY OF MODESTO**  
**COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES**  
**IN FUND BALANCES - NONMAJOR GOVERNMENTAL FUNDS**  
**Year ended June 30, 2010**

	Debt Service		
	Redevelopment Agency	Public Financing Authority	Total
<b>REVENUES:</b>			
Taxes	\$ 4,952,279		\$ 6,690,986
Licenses and permits			54,214
Intergovernmental			19,017,722
Charges for services	171,118		7,525,690
Special assessments levied			38,520
Interest and rent	138,343	\$ 14,272	588,468
Net increase (decrease) in fair value of investments	(9,910)		76,185
Fines and forfeits			1,210,947
Miscellaneous			881,933
<b>Total revenues</b>	<b>5,251,830</b>	<b>14,272</b>	<b>36,084,665</b>
<b>EXPENDITURES:</b>			
<b>Current:</b>			
General government			832,056
Community development	2,092,697		13,390,127
Highways and streets			73,435
Public works			3,511,292
Parks and recreation			2,893,019
Public safety			2,401,686
<b>Capital outlay:</b>			
Community development			775,026
Highways and streets			6,151,611
Public works			1,518,259
Parks and recreation			716,885
Public safety			91,798
<b>Debt service:</b>			
Principal retirement	985,000	895,000	2,045,000
Interest	962,518	2,726,905	4,032,612
Other	1,402,171	6,600	1,408,771
<b>Total expenditures</b>	<b>5,442,386</b>	<b>3,628,505</b>	<b>39,841,577</b>
<b>EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES</b>	<b>(190,556)</b>	<b>(3,614,233)</b>	<b>(3,756,912)</b>
<b>OTHER FINANCING SOURCES (USES):</b>			
Transfers in	1,178,652	3,814,232	7,299,629
Transfers out	(1,199,843)		(3,869,419)
<b>TOTAL OTHER FINANCING SOURCES (USES)</b>	<b>(21,191)</b>	<b>3,814,232</b>	<b>3,430,210</b>
<b>NET CHANGE IN FUND BALANCES</b>	(211,747)	199,999	(326,702)
FUND BALANCES, July 1	2,528,423	4,439,549	64,607,156
PRIOR PERIOD ADJUSTMENT	(905,922)		
<b>FUND BALANCES, June 30</b>	<b>\$ 1,410,754</b>	<b>\$ 4,639,548</b>	<b>\$ 64,280,454</b>

**CITY OF MODESTO**  
**SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE -**  
**BUDGET (GAAP BASIS) AND ACTUAL - OPERATING GRANTS SPECIAL REVENUE FUND**  
**Year ended June 30, 2010**

	Budget		Actual	Variance with Final Budget - Positive (Negative)
	Original	Final		
<b>REVENUES:</b>				
Licenses and permits	\$ 60,000	\$ 60,000	\$ 54,214	\$ (5,786)
Intergovernmental	10,477,485	10,577,485	3,558,214	(7,019,271)
Charges for services	7,227,094	7,352,445	6,209,239	(1,143,206)
Special assessments	36,158	36,158	38,520	2,362
Interest and rent - interest			29,796	29,796
Net increase in fair value of investments			15,369	15,369
Fines and forfeits	1,500	1,500	3,047	1,547
Miscellaneous	417,761	417,761	441,259	23,498
<b>Total revenues</b>	<u>18,219,998</u>	<u>18,445,349</u>	<u>10,349,658</u>	<u>(8,095,691)</u>
<b>EXPENDITURES:</b>				
General government	929,075	936,590	832,056	104,534
Public works	5,305,084	5,339,111	5,029,551	309,560
Parks and recreation	3,633,030	3,919,723	2,735,391	1,184,332
Public safety	5,225,420	5,325,420	1,894,646	3,430,774
<b>Total expenditures</b>	<u>15,092,609</u>	<u>15,520,844</u>	<u>10,491,644</u>	<u>5,029,200</u>
<b>DEFICIENCY OF REVENUES (UNDER) EXPENDITURES</b>	<u>3,127,389</u>	<u>2,924,505</u>	<u>(141,986)</u>	<u>(3,066,491)</u>
<b>OTHER FINANCING SOURCES:</b>				
Transfers in	1,082,743	758,920	1,035,890	276,970
Transfers out	(249,936)	(249,936)	(266,069)	(16,133)
<b>TOTAL OTHER FINANCING SOURCES (USES)</b>	<u>832,807</u>	<u>508,984</u>	<u>769,821</u>	<u>260,837</u>
<b>NET CHANGE IN FUND BALANCE</b>	3,960,196	3,433,489	627,835	(2,805,654)
<b>FUND BALANCES, JULY 1</b>	<u>4,673,420</u>	<u>4,883,055</u>	<u>3,687,242</u>	<u>(1,195,813)</u>
<b>FUND BALANCES, JUNE 30</b>	<u>\$ 8,633,616</u>	<u>\$ 8,316,544</u>	<u>\$ 4,315,077</u>	<u>\$ (4,001,467)</u>

**CITY OF MODESTO**  
**SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE -**  
**BUDGET (GAAP BASIS) AND ACTUAL - LOCAL TRANSPORTATION SPECIAL REVENUE FUND**  
**Year ended June 30, 2010**

	Budget		Actual	Variance with Final Budget - Positive (Negative)
	Original	Final		
<b>REVENUES:</b>				
Intergovernmental	\$ 669,483	\$ 986,934	\$ 52,552	\$ (934,382)
Interest and rent - interest			1,897	1,897
Net increase in fair value of investments			2,889	2,889
Total revenues	<u>669,483</u>	<u>986,934</u>	<u>57,338</u>	<u>(929,596)</u>
<b>EXPENDITURES:</b>				
Highways and streets	<u>556,586</u>	<u>556,586</u>	<u>26,412</u>	<u>530,174</u>
Total expenditures	<u>556,586</u>	<u>556,586</u>	<u>26,412</u>	<u>530,174</u>
<b>EXCESS OF REVENUES OVER EXPENDITURES</b>	<u>112,897</u>	<u>430,348</u>	<u>30,926</u>	<u>(399,422)</u>
<b>OTHER FINANCING SOURCES (USES):</b>				
Transfers out			<u>(28,037)</u>	<u>(28,037)</u>
TOTAL OTHER FINANCING SOURCES (USES)			<u>(28,037)</u>	<u>(28,037)</u>
<b>NET CHANGE IN FUND BALANCE</b>	112,897	430,348	2,889	(427,459)
FUND BALANCES, JULY 1	<u>(2,323,373)</u>	<u>(678,941)</u>		<u>678,941</u>
FUND BALANCE (DEFICITS), JUNE 30	<u>\$ (2,210,476)</u>	<u>\$ (248,593)</u>	<u>\$ 2,889</u>	<u>\$ 251,482</u>

**CITY OF MODESTO**  
**SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE -**  
**BUDGET (GAAP BASIS) AND ACTUAL - TRAFFIC SAFETY SPECIAL REVENUE FUND**  
**Year ended June 30, 2010**

	Budget		Actual	Variance with Final Budget - Positive (Negative)
	Original	Final		
<b>REVENUES</b>				
Charges for services	\$ 475,959	\$ 475,959	\$ 309,770	\$ (166,189)
Motor vehicle fines	1,520,899	1,520,899	1,207,900	(312,999)
Total revenues	<u>1,996,858</u>	<u>1,996,858</u>	<u>1,517,670</u>	<u>(479,188)</u>
<b>EXPENDITURES:</b>				
Public safety	<u>725,000</u>	<u>1,072,730</u>	<u>522,412</u>	<u>550,318</u>
<b>EXCESS OF REVENUES OVER EXPENDITURES</b>	<u>1,271,858</u>	<u>924,128</u>	<u>995,258</u>	<u>(1,029,506)</u>
<b>OTHER FINANCING USES:</b>				
Transfers out	<u>(1,405,266)</u>	<u>(742,000)</u>	<u>(742,000)</u>	
<b>NET CHANGE IN FUND BALANCE</b>	(133,408)	182,128	253,258	71,130
<b>FUND BALANCES, JULY 1</b>	<u>14,931</u>	<u>183,620</u>	<u>236,887</u>	<u>53,267</u>
<b>FUND BALANCES, JUNE 30</b>	<u>\$ (118,477)</u>	<u>\$ 365,748</u>	<u>\$ 490,145</u>	<u>\$ 124,397</u>

**CITY OF MODESTO**  
**SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND**  
**BALANCE - BUDGET (GAAP BASIS) AND ACTUAL - DOWNTOWN**  
**IMPROVEMENT DISTRICT SPECIAL REVENUE FUND**  
**Year ended June 30, 2010**

	Budget		Actual	Variance with Final Budget - Positive (Negative)
	Original	Final		
<b>REVENUES:</b>				
Taxes - business license tax	\$ 210,000	\$ 210,000	\$ 169,471	\$ (40,529)
Interest and rent - interest	1,071	1,071	96	(975)
Net increase in fair value of investments			127	127
Total revenues	<u>211,071</u>	<u>211,071</u>	<u>169,694</u>	<u>(41,377)</u>
<b>EXPENDITURES - community development</b>				
Downtown improvement district administration:				
Professional and contractual services	176,142	176,142	181,042	(4,900)
Materials and supplies	6,530	6,530	3,413	3,117
Other	22,150	22,150	14,469	7,681
Total expenditures	<u>204,822</u>	<u>204,822</u>	<u>198,924</u>	<u>5,898</u>
<b>NET CHANGE IN FUND BALANCE</b>	6,249	6,249	(29,230)	(35,479)
<b>FUND BALANCES, JULY 1</b>	<u>39,392</u>	<u>39,392</u>	<u>45,904</u>	<u>6,512</u>
<b>FUND BALANCES, JUNE 30</b>	<u>\$ 45,641</u>	<u>\$ 45,641</u>	<u>\$ 16,674</u>	<u>\$ (28,967)</u>

**CITY OF MODESTO**  
**SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN**  
**FUND BALANCE - BUDGET (GAAP BASIS) AND ACTUAL - HOUSING**  
**AND COMMUNITY DEVELOPMENT SPECIAL REVENUE FUND**  
**Year ended June 30, 2010**

	Budget		Actual	Variance with Final Budget - Positive (Negative)
	Original	Final		
<b>REVENUES:</b>				
Intergovernmental - federal grants	\$ 14,223,561	\$ 15,036,494	\$ 10,604,583	\$ (4,431,911)
Charges for services	230,757	230,757	350,619	119,862
Interest and rent - interest	245,000	245,000	149,408	(95,592)
Net increase in fair value of investments			166	166
Miscellaneous			13,067	13,067
Total revenues	<u>14,699,318</u>	<u>15,512,251</u>	<u>11,117,843</u>	<u>(4,394,408)</u>
<b>EXPENDITURES</b>				
Community development	13,342,264	13,955,242	8,447,319	5,507,923
Debt service:				
Principal retirement	165,000	165,000	165,000	
Interest	211,876	211,876	343,189	(131,313)
Total expenditures	<u>13,719,140</u>	<u>14,332,118</u>	<u>8,955,508</u>	<u>5,376,610</u>
<b>EXCESS OF REVENUES OVER EXPENDITURES</b>	<u>980,178</u>	<u>1,180,133</u>	<u>2,162,335</u>	<u>982,202</u>
<b>OTHER FINANCING USES:</b>				
Transfers in		99,833		(99,833)
Transfers out	(160,000)	(560,000)	(501,785)	58,215
<b>TOTAL OTHER FINANCING SOURCES (USES)</b>	<u>(160,000)</u>	<u>(460,167)</u>	<u>(501,785)</u>	<u>(41,618)</u>
<b>NET CHANGE IN FUND BALANCE</b>	820,178	719,966	1,660,550	940,584
<b>FUND BALANCES, JULY 1</b>	16,191,898	16,540,985	19,525,097	2,984,112
<b>PRIOR PERIOD ADJUSTMENT</b>			(30,000)	(30,000)
<b>FUND BALANCES, JUNE 30</b>	<u>\$ 17,012,076</u>	<u>\$ 17,260,951</u>	<u>\$ 21,155,647</u>	<u>\$ 3,894,696</u>

**CITY OF MODESTO**  
**SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN**  
**FUND BALANCE - BUDGET (GAAP BASIS) AND ACTUAL - STRATEGIC**  
**PLANNING AND DEVELOPMENT SPECIAL REVENUE FUND**  
**Year ended June 30, 2010**

	Budget		Actual	Variance with Final Budget - Positive (Negative)
	Original	Final		
<b>REVENUES:</b>				
Charges for services	\$ 1,478,868	\$ 1,478,868	\$	\$ (1,478,868)
Interest and rent - interest			2,998	2,998
Net increase in fair value of investments			2,344	2,344
Miscellaneous			1,638	1,638
Total revenues	<u>1,478,868</u>	<u>1,478,868</u>	<u>6,980</u>	<u>(1,471,888)</u>
<b>EXPENDITURES:</b>				
Community development	1,402,140	1,402,140	61,146	1,340,994
Public works	9,168	27,398		27,398
Total expenditures	<u>1,411,308</u>	<u>1,429,538</u>	<u>61,146</u>	<u>1,368,392</u>
<b>EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES</b>	<u>67,560</u>	<u>49,330</u>	<u>(54,166)</u>	<u>(103,496)</u>
<b>NET CHANGE IN FUND BALANCE</b>	67,560	49,330	(54,166)	(103,496)
<b>FUND BALANCES, JULY 1</b>	<u>880,702</u>	<u>491,801</u>	<u>466,606</u>	<u>(25,195)</u>
<b>FUND BALANCES, JUNE 30</b>	<u>\$ 948,262</u>	<u>\$ 541,131</u>	<u>\$ 412,440</u>	<u>\$ (128,691)</u>

## Nonmajor Enterprise Funds

Enterprise Funds are established to account for activities that render services on a user-charge basis to the general public. Nonmajor Enterprise Funds include:

**PARKING FUND** – Revenues in this fund consist of charges for off-street parking and the downtown parking garage, as well as in-lieu parking fees. The revenue is used to develop and maintain parking facilities.

**STORM DRAIN FUND** – To account for storm drain improvements, operations and maintenance. The activities of the fund include street cleaning, rock well maintenance, and compliance with Federal and State water quality standards on storm water discharge.

**COMPOST FUND** – To account for tip fees charged at the City's composting facility for processing various compostable materials and the sale of compost product. Excess revenues over expenses are set aside to protect the enterprise against market fluctuations, and to provide for capital improvements to the facility infrastructure.

**AIRPORT FUND** – To account for all airport operations as stipulated in the City-Stanislaus County agreement of January 1968. Amounts received from the Federal government, State of California, and Stanislaus County, requiring matching amounts by the City, are recorded in this fund and are appropriated to finance approved capital projects.

**GOLF FUND** – Revenues in this fund consist of fees charged for using the City's golf courses. The revenue is used to improve, operate, and maintain golf courses.

**COMMUNITY CENTER FUND** – Accounted for in this fund are all amounts collected for the purpose of operating and maintaining the Modesto Centre Plaza Community Center. Revenues include room rental, catering fees, ticket sales, and other charges for using the center.

**CITY OF MODESTO**  
**COMBINING STATEMENT OF NET ASSETS - NON MAJOR ENTERPRISE FUNDS**  
**June 30, 2010**

	Parking	Storm Drain	Compost
<u>ASSETS</u>			
Current assets:			
Cash and cash equivalents	\$ 99,770	\$ 3,306,866	\$ 763,350
Cash and cash equivalents with fiscal agent			
Receivables:			
Accounts	7,842	636	83,177
Interest	287	6,204	1,256
Utilities, net		557,890	
Taxes			
Due from governments		6,723	
Property held for resale	630,000		
Total current assets	737,899	3,878,319	847,783
Capital assets:			
Land and construction in progress	3,142,479	2,042,940	
Other capital assets, net of accumulated depreciation	7,123,670	15,679,122	932,185
Total assets	11,004,048	21,600,381	1,779,968
<u>LIABILITIES</u>			
Current liabilities:			
Accounts payable	174,749	141,595	8,904
Accrued salaries and benefits	11,321	34,243	14,418
Interest payable			52
Due to other funds	73,373		
Due to other governments			
Current portion - long-term debt			
Deferred revenues			
Total current liabilities	259,443	175,838	23,374
Noncurrent liabilities:			
Obligations under capital leases			
Certificates of participation			
Advances from other funds		1,324,704	
Total liabilities	259,443	1,500,542	23,374
<u>NET ASSETS</u>			
Invested in capital assets, net of related debt	10,266,149	17,722,062	932,185
Unrestricted	478,456	2,377,777	824,409
Total net assets	\$ 10,744,605	\$ 20,099,839	\$ 1,756,594

<u>Airport</u>	<u>Golf</u>	<u>Community Center</u>	<u>Total</u>
\$ 1,343,839	\$ (8,872) 603,150	\$ 157,767	\$ 5,662,720 603,150
13,198	34,613	61,001	200,467
753		58	8,558
			557,890
18			18
214,985			221,708
			630,000
<u>1,572,793</u>	<u>628,891</u>	<u>218,826</u>	<u>7,884,511</u>
1,202,302	494,938	3,764,844	10,647,503
<u>8,791,781</u>	<u>2,065,608</u>	<u>8,664,615</u>	<u>43,256,981</u>
<u>11,566,876</u>	<u>3,189,437</u>	<u>12,648,285</u>	<u>61,788,995</u>
48,846	52,284	37,122	463,500
10,672		19,470	90,124
	43,787		43,839
	188,409		261,782
	250,000		250,000
1,943	204,505		206,448
<u>61,461</u>	<u>738,985</u>	<u>56,592</u>	<u>1,315,693</u>
	4,725,000		4,725,000
			1,324,704
<u>61,461</u>	<u>5,463,985</u>	<u>56,592</u>	<u>7,365,397</u>
9,994,083	(2,414,454)	12,429,459	48,929,484
<u>1,511,332</u>	<u>139,906</u>	<u>162,234</u>	<u>5,494,114</u>
<u>\$ 11,505,415</u>	<u>\$ (2,274,548)</u>	<u>\$ 12,591,693</u>	<u>\$ 54,423,598</u>

**CITY OF MODESTO**  
**COMBINING STATEMENT OF REVENUES, EXPENSES, AND**  
**CHANGES IN FUND NET ASSETS - NON MAJOR ENTERPRISE FUNDS**  
**Year ended June 30, 2010**

	<u>Parking</u>	<u>Storm Drain</u>	<u>Compost</u>
OPERATING REVENUES:			
Charges for services	\$ 1,229,871	\$ 5,365,759	\$ 1,706,189
Miscellaneous	10,124	62,532	
Total operating revenues	<u>1,239,995</u>	<u>5,428,291</u>	<u>1,706,189</u>
OPERATING EXPENSES:			
Salaries and wages	502,195	922,657	357,230
Contractual services	422,231	952,873	63,730
Utilities	131,096	23,357	10,423
Maintenance and supplies	90,859	668,848	472,300
Insurance	37,708	120,888	13,623
Employee benefits	88,320	484,339	163,894
Administration services	53,940	1,215,945	44,192
Allocated indirect administrative costs	64,603	11,329	59,119
Other	3,663	106,811	3,132
Depreciation	396,667	619,268	281,908
Total operating expenses	<u>1,791,282</u>	<u>5,126,315</u>	<u>1,469,551</u>
OPERATING INCOME (LOSS)	<u>(551,287)</u>	<u>301,976</u>	<u>236,638</u>
NONOPERATING REVENUES (EXPENSES)			
Operating grants			
Gain (Loss) on disposition of capital assets			
Operating grants		(1,669)	
Tax revenue			
Tax expense	(26,415)		
Interest income	3,918	38,933	6,110
Net increase in fair value of investments	3,164	17,203	2,856
Rental income			
Trustee fees			
Total nonoperating revenues (expenses)	<u>(19,333)</u>	<u>54,467</u>	<u>8,966</u>
INCOME (LOSS) BEFORE CAPITAL CONTRIBUTIONS AND TRANSFERS	(570,620)	356,443	245,604
Capital contributions		113,862	
Transfers in	(59,046)	700,293	
Transfers out		<u>(322,314)</u>	<u>(113,902)</u>
CHANGE IN NET ASSETS	(629,666)	848,284	131,702
NET ASSETS (DEFICIT), July 1	11,374,271	19,251,555	1,624,892
PRIOR PERIOD ADJUSTMENT			
NET ASSETS (DEFICIT), June 30	<u>\$ 10,744,605</u>	<u>\$ 20,099,839</u>	<u>\$ 1,756,594</u>

<u>Airport</u>	<u>Golf</u>	<u>Community Center</u>	<u>Total</u>
\$ 669,964	\$ 1,923,231	\$ 483,313	\$ 11,378,327
5,601	784	6,249	85,290
<u>675,565</u>	<u>1,924,015</u>	<u>489,562</u>	<u>11,463,617</u>
275,716		667,353	2,725,151
31,119	1,747,442	69,067	3,286,462
114,322	17,176	202,842	499,216
262,911	59,909	313,022	1,867,849
31,803	13,734	62,656	280,412
135,232		245,000	1,116,785
140,627	43,339	7,918	1,505,961
71,346	13,847		220,244
32,686	1,119	7,144	154,555
810,924	310,227	761,478	3,180,472
<u>1,906,686</u>	<u>2,206,793</u>	<u>2,336,480</u>	<u>14,837,107</u>
<u>(1,231,121)</u>	<u>(282,778)</u>	<u>(1,846,918)</u>	<u>(3,373,490)</u>
			(1,669)
265,587			265,587
(418)	(263,553)		(290,386)
12,250	(4,959)	(868)	55,384
6,893	(2,533)	(375)	27,208
166,672	90,431	419,454	676,557
	(2,800)		(2,800)
<u>450,984</u>	<u>(183,414)</u>	<u>418,211</u>	<u>729,881</u>
(780,137)	(466,192)	(1,428,707)	(2,643,609)
599,938			713,800
	270,000	264,034	1,175,281
			(436,216)
(180,199)	(196,192)	(1,164,673)	(1,190,744)
11,685,614	(2,073,356)	13,756,366	55,619,342
	(5,000)		(5,000)
<u>\$ 11,505,415</u>	<u>\$ (2,274,548)</u>	<u>\$ 12,591,693</u>	<u>\$ 54,423,598</u>

**CITY OF MODESTO**  
**COMBINING STATEMENT OF CASH FLOWS - NONMAJOR ENTERPRISE FUNDS**  
Year ended June 30, 2010

	Parking	Storm Drain	Compost
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Receipts from customers and users	\$ 1,239,711	\$ 5,416,437	\$ 1,758,525
Receipts from interfund services provided		1,839	
Payments to suppliers	(426,292)	2,546,856	4,275,619
Payments to employees	(590,323)	(1,410,537)	(516,061)
Payments for interfund services used	(207,940)	(5,542,397)	(4,961,767)
Net cash provided (used) by operating activities	15,156	1,012,198	556,316
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>			
Operating grants received		(1,669)	
Taxes received			
Transfers in	(59,046)	700,293	
Transfers out		(322,314)	(113,902)
Net cash provided (used) by noncapital financing activities	(59,046)	376,310	(113,902)
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>			
Acquisition and construction of capital assets	(673,319)	(2,752)	
Principal repayments			
Interest paid			53
Trustee fees			
Capital grants received		12,430	
Net cash used by capital and related financing activities	(673,319)	9,678	53
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Interest received	6,424	35,014	5,756
Net increase in the fair value of investments	3,164	17,203	2,856
Net cash provided by investing activities	9,588	52,217	8,612
Net increase (decrease) in cash and cash equivalents	(707,621)	1,450,403	451,079
CASH AND CASH EQUIVALENTS, JULY 1	807,391	1,856,463	312,271
PRIOR PERIOD ADJUSTMENT			
CASH AND CASH EQUIVALENTS, JUNE 30	\$ 99,770	\$ 3,306,866	\$ 763,350
<b>RECONCILIATION TO STATEMENT OF NET ASSETS:</b>			
Cash and cash equivalents	\$ 99,770	\$ 3,306,866	\$ 763,350
Cash and cash equivalents with fiscal agent			
TOTAL CASH AND CASH EQUIVALENTS	\$ 99,770	\$ 3,306,866	\$ 763,350

<u>Airport</u>	<u>Golf</u>	<u>Community Center</u>	<u>Total</u>
\$ 856,169	\$ 2,014,894	\$ 877,507	\$ 12,163,243
(1,089,944)	(2,118,475)	(521,881)	1,839
(409,806)		(909,632)	2,665,883
282,523	74,017	(151,895)	(3,836,359)
<u>(361,058)</u>	<u>(29,564)</u>	<u>(705,901)</u>	<u>(10,507,459)</u>
			487,147
			(1,669)
265,587			265,587
	270,000	264,034	1,175,281
			<u>(436,216)</u>
<u>265,587</u>	<u>270,000</u>	<u>264,034</u>	<u>1,002,983</u>
(240,495)			(916,566)
	(235,000)		(235,000)
	939		992
	(2,800)		(2,800)
<u>49,375</u>			<u>61,805</u>
<u>(191,120)</u>	<u>(236,861)</u>		<u>(1,091,569)</u>
17,474	(4,958)	(713)	58,997
<u>6,893</u>	<u>(2,533)</u>	<u>(375)</u>	<u>27,208</u>
<u>24,367</u>	<u>(7,491)</u>	<u>(1,088)</u>	<u>86,205</u>
(262,224)	(3,916)	(442,955)	484,766
1,606,063	603,194	600,722	5,786,104
	(5,000)		(5,000)
<u>\$ 1,343,839</u>	<u>\$ 594,278</u>	<u>\$ 157,767</u>	<u>\$ 6,265,870</u>
\$ 1,343,839	\$ (8,872)	\$ 157,767	\$ 5,662,720
	603,150		603,150
<u>\$ 1,343,839</u>	<u>\$ 594,278</u>	<u>\$ 157,767</u>	<u>\$ 6,265,870</u>

(continued)

**CITY OF MODESTO**  
**COMBINING STATEMENT OF CASH FLOWS - NON MAJOR ENTERPRISE FUNDS (Continued)**  
Year ended June 30, 2010

	Parking	Storm Drain	Compost
<b>RECONCILIATION OF OPERATING INCOME (LOSS)</b>			
<b>TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:</b>			
Operating income (loss)	\$ (551,287)	\$ 301,976	\$ 236,638
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:			
Depreciation	396,667	619,268	281,908
Rental income			
Taxes paid	(26,415)		
Change in assets and liabilities:			
(Increase) decrease in accounts receivable	(284)	2,825	52,336
(Increase) in utilities receivable		(12,840)	
Increase (decrease) in accounts payable and accrued expenses	144,250	104,510	(19,093)
Increase in accrued salaries and benefits	192	(3,541)	5,063
Increase (decrease) in due to other funds	73,373		
Increase (decrease) in due to other governments	(21,340)		(536)
Increase (decrease) in deferred revenues			
Total adjustments	566,443	710,222	319,678
Net cash provided (used) by operating activities	\$ 15,156	\$ 1,012,198	\$ 556,316
 <b>NONCASH INVESTING, CAPITAL AND FINANCING</b>			
<b>ACTIVITIES:</b>			
Capital assets transferred from other funds		\$ 113,862	

<u>Airport</u>	<u>Golf</u>	<u>Community Center</u>	<u>Total</u>
\$ <u>(1,231,121)</u>	\$ <u>(282,778)</u>	\$ <u>(1,846,918)</u>	\$ <u>(3,373,490)</u>
810,924	310,227	761,478	3,180,472
166,672	90,431	419,454	676,557
(418)	(263,553)		(290,386)
11,989	1,374	(31,509)	36,731
			(12,840)
(121,667)	48,360	(11,127)	145,233
1,142		2,721	5,577
	67,301		140,674
(522)			(22,398)
<u>1,943</u>	<u>(926)</u>		<u>1,017</u>
<u>870,063</u>	<u>253,214</u>	<u>1,141,017</u>	<u>3,860,637</u>
\$ <u><u>(361,058)</u></u>	\$ <u><u>(29,564)</u></u>	\$ <u><u>(705,901)</u></u>	\$ <u><u>487,147</u></u>

\$ 599,938

## Internal Service Funds

Internal Service Funds are established to finance and account for services and commodities furnished by a designated agency of a governmental unit to other departments of the same governmental unit. Since the services and commodities are supplied exclusively to other departments of a governmental jurisdiction, they are distinguishable from those public services which are rendered to the public in general and which are accounted for in General, Special Revenue, or Enterprise Funds. Internal Service Funds include:

**FLEET MANAGEMENT FUND** – To provide the maintenance necessary for the City's equipment pool, which serves the needs of all City departments.

**CENTRAL SERVICES FUND** – To provide office supplies, various maintenance and construction materials, records storage, and mail services to all City departments.

**INFORMATION AND TECHNOLOGY SERVICES FUND** – To finance and account for the replacement, upgrade and maintenance of the City's network and technology infrastructure, and to develop and implement a coordinated City-wide information technology plan.

**INSURANCE FUND** – To finance and account for the City's insurance and risk management programs.

**EMPLOYEE BENEFITS MANAGEMENT FUND** – To account for all compensated absences and other employee benefits. Insurance benefits for current employees are accounted for in the Insurance Fund.

**BUILDING SERVICES FUND** – To account for the true cost of occupying and maintaining office space, to better reflect the value of that space, and to accumulate amounts for future building repair costs.

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**CITY OF MODESTO**  
**COMBINING STATEMENT OF NET ASSETS - INTERNAL SERVICE FUNDS**  
**June 30, 2010**

	Fleet Management	Central Services	Information & Technology Services
<u>ASSETS</u>			
Current assets:			
Cash and cash equivalents	\$ 9,865,815	\$ 1,003,921	\$ 4,742,907
Receivables:			
Accounts receivable	1,550		
Interest	17,423	1,780	8,444
Inventories		482,315	
Due from governments			142,462
Prepaid expenses			189,000
Due from other funds			
Total current assets	9,884,788	1,488,016	5,082,813
Noncurrent assets:			
Notes receivable, net			
Land and construction in progress	533,015		1,043,109
Other capital assets, net of accumulated depreciation	13,408,732	78,658	2,691,641
Total assets	23,826,535	1,566,674	8,817,563
<u>LIABILITIES</u>			
Current liabilities:			
Accounts payable	68,922	86,600	910,889
Accrued salaries and benefits	47,191	7,805	75,192
Interest Payable			
Current portion - compensated absences			
Current portion - claims liability			
Current portion - capital lease			187,135
Current portion - long-term debt	33,778		
Total current liabilities	149,891	94,405	1,173,216
Noncurrent liabilities:			
Compensated absences			
Claims liability			
Net OPEB obligation			
Long-term debt:			
Notes payable	20,658		
Obligations under capital leases			705,974
Total liabilities	170,549	94,405	1,879,190
<u>NET ASSETS</u>			
Invested in capital assets, net of related debt	13,907,969	78,658	3,028,776
Unrestricted	9,748,017	1,393,611	3,909,597
Total net assets	\$ 23,655,986	\$ 1,472,269	\$ 6,938,373

<u>Insurance</u>	<u>Employee Benefits Management</u>	<u>Building Services</u>	<u>Total</u>
\$ 18,848,205	\$ 17,200,599	\$ 181,959	\$ 51,843,406
208,989	18,472		229,011
19,734	31,890	384	79,655
			482,315
			142,462
			189,000
<u>19,076,928</u>	<u>17,250,961</u>	<u>182,343</u>	<u>52,965,849</u>
			1,576,124
	<u>1,637</u>	<u>112,996</u>	<u>16,293,664</u>
<u>19,076,928</u>	<u>17,252,598</u>	<u>295,339</u>	<u>70,835,637</u>
110,566	17,879	41,980	1,236,836
13,822	3,701	17,299	165,010
3,138	446		3,584
	4,808,016		4,808,016
4,880,570			4,880,570
			187,135
			33,778
<u>5,008,096</u>	<u>4,830,042</u>	<u>59,279</u>	<u>11,314,929</u>
	6,931,285		6,931,285
16,390,335			16,390,335
	45,527,073		45,527,073
			20,658
			<u>705,974</u>
<u>21,398,431</u>	<u>57,288,400</u>	<u>59,279</u>	<u>80,890,254</u>
	1,637	112,996	17,130,036
<u>(2,321,503)</u>	<u>(40,037,439)</u>	<u>123,064</u>	<u>(27,184,653)</u>
\$ <u><u>(2,321,503)</u></u>	\$ <u><u>(40,035,802)</u></u>	\$ <u><u>236,060</u></u>	\$ <u><u>(10,054,617)</u></u>

**CITY OF MODESTO**  
**COMBINING STATEMENT OF REVENUES, EXPENSES, AND CHANGES**  
**IN FUND NET ASSETS - INTERNAL SERVICE FUNDS**  
Year ended June 30, 2010

	Fleet Management	Central Services	Information & Technology Services
<b>OPERATING REVENUES:</b>			
Charges for services	\$ 6,369,042	\$ 35,618	\$ 6,440,645
Sales		4,289,240	
Cost of sales		(3,733,953)	
Total operating revenues	<u>6,369,042</u>	<u>590,905</u>	<u>6,440,645</u>
<b>OPERATING EXPENSES:</b>			
Salaries and wages	1,025,718	218,619	1,972,207
Contractual services	577,712	81,137	245,465
Utilities	8,155	1,033	208,661
Maintenance and supplies	2,428,611	42,729	1,257,050
Insurance	87,830	10,086	84,826
Claims expense			
Employee benefits	513,181	107,377	750,616
Administration services	190,759	10,200	105
Allocated indirect administrative costs	308,280		
Other	12,152	507	16,517
Depreciation	2,856,159	9,415	531,431
Total operating expenses	<u>8,008,557</u>	<u>481,103</u>	<u>5,066,878</u>
<b>OPERATING INCOME (LOSS)</b>	<u>(1,639,515)</u>	<u>109,802</u>	<u>1,373,767</u>
<b>NONOPERATING REVENUES (EXPENSES)</b>			
Operating grant			142,462
Loss on disposition of capital assets	(375,994)	(2,001)	(18,907)
Interest income	89,665	8,460	45,083
Net increase (decrease) in fair value of investments	48,680	4,401	23,945
Interest expense	(4,311)		(4,284)
Total nonoperating revenues (expenses)	<u>(241,960)</u>	<u>10,860</u>	<u>188,299</u>
<b>INCOME (LOSS) BEFORE CAPITAL CONTRIBUTIONS AND TRANSFERS</b>	<u>(1,881,475)</u>	<u>120,662</u>	<u>1,562,066</u>
Capital contributions			6,566
Transfers in	1,414,206		
Transfers out	(294,518)	(77,000)	(492,103)
<b>CHANGE IN NET ASSETS</b>	<u>(761,787)</u>	<u>43,662</u>	<u>1,076,529</u>
<b>NET ASSETS (DEFICITS), July 1, (as restated)</b>	<u>24,451,315</u>	<u>1,428,607</u>	<u>5,861,844</u>
<b>PRIOR PERIOD ADJUSTMENTS</b>	<u>(33,542)</u>		
<b>NET ASSETS (DEFICITS), June 30</b>	<u>\$ 23,655,986</u>	<u>\$ 1,472,269</u>	<u>\$ 6,938,373</u>

<u>Insurance</u>	<u>Employee Benefits Management</u>	<u>Building Services</u>	<u>Total</u>
\$ 24,468,686	\$ 2,953,289	\$ 1,801,831	\$ 42,069,111
			4,289,240
			(3,733,953)
<u>24,468,686</u>	<u>2,953,289</u>	<u>1,801,831</u>	<u>42,624,398</u>
380,716	90,951	392,925	4,081,136
61,534	277,281	582,935	1,826,064
1,383		218,505	437,737
8,452	9,439	191,917	3,938,198
14,919,158	3,365	37,265	15,142,530
6,541,335			6,541,335
156,714	7,794,596	210,299	9,532,783
1,448,533	52,937	25,883	1,728,417
			308,280
13,120	12,201	449	54,946
5,921	1,025	4,773	3,408,724
<u>23,536,866</u>	<u>8,241,795</u>	<u>1,664,951</u>	<u>47,000,150</u>
<u>931,820</u>	<u>(5,288,506)</u>	<u>136,880</u>	<u>(4,375,752)</u>
			142,462
			(396,902)
324,800	165,945	41,008	674,961
109,355	98,948	1,012	286,341
			(8,595)
<u>434,155</u>	<u>264,893</u>	<u>42,020</u>	<u>698,267</u>
1,365,975	(5,023,613)	178,900	(3,677,485)
			6,566
			1,414,206
		(91,591)	(955,212)
<u>1,365,975</u>	<u>(5,023,613)</u>	<u>87,309</u>	<u>(3,211,925)</u>
(3,687,478)	(35,012,189)	148,751	(6,809,150)
			(33,542)
<u>\$ (2,321,503)</u>	<u>\$ (40,035,802)</u>	<u>\$ 236,060</u>	<u>\$ (10,054,617)</u>

**CITY OF MODESTO**  
**COMBINING STATEMENT OF CASH FLOWS - INTERNAL SERVICE FUNDS**  
**Year ended June 30, 2010**

	<u>Fleet Management</u>	<u>Central Services</u>	<u>Information &amp; Technology Services</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Receipts from customers and users	\$ 192,495	\$ 15,144	\$ (54,816)
Receipts from interfund services provided	6,183,389	575,760	6,352,999
Payments to suppliers	(2,891,105)	(165,373)	(1,047,352)
Payment of insurance claims			
Payments to employees	(1,526,745)	(326,734)	(2,708,057)
Payments for interfund services used	(775,886)	(80,680)	(86,226)
Net cash provided (used) by operating activities	<u>1,182,148</u>	<u>18,117</u>	<u>2,456,548</u>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>			
Transfers in	1,414,206		
Transfers out	(294,518)	(77,000)	(492,103)
Due from other funds	101,576		
Operating grants received			142,462
Net cash provided (used) by noncapital financing activities	<u>1,221,264</u>	<u>(77,000)</u>	<u>(349,641)</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>			
Acquisition and construction of capital assets	(1,399,903)	(30,362)	(1,693,630)
Proceeds from sale of capital assets	(375,994)	(2,001)	(18,907)
Principal repayments	(31,816)		822,393
Interest paid	(4,311)		(4,284)
Net cash used by capital and related financing activities	<u>(1,812,024)</u>	<u>(32,363)</u>	<u>(894,428)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Interest received	101,393	9,095	48,942
Net increase in the fair value of investments	48,680	4,401	23,945
Net cash provided by investing activities	<u>150,073</u>	<u>13,496</u>	<u>72,887</u>
Net increase (decrease) in cash and cash equivalents	741,461	(77,750)	1,285,366
PRIOR PERIOD ADJUSTMENTS	(33,542)		
CASH AND CASH EQUIVALENTS, JULY 1	<u>9,157,896</u>	<u>1,081,671</u>	<u>3,457,541</u>
CASH AND CASH EQUIVALENTS, JUNE 30	<u>\$ 9,865,815</u>	<u>\$ 1,003,921</u>	<u>\$ 4,742,907</u>

<u>Insurance</u>	<u>Employee Benefits Management</u>	<u>Building Services</u>	<u>Total</u>
\$ (719,891)	\$ 2,825,011	\$ (320,897)	\$ 1,937,046
25,090,373	109,806	2,122,728	40,435,055
(15,583,186)	(953,816)	(928,133)	(21,568,965)
(6,695,983)			(6,695,983)
(536,373)	(3,430,169)	(597,804)	(9,125,882)
(1,489,335)	(71,490)	(156,201)	(2,659,818)
<u>65,605</u>	<u>(1,520,658)</u>	<u>119,693</u>	<u>2,321,453</u>
			1,414,206
		(91,591)	(955,212)
			101,576
<u>3,138</u>	<u>446</u>		<u>146,046</u>
<u>3,138</u>	<u>446</u>	<u>(91,591)</u>	<u>706,616</u>
			(3,123,895)
			(396,902)
			790,577
			<u>(8,595)</u>
			<u>(2,738,815)</u>
330,422	203,241	41,244	734,337
109,355	98,948	1,012	286,341
<u>439,777</u>	<u>302,189</u>	<u>42,256</u>	<u>1,020,678</u>
508,520	(1,218,023)	70,358	1,309,932
			(33,542)
<u>18,339,685</u>	<u>18,418,622</u>	<u>111,601</u>	<u>50,567,016</u>
\$ <u><u>18,848,205</u></u>	\$ <u><u>17,200,599</u></u>	\$ <u><u>181,959</u></u>	\$ <u><u>51,843,406</u></u>

(continued)

**CITY OF MODESTO**  
**COMBINING STATEMENT OF CASH FLOWS - INTERNAL SERVICE FUNDS (Continued)**  
**Year ended June 30, 2010**

	<u>Fleet Management</u>	<u>Central Services</u>	<u>Information &amp; Technology Services</u>
<b>RECONCILIATION OF OPERATING INCOME (LOSS) TO</b>			
<b>NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:</b>			
Operating income (loss)	\$ (1,639,515)	\$ 109,802	\$ 1,373,767
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:			
Depreciation	2,856,159	9,414	531,431
Change in assets and liabilities:			
(Increase) decrease in accounts receivable	6,842		
(Increase) decrease in due from governments			(142,462)
(Increase) in prepaid expenses			(189,000)
Decrease in inventories		429,747	
Increase (decrease) in accounts payable and accrued expenses	(53,492)	(530,108)	868,046
Increase in accrued salaries and benefits payable	12,154	(738)	14,766
Increase in compensated absences and OPEB			
Decrease in claims liability			
Total adjustments	<u>2,821,663</u>	<u>(91,685)</u>	<u>1,082,781</u>
Net cash provided (used) by operating activities	<u>\$ 1,182,148</u>	<u>\$ 18,117</u>	<u>\$ 2,456,548</u>
 <b>NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES:</b>			
Capital contributions			\$ 6,566
New capital lease transaction			

<u>Insurance</u>	<u>Employee Benefits Management</u>	<u>Building Services</u>	<u>Total</u>
\$ <u>931,820</u>	\$ <u>(5,288,506)</u>	\$ <u>136,880</u>	\$ <u>(4,375,752)</u>
5,921	1,025	4,773	3,408,723
(98,204)	(18,472)		(109,834)
			(142,462)
			(189,000)
			429,747
(620,341)	(670,082)	(27,380)	(1,033,357)
1,057	884	5,420	33,543
	4,454,493		4,454,493
<u>(154,648)</u>			<u>(154,648)</u>
<u>(866,215)</u>	<u>3,767,848</u>	<u>(17,187)</u>	<u>6,697,205</u>
\$ <u><u>65,605</u></u>	\$ <u><u>(1,520,658)</u></u>	\$ <u><u>119,693</u></u>	\$ <u><u>2,321,453</u></u>
			\$ 6,566

## AGENCY FUNDS

Agency Funds account for assets held by the City as an agent for individuals, governmental entities and non-public organizations.

**Special Districts** – To account for collection of special district assessments from property owners and forwarding these collections to trustees for payment to bondholders.

**Tuolumne River Regional Park** – To account for cash and investments of the Tuolumne River Regional Park, a joint powers agency between the City of Modesto, Stanislaus County and City of Ceres. The agency provides financing, development, and maintenance of the Tuolumne River Regional Park facilities. The cash and investments of the Park are invested as part of the City's investment pool.

**City-County Capital Improvements and Financing Agency** - To account for cash and investments of the City-County Capital Improvements and Financing Agency, a joint powers agency between the City of Modesto and Stanislaus County. The agency built and maintains a joint City-County government complex in downtown Modesto. The cash and investments of the Agency are invested as part of the City's investment pool.

**Stanislaus Drug Enforcement Agency** - To account for cash and investments of the Stanislaus Drug Enforcement Agency, a joint powers agency between Stanislaus County and the cities of Modesto, Oakdale, Turlock, Ceres, Hughson, Newman, Patterson, and Waterford. The agency's purpose is to maintain a specially trained police unit to assist each of the participating agencies in the enforcement of drug control laws, and to study, plan, and set priorities for effective enforcement of such laws throughout Stanislaus County. Cash and investments of the Agency are invested in the City's investment pool.

**Ceres-Modesto Fire Protection Agency** - To record and distribute the special assessments for fire protection that were established under the Industrial Fire District. This is a joint powers agency between the City of Modesto, the City of Ceres, and the Industrial Fire District. Cash and investments of the Agency are invested in the City's investment pool.

**CITY OF MODESTO**  
**STATEMENT OF CHANGES IN ASSETS AND LIABILITIES AGENCY FUNDS**  
Year ended June 30, 2010

	Balance June 30, 2009	Additions	Deletions	Balance June 30, 2010
<hr/> <u>Special Districts</u> <hr/>				
<u>ASSETS</u>				
Cash and cash equivalents	\$ 4,057,360	\$ 2,389,806	\$ 2,325,290	\$ 4,121,876
Cash and cash equivalents with fiscal agent	3,896,016	1,992,583	1,964,163	3,924,436
	<u>\$ 7,953,376</u>	<u>\$ 4,382,389</u>	<u>\$ 4,289,453</u>	<u>\$ 8,046,312</u>
 <u>LIABILITIES</u>				
Due to special district bondholders	\$ 7,953,376	\$ 4,382,389	\$ 4,289,453	\$ 8,046,312
	<u>\$ 7,953,376</u>	<u>\$ 4,382,389</u>	<u>\$ 4,289,453</u>	<u>\$ 8,046,312</u>
<hr/> <u>Tuolumne River Regional Park</u> <hr/>				
<u>ASSETS</u>				
Cash and cash equivalents	\$ (3)	\$ 2,304,493	\$ 1,909,780	\$ 394,710
	<u>\$ (3)</u>	<u>\$ 2,304,493</u>	<u>\$ 1,909,780</u>	<u>\$ 394,710</u>
 <u>LIABILITIES</u>				
Deposits held as agent for others	\$ (3)	\$ 2,304,493	\$ 1,909,780	\$ 394,710
	<u>\$ (3)</u>	<u>\$ 2,304,493</u>	<u>\$ 1,909,780</u>	<u>\$ 394,710</u>
<hr/> <u>City/County Joint Powers Financing Authority</u> <hr/>				
<u>ASSETS</u>				
Cash and cash equivalents	\$ 269,059	\$ 2,057,813	\$ 2,118,581	\$ 208,291
	<u>\$ 269,059</u>	<u>\$ 2,057,813</u>	<u>\$ 2,118,581</u>	<u>\$ 208,291</u>
 <u>LIABILITIES</u>				
Deposits held as agent for others	\$ 269,059	\$ 2,057,813	\$ 2,118,581	\$ 208,291
	<u>\$ 269,059</u>	<u>\$ 2,057,813</u>	<u>\$ 2,118,581</u>	<u>\$ 208,291</u>
<hr/> <u>Stanislaus Drug Enforcement Agency</u> <hr/>				
<u>ASSETS</u>				
Cash and cash equivalents	\$ 2,569,440	\$ 3,623,932	\$ 2,496,119	\$ 3,697,253
	<u>\$ 2,569,440</u>	<u>\$ 3,623,932</u>	<u>\$ 2,496,119</u>	<u>\$ 3,697,253</u>
 <u>LIABILITIES</u>				
Deposits held as agent for others	\$ 2,569,440	\$ 3,623,932	\$ 2,496,119	\$ 3,697,253
	<u>\$ 2,569,440</u>	<u>\$ 3,623,932</u>	<u>\$ 2,496,119</u>	<u>\$ 3,697,253</u>
<hr/> <u>Industrial Fire District</u> <hr/>				
<u>ASSETS</u>				
Cash and cash equivalents	\$ 236,564	\$ 493,141	\$ 296,186	\$ 433,519
	<u>\$ 236,564</u>	<u>\$ 493,141</u>	<u>\$ 296,186</u>	<u>\$ 433,519</u>
 <u>LIABILITIES</u>				
Deposits held as agent for others	\$ 236,564	\$ 493,141	\$ 296,186	\$ 433,519
	<u>\$ 236,564</u>	<u>\$ 493,141</u>	<u>\$ 296,186</u>	<u>\$ 433,519</u>
<hr/> <u>Totals - All Agency Funds</u> <hr/>				
<u>ASSETS</u>				
Cash and cash equivalents	\$ 7,132,420	\$ 10,869,185	\$ 9,145,956	\$ 8,855,649
Cash and cash equivalents with fiscal agent	3,896,016	1,992,583	1,964,163	3,924,436
	<u>\$ 11,028,436</u>	<u>\$ 12,861,768</u>	<u>\$ 11,110,119</u>	<u>\$ 12,780,085</u>
 <u>LIABILITIES</u>				
Due to special district bondholders	\$ 7,953,376	\$ 4,382,389	\$ 4,289,453	\$ 8,046,312
Deposits held as agent for others	3,075,060	8,479,379	6,820,666	4,733,773
	<u>\$ 11,028,436</u>	<u>\$ 12,861,768</u>	<u>\$ 11,110,119</u>	<u>\$ 12,780,085</u>

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## **STATISTICAL SECTION**



## Statistical Section

This part of the Comprehensive Annual Financial Report presents detailed information to aid in understanding what the information in the financial statements, note disclosures, and required supplementary information says about the City's overall financial health. In contrast to the financial section, the statistical section information is not subject to independent audit.

### Financial Trends

These schedules contain trend information to help the reader understand how the City's financial performance has changed over time.

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

### Revenue Capacity

This schedule gives information on the City's most significant local revenue source, the water user charges:

1. Water Utility System – Ten Largest Customers
2. Water revenues by customer class
3. Water rates

### Debt Capacity

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

1. Ratio of Outstanding Debt by Type
2. Computation of Direct and Overlapping Debt
3. Computation of Legal Bonded Debt Margin
4. Bonded Debt Pledged Revenue Coverage, Wastewater Revenue Bonds
5. Continuing Disclosure Requirements:
  - a. Wastewater Revenue Bonds and Refunding Revenue Bonds
  - b. Water Utility System Revenue Certificates of Participation and Refunding Revenue Certificates of Participation, and Modesto Irrigation District Financing Authority Domestic Water Project Revenue Bonds and Refunding Revenue Bonds

### Demographic and Economic Information

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

1. Demographic and Economic Statistics
2. Principal Employers

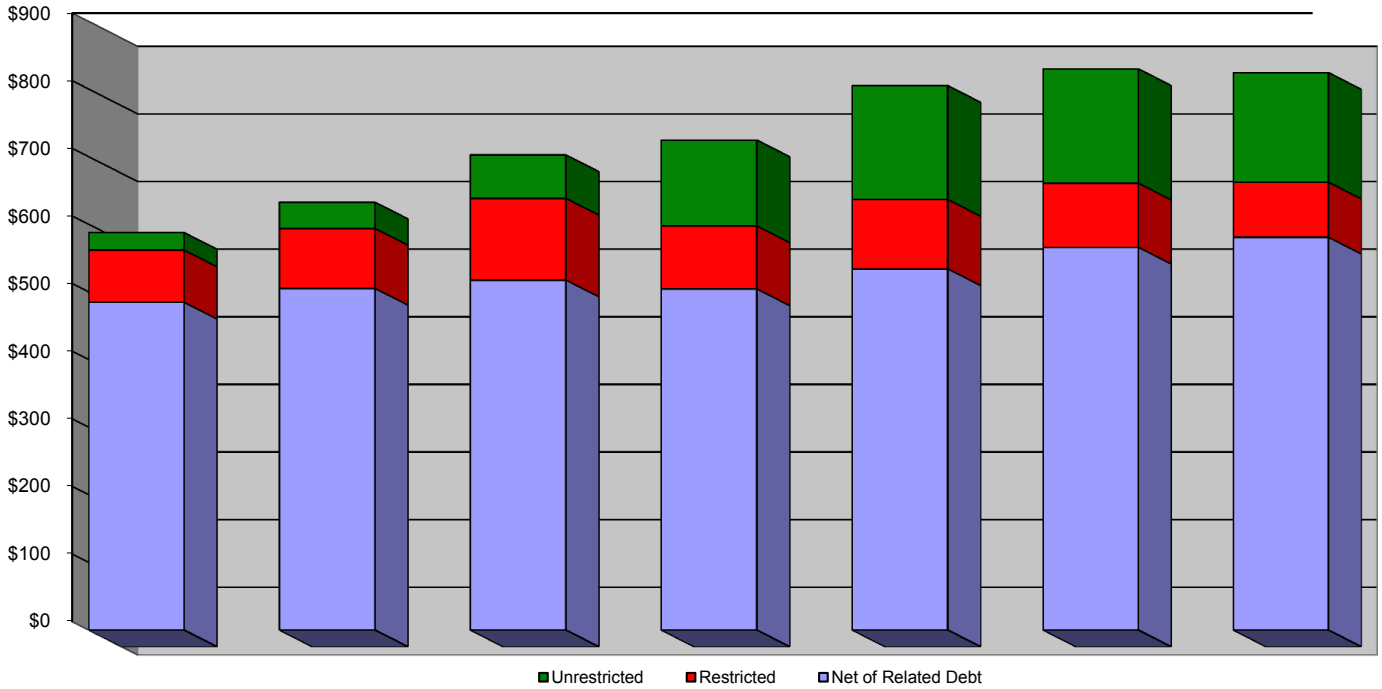
### Operating Information

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

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

Sources: Unless otherwise noted, the information in these schedules is derived from the Comprehensive Annual Financial Reports for the relevant year. The City implemented GASB Statement No. 34 in 2002; however, for schedules presenting entity-wide information, the City has elected to include information beginning in fiscal year 2003.

**CITY OF MODESTO**  
**NET ASSETS BY COMPONENT**  
 Last Seven Fiscal Years  
 (accrual basis of accounting)



	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>
<b>Governmental activities</b>							
Invested in capital assets, net of related debt	\$275,171,096	\$288,391,776	\$296,401,824	\$333,409,532	\$339,396,266	\$347,357,492	\$329,592,169
Restricted	76,577,126	88,725,341	120,937,678	93,168,664	102,602,698	94,819,773	81,528,516
Unrestricted	(11,382,001)	(6,715,483)	(2,303,306)	(12,566,297)	4,627,884	(472,402)	14,399,778
Total governmental activities net assets	<u>\$340,366,221</u>	<u>\$370,401,634</u>	<u>\$415,036,196</u>	<u>\$414,011,899</u>	<u>\$446,626,848</u>	<u>\$441,704,863</u>	<u>\$425,520,463</u>
<b>Business-type activities</b>							
Invested in capital assets, net of related debt	\$209,230,461	\$216,558,150	\$220,881,691	\$170,791,021	\$194,435,373	\$218,432,739	\$251,025,494
Restricted	763,190						
Unrestricted	37,266,369	45,548,813	66,550,276	139,613,374	163,792,245	169,639,845	147,661,517
Total business-type activities net assets	<u>\$247,260,020</u>	<u>\$262,106,963</u>	<u>\$287,431,967</u>	<u>\$310,404,395</u>	<u>\$358,227,618</u>	<u>\$388,072,584</u>	<u>\$398,687,011</u>
<b>Primary government</b>							
Invested in capital assets, net of related debt	\$484,401,557	\$504,949,926	\$517,283,515	\$504,200,553	\$533,831,639	\$565,790,231	\$580,617,663
Restricted	77,340,316	88,725,341	120,937,678	93,168,664	102,602,698	94,819,773	81,528,516
Unrestricted	25,884,368	38,833,330	64,246,970	127,047,077	168,420,129	169,167,443	162,061,295
Total primary government net assets	<u>\$587,626,241</u>	<u>\$632,508,597</u>	<u>\$702,468,163</u>	<u>\$724,416,294</u>	<u>\$804,854,466</u>	<u>\$829,777,447</u>	<u>\$824,207,474</u>

**CITY OF MODESTO**  
**CHANGES IN NET ASSETS**  
**Last Seven Fiscal Years**  
**(Accrual Basis of Accounting)**

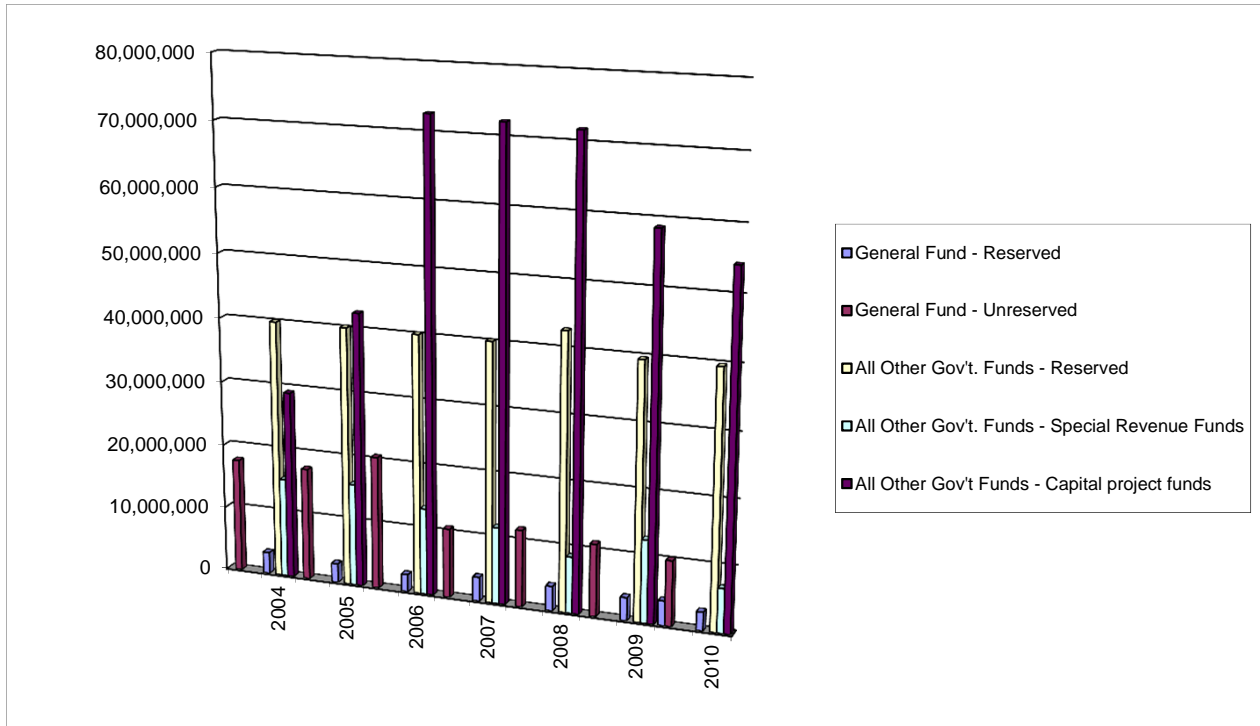
	2004	2005	2006	2007	2008	2009	2010
<b>Expenses</b>							
<b>Governmental Activities:</b>							
General Government	\$13,954,909	\$15,273,174	\$15,529,735	\$17,227,876	\$15,997,582	\$12,700,264	\$12,093,091
Community Development	\$10,517,243	\$14,105,411	\$12,241,213	12,025,105	14,619,525	14,694,997	18,912,766
Highways and streets	23,136,950	23,721,458	26,025,311	26,246,306	26,436,475	23,682,253	23,668,779
Public works	6,458,522	5,263,984	6,491,062	12,557,512	11,471,344	9,151,786	6,759,562
Parks and Recreation	12,682,746	13,334,330	11,733,698	14,568,192	14,264,334	15,070,007	13,268,871
Public safety	68,258,235	71,239,341	74,500,043	83,793,361	88,651,249	84,395,987	80,254,834
Interest on Long Term Debt	4,515,439	4,987,911	5,178,130	7,286,026	4,998,482	6,114,875	5,766,421
<b>Total Governmental Activities Expenses</b>	<b>139,524,044</b>	<b>147,925,609</b>	<b>151,699,192</b>	<b>173,704,378</b>	<b>176,438,991</b>	<b>165,810,169</b>	<b>160,724,324</b>
<b>Business-Type Activities:</b>							
Parking	651,330	1,162,479	1,287,450	1,475,340	1,982,066	2,011,386	1,826,401
Water	27,051,982	30,691,348	29,989,775	35,540,918	36,713,351	38,190,214	43,619,704
Sewer	21,386,084	22,422,268	22,716,100	24,156,577	23,974,989	22,416,713	28,055,056
Storm Drain	5,327,334	6,111,317	5,795,746	6,924,335	6,349,113	6,140,963	5,201,741
Compost			941,919	1,225,462	1,312,511	1,130,816	1,480,068
Airport	1,120,922	1,131,889	1,342,645	2,039,988	1,444,667	1,682,644	1,918,113
Bus	10,122,176	11,074,907	12,119,311	13,758,421	14,834,612	15,210,224	15,671,731
Golf	2,432,202	2,354,759	2,461,470	2,479,447	2,497,161	2,440,599	2,473,968
Community Center	2,078,752	2,323,169	2,465,644	2,543,121	2,465,825	2,303,256	2,346,175
<b>Total Business-Type Activities Expenses</b>	<b>70,170,782</b>	<b>77,272,136</b>	<b>79,120,060</b>	<b>90,143,609</b>	<b>91,574,295</b>	<b>91,526,815</b>	<b>102,592,957</b>
<b>Total Primary Government Expenses</b>	<b>\$209,694,826</b>	<b>\$225,197,745</b>	<b>\$230,819,252</b>	<b>\$263,847,987</b>	<b>\$268,013,286</b>	<b>\$257,336,984</b>	<b>\$263,317,281</b>
<b>Program Revenues</b>							
<b>Governmental Activities:</b>							
<b>Charges for Services:</b>							
General Government	\$3,321,760	\$3,252,732	\$4,179,505	\$3,775,368	\$6,726,893	\$6,987,127	\$6,323,865
Community Development	9,592,055	11,294,130	9,466,082	10,873,541	7,869,742	4,788,324	2,941,932
Highway and streets	2,005,336	14,081,840	12,104,089	10,719,009	5,804,342	8,222,178	2,801,213
Public Works	9,267,650	2,024,509	1,986,957	1,757,648	5,110,428	1,349,956	3,344,967
Parks and Recreation	3,992,598	4,821,884	4,928,366	4,437,320	5,590,196	4,006,123	6,038,468
Public Safety	6,794,911	8,011,509	7,124,387	8,414,456	4,868,612	4,625,935	4,325,231
Operating Grants and Contributions	15,975,814	13,736,453	11,892,511	12,701,177	14,221,390	11,424,548	14,559,357
Capital Grants and Contributions	18,368,908	22,799,320	38,484,548	4,207,389	17,930,957	6,595,213	10,876,018
<b>Total Government Activities Program Revenues</b>	<b>69,319,032</b>	<b>80,022,377</b>	<b>90,166,445</b>	<b>56,885,908</b>	<b>68,122,560</b>	<b>\$47,999,404</b>	<b>\$51,211,051</b>
<b>Business-Type Activities:</b>							
<b>Charges for Services:</b>							
Parking	890,263	908,920	1,176,061	1,128,755	1,297,484	1,256,360	1,239,995
Water	31,353,046	31,315,920	42,639,348	49,305,033	51,679,042	53,218,692	54,670,041
Sewer	25,292,995	24,419,607	23,083,280	24,833,019	29,340,615	35,854,857	37,310,731
Storm Drain	5,227,844	5,162,217	5,277,304	5,403,474	5,338,838	5,301,150	5,428,291
Compost			1,317,105	1,254,137	1,075,032	1,397,708	1,706,189
Airport	559,479	559,215	577,688	604,214	593,349	661,524	675,565
Bus	2,077,503	2,264,506	2,645,622	2,545,790	3,182,762	2,944,108	2,769,814
Golf	2,160,223	2,115,712	2,222,738	2,189,384	2,124,672	1,984,769	1,924,015
Community Center	496,680	504,338	543,085	552,878	532,471	492,989	489,562
Operating Grants and Contributions	6,217,613	7,525,367	8,317,889	11,059,129	12,459,707	11,462,346	13,706,512
Capital Grants and Contributions	10,145,892	8,498,408	10,467,873	7,962,675	9,793,356	4,527,875	2,898,489
<b>Total Business-Type Activities Program Revenue</b>	<b>84,421,538</b>	<b>83,274,210</b>	<b>98,267,993</b>	<b>106,838,488</b>	<b>117,417,328</b>	<b>119,102,378</b>	<b>122,819,204</b>
<b>Total Primary Government Program Revenues</b>	<b>\$153,740,570</b>	<b>\$163,296,587</b>	<b>\$188,434,438</b>	<b>\$163,724,396</b>	<b>\$185,539,888</b>	<b>167,101,782</b>	<b>174,030,255</b>
<b>Net (Expense)/Revenue</b>							
Governmental Activities	(\$70,205,012)	(\$67,903,232)	(\$61,532,747)	(116,818,470)	(108,316,431)	(117,810,765)	(109,513,273)
Business-Type Activities	14,250,756	6,002,074	19,147,933	16,694,879	25,843,033	27,575,563	20,226,247
<b>Total Primary Government Net Expense</b>	<b>(\$55,954,256)</b>	<b>(\$61,901,158)</b>	<b>(\$42,384,814)</b>	<b>(\$100,123,591)</b>	<b>(\$82,473,398)</b>	<b>(\$90,235,202)</b>	<b>(\$89,287,026)</b>

(continued)

**City of Modesto**  
**CHANGES IN NET ASSETS**  
(continued)  
**Last Seven Fiscal Years**  
**(Accrual Basis of Accounting)**

	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>
General Revenues and Other Changes in Net Assets							
Governmental Activities:							
Taxes:							
Utility Users Tax	\$14,659,986	\$15,621,566	\$17,583,690	\$18,319,573	\$19,173,295	19,093,222	12,306,702
Property taxes, levied for general purposes	11,294,599	11,316,694	14,318,747	16,456,379	16,202,587	13,863,471	19,117,518
Tax increments for redevelopment agency	3,183,871	3,909,452	4,450,836	5,303,521	5,813,822	6,228,634	6,521,515
Transient occupancy tax	2,110,909	2,098,303	2,181,467	2,264,699	2,038,255	1,853,732	1,460,613
Franchise tax	3,455,535	3,420,453	3,693,307	3,823,216	7,735,131	4,779,854	3,962,159
Business license tax - for general purposes	9,231,136	9,726,816	10,374,157	10,359,058	9,680,721	9,330,563	9,068,219
Business license tax - for downtown improvement district	190,644	201,308	214,022	221,487	202,100	196,253	169,471
Grants and contributions not restricted to specific programs:							
Sales tax	27,151,779	26,589,449	29,627,835	27,884,852	26,305,982	24,578,230	22,301,060
Motor vehicle license fee	9,052,449	16,403,864	14,986,883	16,233,262	16,856,108	15,255,503	13,945,172
Other	1,204,485	1,702,234	4,070,593	4,169,354	917,347	3,285,651	1,286,466
Unrestricted investment earnings	1,004,974	4,463,080	3,255,401	8,330,079	9,960,367	5,247,506	1,211,702
Miscellaneous	2,479,871	3,792,340	2,827,161	3,582,325	3,469,916	5,809,581	2,502,397
Settlements							
Transfers	(1,902,932)	(1,306,914)	(1,416,790)	(1,153,632)	(779,437)	(5,490,881)	402,303
Special Item - PCE legal fees							
<b>Total Government Activities</b>	<u>83,117,306</u>	<u>97,938,645</u>	<u>106,167,309</u>	<u>115,794,173</u>	<u>117,576,194</u>	<u>104,031,319</u>	<u>94,255,297</u>
Business-Type Activities:							
Taxes:							
Property taxes, generated by and allocated to the airport	204,091	239,518	166,641	209,722	182,031	202,460	265,587
Business license tax, generated by and allocated to the airport	7,870	20,546	41,108	13,054	19,188		
Unrestricted investment earnings	857,751	1,819,870	2,504,291	5,406,639	7,099,765	6,227,615	3,155,954
Miscellaneous		1,306,914				253,032	
Transfers	1,902,932	7,396,627	1,416,790	1,153,632	779,437	5,490,881	(402,303)
Settlements and Recoveries			3,784,295		14,525,389		447,102
Special item	(6,298,525)	(1,938,606)	(1,736,054)	(505,498)	(625,620)	(2,211,514)	(1,326,309)
<b>Total Business-Type Activities</b>	<u>(3,325,881)</u>	<u>8,844,869</u>	<u>6,177,071</u>	<u>6,277,549</u>	<u>21,980,190</u>	<u>9,962,474</u>	<u>2,140,031</u>
<b>Total Primary Government</b>	<u>\$79,791,425</u>	<u>\$106,783,514</u>	<u>\$112,344,380</u>	<u>\$122,071,722</u>	<u>\$139,556,384</u>	<u>\$113,993,793</u>	<u>\$96,395,328</u>
Change in Net Assets							
Governmental Activities	\$12,912,294	\$30,035,413	\$44,634,562	(\$1,024,297)	\$9,259,763	(\$13,779,446)	(\$15,257,976)
Business-Type Activities	10,924,875	14,846,943	25,325,004	22,972,428	47,823,223	37,538,037 #	22,366,278
<b>Total Primary Government</b>	<u>\$23,837,169</u>	<u>\$44,882,356</u>	<u>\$69,959,566</u>	<u>\$21,948,131</u>	<u>\$57,082,986</u>	<u>\$23,758,591</u>	<u>\$7,108,302</u>

**CITY OF MODESTO**  
**FUND BALANCES OF GOVERNMENTAL FUNDS**  
**Last Seven Fiscal Years**  
**(Modified Accrual Basis of Accounting)**



	2004	2005	2006	2007	2008	2009	2010
<b>General Fund</b>							
Reserved	\$3,327,569	\$2,955,054	2,702,381	\$3,734,973	\$3,816,559	\$3,568,273	\$2,871,715
Unreserved	17,651,800	17,460,005	20,607,134	10,713,910	11,942,168	11,185,485	10,103,645
<b>Total General Fund</b>	<u>\$20,979,369</u>	<u>\$20,415,059</u>	<u>\$23,309,515</u>	<u>\$14,448,883</u>	<u>\$15,758,727</u>	<u>\$14,753,758</u>	<u>\$12,975,360</u>
<b>All Other Governmental Funds</b>							
Reserved	\$40,013,124	\$40,160,539	\$40,168,886	\$40,174,920	\$42,799,130	\$39,607,945	39,686,892
Unreserved, reported in:							
Special revenue funds	15,398,402	15,931,290	13,431,304	11,885,910	8,746,111	12,808,809	6,867,750
Capital project funds	29,172,787	42,534,688	72,752,412	72,253,464	71,780,583	58,718,023	54,341,594
<b>Total all other governmental funds</b>	<u>\$84,584,313</u>	<u>\$98,626,517</u>	<u>\$126,352,602</u>	<u>\$124,314,294</u>	<u>\$123,325,824</u>	<u>\$111,134,777</u>	<u>\$100,896,236</u>

The change in total fund balance for the General Fund and other governmental funds is explained in Management's Discussion and Analysis.

Note: The City has elected to show only seven years of data for this schedule.

**CITY OF MODESTO**  
**CHANGES IN FUND BALANCE OF GOVERNMENTAL FUNDS**  
**Last Seven Fiscal Years**  
**(Modified Accrual Basis of Accounting)**

	2004	2005	2006	2007	2008	2009	2010
<b>Revenues</b>							
Taxes	\$44,185,552	\$46,295,678	\$52,816,596	\$56,748,017	\$57,142,392	\$55,345,729	\$52,606,197
Licenses, permits and fees	250,129	128,754	146,854	187,289	153,545	132,459	138,811
Intergovernmental	70,583,373	73,889,063	64,759,658	66,129,862	71,179,504	63,606,634	61,551,617
Charges for services	33,203,507	41,660,016	37,802,149	36,979,023	33,319,642	27,051,151	23,509,170
Special assessments levied	386,368	107,696	65,909	51,634	35,294	37,299	38,520
Interest and rent	2,911,392	3,146,452	3,755,169	4,837,419	5,236,476	2,909,155	1,322,005
Net increase in fair value of investments	(1,458,065)	186,515	103,036	1,168,857	1,404,913	860,820	399,322
Fines and forfeits	1,294,193	1,646,472	1,675,926	2,699,445	2,614,523	2,443,506	2,253,014
Contribution from property owners			30,473,773				
Miscellaneous	2,479,871	2,991,745	2,821,161	2,814,421	3,469,916	5,809,581	2,502,397
<b>Total Revenues</b>	<b>153,836,320</b>	<b>170,052,391</b>	<b>194,420,231</b>	<b>171,615,967</b>	<b>174,556,205</b>	<b>158,196,334</b>	<b>144,321,053</b>
<b>Expenditures</b>							
Current:							
General government	11,878,443	11,819,603	14,111,535	15,517,544	15,107,461	13,715,577	11,482,240
Community development	10,113,628	12,832,640	12,296,072	11,789,640	13,820,295	14,137,095	18,536,120
Highways and streets	11,568,810	12,152,087	14,357,041	12,553,681	12,549,018	9,721,445	8,102,327
Public works	4,876,115	5,053,030	5,647,023	11,307,307	9,719,098	7,667,125	6,124,685
Parks and recreation	11,374,052	12,021,937	11,662,263	13,348,613	12,605,651	13,307,764	12,138,077
Public safety	62,747,623	70,882,176	74,527,875	80,988,650	82,707,285	78,103,260	75,081,791
Capital outlay	33,092,718	24,412,735	21,563,774	30,194,778	22,745,308	27,663,037	16,655,242
Debt service:							
Principal retirement	1,563,472	1,666,764	1,901,827	2,008,538	2,265,000	1,093,000	2,045,000
Interest	4,502,666	4,425,980	4,576,780	4,413,300	3,473,369	3,033,829	4,032,612
Advance refunding escrow				822,228			
Other	18,355	553,645	618,742	1,333,129	1,337,611	1,395,211	1,408,771
<b>Total Expenditures</b>	<b>151,735,882</b>	<b>155,820,597</b>	<b>161,262,932</b>	<b>184,277,408</b>	<b>176,330,096</b>	<b>169,837,343</b>	<b>155,606,865</b>
Excess of revenues over (under) expenditures	2,100,438	14,231,794	33,157,299	(12,661,441)	(1,773,891)	(11,641,009)	(11,285,812)
<b>Other Financing Sources (Uses)</b>							
Transfers in	19,332,436	17,962,442	17,724,718	23,985,863	24,429,880	19,237,526	12,346,246
Transfers out	(20,819,979)	(19,644,937)	(20,267,476)	(26,399,280)	(22,579,265)	(18,149,564)	(12,402,937)
Proceeds of capital lease							
Proceeds of loan payable	212,241			44,138	244,650	209,575	
Proceeds of notes payable	4,500,000						
Proceeds of lease revenue bonds				62,275,000		65,170,000	
Refunding of lease revenue bonds						(65,210,000)	
Sale of Assets		928,595	6,000	767,904		34,900	
Payments to refunded debt escrow agent				(58,911,124)		(2,431,247)	
<b>Total other financing sources (uses)</b>	<b>3,224,698</b>	<b>(753,900)</b>	<b>(2,536,758)</b>	<b>1,762,501</b>	<b>2,095,265</b>	<b>(1,138,810)</b>	<b>(56,691)</b>
<b>Net Change in fund balances</b>	<b>5,325,136</b>	<b>13,477,894</b>	<b>30,620,541</b>	<b>(10,898,940)</b>	<b>321,374</b>	<b>(\$12,779,819)</b>	<b>(\$11,342,503)</b>
FUND BALANCES, July 1	100,238,546	105,563,682	119,041,576	149,662,117	138,763,177	\$139,084,551	\$125,888,535
PRIOR PERIOD ADJUSTMENT						(\$416,197)	(\$674,436)
<b>FUND BALANCES, June 30</b>	<b>\$105,563,682</b>	<b>\$119,041,576</b>	<b>\$149,662,117</b>	<b>\$138,763,177</b>	<b>\$139,084,551</b>	<b>125,888,535</b>	<b>113,871,596</b>
Debt service as a percentage of noncapital expenditures	0.05389	0.04884	0.04886	0.04979	0.03917	0.03020	0.04623

Note : The City has elected to show only seven years of data for this schedule.

**CITY OF MODESTO**  
**REVENUE CAPACITY - MOST SIGNIFICANT LOCAL REVENUE SOURCE**  
**WATER UTILITY CHARGES**  
**(Fiscal Year ended June 30, 2010)**

Ten Largest Customers of Water Utility System, Year Ended 06/30/10

<u>Customer</u>	<u>Usage (ccf) (1)</u>	<u>% of Total Usage</u>	<u>Water Sales Revenue (\$)</u>	<u>% of Total Water Sales Revenue</u>
1) City of Modesto	418,286	1.44%	\$759,779	1.52%
2) Signature Fruit Co, LLC	491,435	1.69%	644,383	1.29%
3) Modesto City Schools	385,633	1.33%	619,042	1.24%
4) Stanislaus Food Products	346,940	1.20%	468,984	0.94%
5) Foster Farms	330,064	1.14%	430,271	0.86%
6) Modesto Irrigation Dist	198,817	0.69%	285,468	0.57%
7) Stanislaus Housing Authority	161,363	0.56%	271,324	0.54%
8) Stanislaus County Building MAI	126,208	0.43%	206,937	0.41%
9) Sylvan Union School Dist	125,689	0.43%	203,885	0.41%
10) Yosemite Comm Coll Dist	109,723	0.38%	199,493	0.40%
Total Top Ten	<u>2,694,158</u>	<u>9.29%</u>	<u>\$4,089,566</u>	<u>8.18%</u>

Total Flat/Metered Revenues (Water Sales)

\$50,015,340

(1) "ccf" means "hundred cubic feet"

Sales Revenue, Year Ended 0

Residential - flat rates

\$21,256,928

Commercial, Industrial and municipal - metered rates

28,758,412

Total Water Sales

\$50,015,340

Water Rates and Charges as of 07/01/09

The average monthly flat rate service charge for residential customers is:

\$42.31

Commercial Accounts:

\$13.71  
19.45  
33.66  
50.79  
96.51  
147.88  
290.51  
461.75  
661.58  
1,232.31

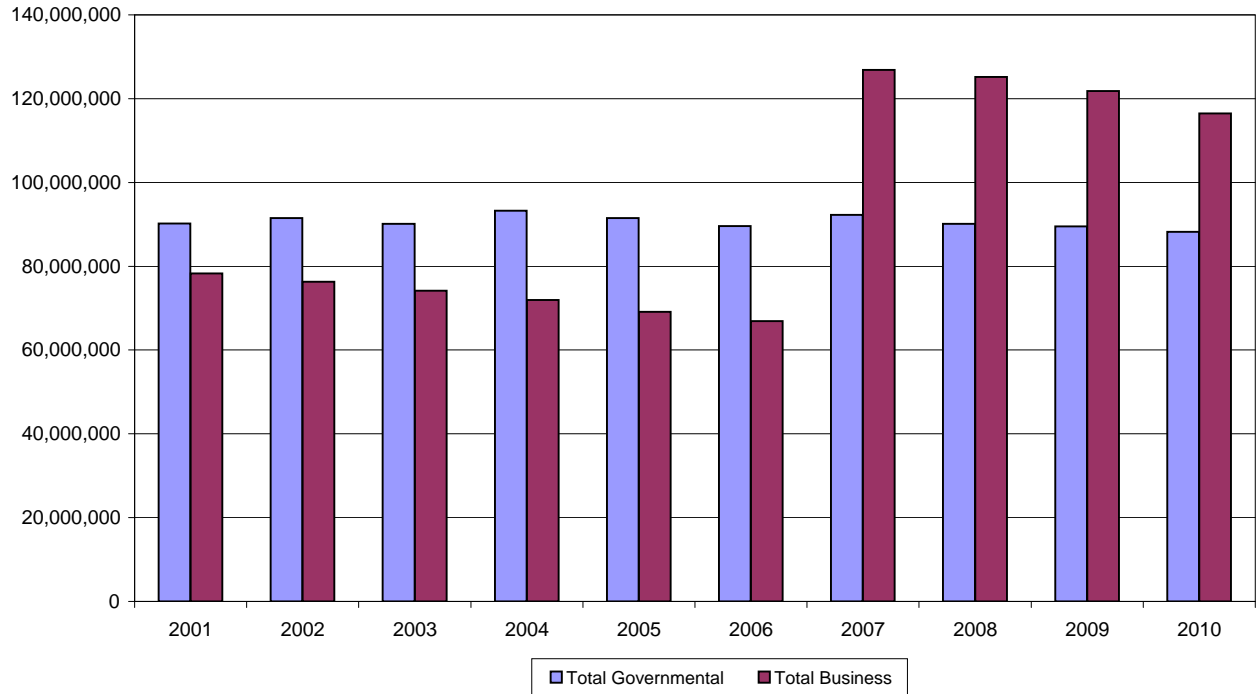
In addition to these minimum charges, commercial accounts are charged \$1.28 per 100 cubic feet of water used.

Source:

City of Modesto-Customer Services

**Note: Information about Water Utility Customers was not available for the year ended June 30, 1998.**

**CITY OF MODESTO**  
**RATIO OF OUTSTANDING DEBT BY TYPE**  
**Last Ten Fiscal Years**



**Governmental Activities**

Fiscal Year	Governmental Activities					Total
	Loans Payable	Certificates of Participation	Lease Revenue Bonds	Notes Payable	Obligations Under Capital Leases	
2001		25,280,000	64,615,000		329,594	90,224,594
2002	\$191,835	24,625,000	64,250,000	\$262,807	2,153,350	91,482,992
2003	348,273	23,935,000	63,865,000	241,880	1,753,685	90,143,838
2004	523,363	23,215,000	63,455,000	4,719,663	1,335,182	93,248,208
2005	485,077	22,455,000	63,000,000	4,696,076	896,833	91,532,986
2006	446,634	21,655,000	62,505,000	4,535,034	444,904	89,586,572
2007	449,138	20,820,000	66,440,000	4,365,446	211,354	92,285,938
2008	693,788	19,935,000	65,210,000	4,187,220	137,392	90,163,400
2009	903,362	19,000,000	65,170,000	3,999,252	454,401	89,527,015
2010	903,362	18,015,000	64,275,000	3,802,436	1,221,553	88,217,351

**Business-Type Activities**

Fiscal Year	Business-Type Activities					Total Primary Government	Percentage of Personal Income (a)	Per Capita (a)
	Loans Payable	Certificates of Participation	Revenue Bonds	Capital Leases	Total			
2001	3,056,210	30,525,000	44,735,000		78,316,210	168,540,804	3.82%	895.13
2002	2,887,342	29,765,000	43,640,000		76,292,342	167,775,334	3.55%	844.79
2003	2,713,066	28,965,000	42,490,000		74,168,066	164,311,904	3.33%	808.22
2004	2,533,380	28,125,000	41,285,000		71,943,380	165,191,588	3.09%	801.12
2005	2,347,602	27,240,000	39,235,000	\$290,487	69,113,089	160,646,075	2.87%	773.70
2006	2,156,040	26,305,000	38,245,000	222,588	66,928,628	156,515,200	2.81%	752.09
2007	1,958,276	71,595,000	53,130,000	151,633	126,834,909	219,120,847	3.76%	1,047.55
2008	1,754,300	71,915,000	51,420,000	77,485	125,166,785	215,330,185	3.69%	1,025.69
2009	1,543,554	70,545,000	49,760,000	0	121,848,554	211,375,569	3.47%	1,006.13
2010	1,326,174	67,066,213	48,050,000	0	116,442,387	204,659,738	3.07%	967.49

Note: debt amounts are gross outstanding at year end without eliminating any premiums, discounts, or other amortization amounts.  
(a) See Demographic and Economic Statistics for personal income and population data.

**CITY OF MODESTO**  
**COMPUTATION OF DIRECT AND OVERLAPPING DEBT**  
**June 30, 2010**

<u>Jurisdiction</u>	<u>Net Debt Outstanding (1)</u>	<u>Percentage Applicable to City of Modesto (2)</u>	<u>Amount Applicable to City of Modesto</u>
Direct debt:			
City of Modesto	\$ <u>0</u>	100%	\$ <u>0</u>
Overlapping General Obligation debt - school districts:			
Ceres Unified District	44,794,682	5.71	2,557,776
Hart-Ransom Union School District	3,899,767	34.75	1,355,169
Modesto Elementary School District	15,963,051	79.23	12,647,525
Modesto High School District	59,694,357	67.18	40,102,669
Paradise Elementary School District	400,000	0.00	0
Salida Union Elementary District	940,000	28.99	272,506
Stanislaus Union School District	13,005,000	27.09	3,523,055
Sylvan School District	27,555,000	77.27	21,291,749
Yosemite Community College District	<u>228,190,000</u>	35.62	81,281,278
Total overlapping debt	<u>394,441,857</u>		<u>163,031,727</u>
Total direct and overlapping debt	<u>\$ 394,441,857</u>		<u>\$ 163,031,727</u>

NOTES:

source of data for School Districts: Stanislaus County Auditor.

- (1) Gross debt outstanding less applicable amounts in debt service funds.
- (2) Determined by ratio of assessed valuation of property subject to taxation in overlapping portion to valuation of all property subject to taxation in the jurisdiction.

**CITY OF MODESTO**  
**COMPUTATION OF LEGAL DEBT MARGIN**  
**June 30, 2010**

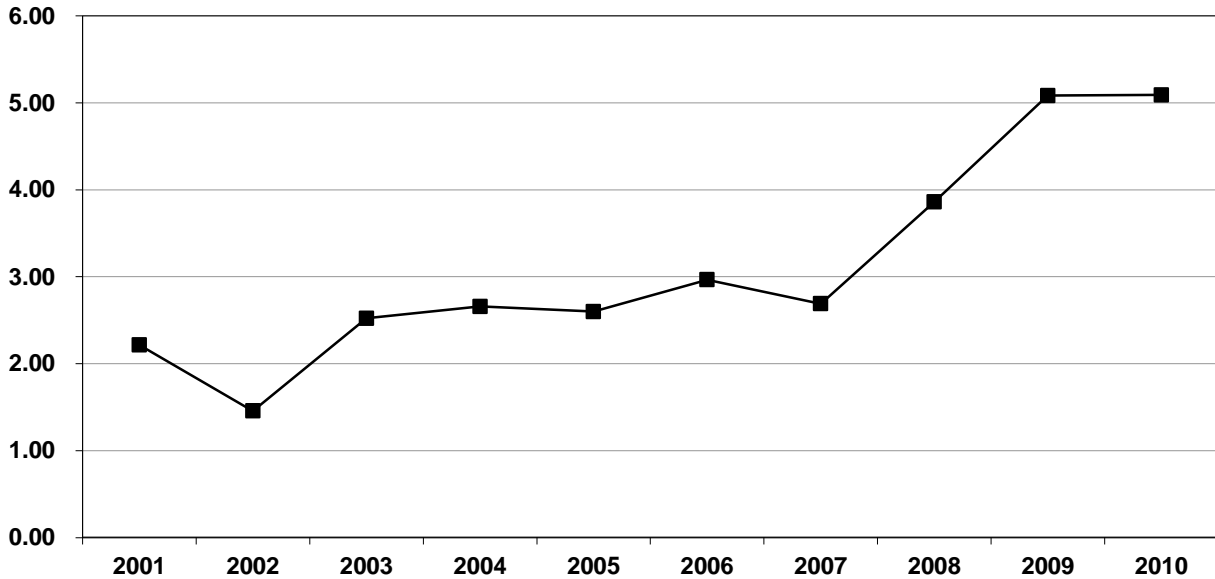
Net assessed value (1)		\$ 12,151,454,248
Plus homeowners' exemption (1)		<u>226,617,558</u>
Gross assessed value (1)		\$ 12,378,071,806
Debt limit - 15% of gross assessed value (2)		\$ 1,856,710,771
Amount of debt applicable to debt limit:		
Total general bonded debt, including special assessment debt	\$	<u>0</u>
Less: Assets in debt service funds available for payment of principal	\$	<u>0</u>
Other deductions: Special assessment debt	<u>0</u>	
Total deductions		<u>0</u>
Total amount of debt applicable to debt limit		<u>0</u>
Legal debt margin		<u><u>\$ 1,856,710,771</u></u>

Fiscal Year	Debt Limit	Total Net Debt Applicable to Limit	Legal Debt Margin	Total Net Debt Applicable to the Limit as a Percentage of Debt Limit
2006	\$ 1,911,402,504	\$ 0	\$ 1,911,402,504	0%
2007	\$ 2,160,683,976	\$ 0	\$ 2,160,683,976	0%
2008	\$ 2,327,946,572	\$ 0	\$ 2,327,946,572	0%
2009	\$ 2,138,574,915	\$ 0	\$ 2,138,574,915	0%
2010	\$ 1,856,710,771	\$ 1	\$ 1,856,710,771	0%

Notes: (1) Source of Data: Stanislaus County Auditor; Certified Values Report (AUD70-2360-100, including aircraft)  
(2) Section 43605 California Government Code.

Note: The City has elected to show only three Five of data for this schedule.

**CITY OF MODESTO**  
**REVENUE BOND COVERAGE**  
**WASTEWATER REVENUE BONDS**  
**Last ten fiscal years**



<u>Fiscal Year</u>	<u>Gross Revenue (1)</u>	<u>Operating Expenses (2)</u>	<u>Net Revenue Available for Debt Service</u>	<u>Debt Service Requirements(3)</u>	<u>Coverage</u>
2001	21,102,892	13,244,750	7,858,142	3,549,180	2.21
2002	22,288,061	17,117,917	5,170,144	3,550,017	1.46
2003	24,623,786	15,664,660	8,959,126	3,551,958	2.52
2004	26,123,771	16,687,958	9,435,813	3,550,120	2.66
2005	25,701,300	16,476,917	9,224,383	3,549,633	2.60
2006	24,695,878	16,044,781	8,651,097	2,916,462	2.97
2007	26,367,977	16,399,785	9,968,192	3,705,523	2.69
2008	32,214,071	16,280,914	15,933,157	4,127,837	3.86
2009	37,539,860	17,050,138	20,489,722	4,030,633	5.08
2010	39,086,504	18,161,292	20,925,212	4,110,221	5.09

- Notes: (1) Consists of all receipts of the Sewer fund not dedicated to capital spending purposes and including charges for services, connection fees, interest and rental income.  
(2) Reflects total sewer fund operating expenses less depreciation; also includes certain transfers out that are made for operational costs incurred in other funds.  
(3) Includes total principal and interest of Wastewater Refunding Revenue Bonds Series 2005A and 2005 B and 2006 Wastewater Revenue Bonds.

**CITY OF MODESTO**  
**CONTINUING DISCLOSURE REQUIREMENTS INFORMATION**  
**Year Ended June 30, 2010**

Wastewater Revenue Refunding Bonds, Series 2005 A and B, and  
Wastewater Revenue Bonds, Series 2006 A

Connection charge information: The Sewer Enterprise imposes connection fees on a on-time basis to new users of the sewer system and to users who significantly expand their usage. The fees have three components:

Capacity charge: \$4,905 per Equivalent Dwelling Unit for residential units. Commercial and industrial property charged based on type of business.  
 Sub-trunk sewer charge: \$645 per acre  
 Connection (lateral) charge: \$33 per linear foot of lot frontage adjacent to the sewer line.

<u>Category</u>	<u>Customer Base by Type of Account</u>		
	<u>Number of Accounts</u>	<u>% of Total Accounts</u>	<u>% of Sewer Fee Operating Revenue</u>
Residential	57,018	95.52%	55.25%
Commercial	2,635	4.41%	12.27%
Industrial	42	0.07%	30.78%
Total	<u>59,695</u>	<u>100.00%</u>	<u>98.30%</u>

Ten Largest Users of Sewer Facilities, Year Ended 6/30/10

<u>User</u>	<u>Sewer Fee Revenue</u>	<u>% of Sewer Fee Operating Revenue</u>
1) Del Monte Corporation	\$ 2,248,400	6.34%
2) Stanislaus Food Products	2,040,183	5.75%
3) Signature Fruit CO, LLC	1,737,981	4.90%
4) Gallo Glass	1,146,917	3.23%
5) Frito Lay, Site #34390	893,187	2.52%
6) Foster Farms	885,692	2.50%
7) City of Ceres	662,795	1.87%
8) Nestle Food Company	392,513	1.11%
9) Modesto City Schools	200,679	0.57%
10) Stan CO Housing Authority	158,417	0.45%
Total (Top Ten Customers)	<u>\$ 10,366,764</u>	<u>29.24%</u>
Total (All Customers)	<u>\$ 35,455,433</u>	

The average single-family residence monthly sewer charge is \$24.11

<u>Commercial Group</u>	<u>Charge Per 1,000 Gallons</u>	<u>Fixed Charge</u>
Group 1 (no food, just toilets or working facilities)	\$1.76	\$3.33
Group 2 (commercial laundromats, service stations, hotels without food)	\$2.17	\$3.33
Group 3 (industrial laundromats, hotels with food)	\$2.58	\$3.33
Group 4 (restaurants, bakeries, auto steam, markets)	\$3.07	\$3.33

Industrial users pay a minimum account charge of \$3.33 with additional charges of: \$1,918.51 per million gallons of flow, \$95.25 per 1,000 pounds of excess biochemical oxygen demand (BOD), and \$166.57 per 1,000 pounds of Total Suspended Solids (TSS).

The Annual Budget of the City of Modesto is available from the City of Modesto Finance Department.

Updates of other required disclosures may be found elsewhere in this report, as follows:

Statement of Revenues, Expenses and Changes in Fund Net Assets	Page 27	
Principal Amount of Bonds and Other Parity Debt	Page 44-45	(Note III-C)
Historical Debt Service Coverage	Page 115	
	(continued)	

**CITY OF MODESTO**  
**WASTEWATER COMPARISON INFORMATION**  
**Year Ending June 30, 2010**

Residential, commercial and industrial rates have increased according to the following approved schedule.

**CITY OF MODESTO**  
**WASTEWATER SYSTEM**  
**Six Year History Rate Increases**

<u>Fiscal Year</u>	<u>Percent Increase</u>
2004/05	3.0
2005/06	0.0
2006/07	0.0
2007/08	30.0
2008/09	30.0
2009/10	0.0

**Comparative Monthly Wastewater Service Charges.** The City's residential charges as of July 1, 2009 are set forth in the table below with a comparison to other Central Valley and Northern California cities.

**CITY OF MODESTO**  
**WASTEWATER SYSTEM**  
**Monthly Sewer Charge Comparison**  
**Residential Service**  
**As of July 1, 2009**

<u>City</u>	<u>Monthly Residential Charge</u>
<b>Modesto</b>	<b>\$24.11</b>
Stockton	22.75
Fresno(1)	24.98
Lodi(2)	34.68
Turlock	38.55
Tracy	31.00

(1) Minimum charge.

(2) Based upon a three-bedroom residence.

**CITY OF MODESTO**  
**CONTINUING DISCLOSURE REQUIREMENTS**  
**Year Ending June 30, 2010**

**CITY OF MODESTO**  
**WASTEWATER SYSTEM**  
**Wastewater Connection Fees Comparison**  
**As of January 1, 2009**

<u>City</u>	<u>Connection Fee</u>
<b>Modesto</b>	<b>\$4,905</b>
Turlock (1)	2,281
Fresno	2,119
Stockton-South of the Calaveras River (2)	4,096
Tracy	15,300
Stockton-North of the Calaveras River (3)	4,911
Lodi (4)	5,785

---

(1) Based on local street rate.

(2) Represents an average of six fee zones.

(3) Represents an average of three fee zones.

(4) Based upon a two-bedroom residence.

## APPENDIX D

### DEFINITIONS AND SUMMARY OF THE AMENDED AND RESTATED TRUST AGREEMENT

The following is a summary of the provisions of the Amended and Restated Trust Agreement. This summary is not intended to be definitive and is qualified in its entirety by reference to the aforementioned document. A copy of the Amended and Restated Trust Agreement is available upon request from the Trustee.

All capitalized terms not defined herein or elsewhere in this Supplement shall have the meanings set forth in the Amended and Restated Trust Agreement.

#### THE TRUST AGREEMENT

Certain provisions of the Amended and Restated Trust Agreement are summarized below. THIS SUMMARY DOES NOT PURPORT TO BE COMPLETE OR DEFINITIVE AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO THE FULL TERMS OF THE AMENDED AND RESTATED TRUST AGREEMENT.

#### Definitions

The following are summaries of definitions of certain terms from the Amended and Restated Trust Agreement used in this Definitions and Summary of the Amended and Restated Trust Agreement or elsewhere in this Supplement.

“Alternate Liquidity Facility” means a letter of credit (including, without limitation, the Replacement Liquidity Facility), line of credit, surety bond, standby purchase agreement or other security or liquidity instrument, as the case may be, approved by the 2008 Certificate Insurer and issued in accordance with the terms of the Trust Agreement with respect to the 2008 Certificates as a replacement or substitute for any Liquidity Facility then in effect.

“Authority” means the Modesto Public Financing Authority, a joint exercise of powers authority duly organized and existing under and by virtue of the laws of the State.

“Authorized Denominations” means (i) with respect to 2008 Certificates in a Daily Mode or Weekly Mode, \$100,000 and any integral multiple of \$5,000 in excess thereof; (ii) with respect to 2008 Certificates in a Flexible Mode, \$100,000 and any integral multiple of \$1,000 in excess thereof; and (iii) with respect to 2008 Certificates in a Term Rate Mode or Fixed Rate Mode, \$5,000 and any integral multiple thereof.

“Automatic Termination Event” means an event of default set forth in a Reimbursement Agreement between the Authority and a Liquidity Facility Provider which would result in the immediate termination of the Liquidity Facility provided pursuant to such Reimbursement Agreement prior to its stated expiration date without prior notice from the Liquidity Facility Provider to the Trustee.

“Bank” means JPMorgan Chase Bank, N.A., and its successors or assigns.

“Book-Entry System” means a system under which physical certificates in fully registered form are registered only in the name of a Securities Depository or its nominee.

“Business Day” means any day other than (i) a Saturday or Sunday or (ii) a day on which the Trustee is required or authorized to be closed or (iii) a day on which the office of the applicable Credit Enhancement Provider at which draws or advances will be paid is required or authorized to be closed or (iv) a day on which The New York Stock Exchange is closed.

“Cancellation Date” means the date on which the 2008 Certificate Insurance Policy is cancelled, which date will be the seventh Business Day following receipt by the Trustee of written notice from (i) the Bank specifying that the 2008 Certificate Insurance Policy is to be cancelled in accordance with the terms of the Reimbursement Agreement between the Bank and the City or (ii) the Authority with the consent of the Bank specifying that the 2008 Certificate Insurance Policy is to be replaced with a substitute Credit Enhancement.

“Certificate of the Authority” means an instrument in writing signed by the Auditor and Treasurer of the Authority or by any other officer of the Authority duly authorized by the Authority for that purpose.

“Certificate Payment Date” means, with respect to any 2008 Certificate, the Certificate Payment Date designated therein, which is the October 1 on which or, in the case of 2008 Certificates subject to mandatory sinking fund prepayment, by which, the principal component of the final 2008 Payment evidenced and represented thereby will become due and payable.

“City” means the City of Modesto, a charter city and municipal corporation, duly organized and existing under and by virtue of the Constitution and laws of the State.

“Code” means the Internal Revenue Code of 1986, and the regulations issued thereunder, as the same may be amended from time to time, and any successor provisions of law. Reference to a particular section of the Code will be deemed to be a reference to any successor to any such section.

“Contract” means that certain Master Contract, as supplemented by the 1997 Supplemental Contract and the 2008 Supplemental Contract, and as otherwise amended or supplemented from time to time.

“Control Event” means that one or more of the circumstances referred to in the Trust Agreement has occurred as a result of which all references in the Trust Agreement to the 2008 Certificate Insurer and all provisions in the Trust Agreement for the benefit of the 2008 Certificate Insurer are of no effect (other than rights of the 2008 Certificate Insurer derived through subrogation and assignment).

“Corporate Trust Office” means the corporate trust office of the Trustee in San Francisco, California, or such other office as may be specified by written notice from the Trustee to the Authority.

“Costs of Issuance” means all items of expense directly or indirectly payable by or reimbursable to the City or the Authority and related to the authorization, execution and delivery of the 2008 Supplemental Contract and the Trust Agreement and the execution, sale and delivery of the 2008 Certificates, including, but not limited to, costs of preparation and reproduction of documents, costs of rating agencies and costs to provide information required by rating agencies, filing and recording fees, initial fees and charges of the Trustee and its counsel, legal fees and charges, fees and disbursements of consultants and professionals, fees and expenses of the underwriter, fees and charges for preparation, execution and safekeeping of the 2008 Certificates, fees of the Liquidity Facility Provider, fees of the Authority and any other cost, charge or fee in connection with the original execution and delivery of the 2008 Certificates.

“Costs of Issuance Fund” means the fund by that name established pursuant to the Trust Agreement.

“Credit Enhancement” means the 2008 Certificate Insurance Policy issued by the 2008 Certificate Insurer. In case a letter of credit is provided as a Liquidity Facility, such letter of credit will also be considered a Credit Enhancement and its issuer, a Credit Enhancement Provider, if such letter of credit is a direct-pay letter of credit that provides for the payment of the principal of, and interest with respect to, the 2008 Certificates as they become due.

“Credit Enhancement Provider” means, with respect to a Credit Enhancement, the issuer or provider thereof.

“Daily Mode” means the Mode during which the 2008 Certificates evidence interest at the Daily Rate.

“Daily Rate” means the per annum interest rate with respect to the 2008 Certificates in the Daily Mode determined pursuant to the Trust Agreement.

“Daily Rate Period” means the period during which the 2008 Certificates in the Daily Mode will evidence interest at a Daily Rate, which will be from the Business Day upon which a Daily Rate is set to but not including the next succeeding Business Day.

“Delivery Date” means May 29, 2008.

“Event of Default” means an event described in the Trust Agreement.

“Expiration Date” means the stated expiration date of a Liquidity Facility, as it may be extended from time to time as provided in such Liquidity Facility, or any earlier date on which such Liquidity Facility will terminate at the direction of the Authority, expire or be cancelled (other than the date on which a Liquidity Facility will terminate as a result of an Automatic Termination Event or an event of default under the Reimbursement Agreement entered into in connection with such Liquidity Facility).

“Favorable Opinion of Special Counsel” means, with respect to any action the occurrence of which requires such an opinion, an Opinion of Special Counsel, addressed to the Trustee, to the effect that the action proposed to be taken will not, in and of itself, adversely affect any exclusion from gross income of interest with respect to the 2008 Certificates.

“Federal Securities” will have the meaning ascribed thereto in the Contract.

“Fiscal Year” means the period beginning on July 1 of each year and ending on the next succeeding June 30, or any other annual accounting period hereafter selected and designated by the Authority as its Fiscal Year.

“Fixed Rate” means the per annum interest rate or interest rates evidenced by the 2008 Certificates in a Fixed Rate Mode determined pursuant to the Trust Agreement.

“Fixed Rate Mode” means the Mode during which the 2008 Certificates evidence interest at a Fixed Rate.

“Fixed Rate Period” means, with respect to 2008 Certificates converted to the Fixed Rate Mode, the period from the Mode Change Date upon which the 2008 Certificates were converted to a Fixed Rate Mode to but not including the Maturity Date.

“Flexible Mode” means the Mode during which the 2008 Certificates evidence interest at Flexible Rates.

“Flexible Rate” means, with respect to the 2008 Certificates in a Flexible Mode, the per annum interest rate determined for the 2008 Certificate pursuant to the Trust Agreement.

“Flexible Rate Certificates” means the 2008 Certificates in a Flexible Mode.

“Flexible Rate Period” means, with respect to the 2008 Certificates in a Flexible Mode, the period of from 1 to 397 calendar days (which Flexible Rate Period must end on a day preceding a Business Day) during which a Flexible Rate Certificate will evidence interest at a Flexible Rate, as established by the Remarketing Agent pursuant to the Trust Agreement.

“Improvement Fund” means the fund by that name established pursuant to the Contract.

“Independent Certified Public Accountant” means any certified public accountant or firm of such accountants duly licensed and entitled to practice and practicing as such under the laws of the State, appointed and paid by the Authority, and who, or each of whom:

(1) is in fact independent according to the Statement of Auditing Standards No. 1 and not under the domination of the Authority;

(2) does not have a substantial financial interest, direct or indirect, in the operations of the Authority; and

(3) is not connected with the Authority as a member, officer or employee of the Authority, but who may be regularly retained to audit the accounting records of and make reports thereon to the Authority.

“Information Services” means Financial Information, Inc.’s “Daily Called Bond Service,” 30 Montgomery Street, 10th Floor, Jersey City, New Jersey 07302, Attention: Editor; FIS/Mergent, Inc., 5250 77 Center Drive, Suite 150, Charlotte, North Carolina 28217, Attn: Call Notification; Standard & Poor’s Securities Evaluation, Inc., 55 Water Street, 45th Floor, New York, New York 10041, Attention: Notification Department; Xcitek, 5 Hanover Square, New York, New York 10004; and, in accordance with then current guidelines of the Securities and Exchange Commission, such other addresses and/or such other services providing information with respect to the redemption of bonds or the prepayment of certificates of participation as the Authority may designate in a Certificate of the Authority filed with the Trustee.

“Insurer Indenture Event of Default” means and includes the occurrence of one or more of the following events:

(a) any principal or interest evidenced by the 2008 Certificates (including Liquidity Provider Certificates or Subrogated Certificates) is not paid by the 2008 Certificate Insurer when, as, and in the amounts required to be paid pursuant to the terms of the 2008 Certificate Insurance Policy; or

(b) (i) any material provision of the 2008 Certificate Insurance Policy relating to the obligation of the 2008 Certificate Insurer to make payments of principal and interest thereunder at any time for any reason ceases to be valid and binding on the 2008 Certificate Insurer in accordance with the terms of the 2008 Certificate Insurance Policy or the New York Department of Insurance, or a court or other governmental authority of appropriate jurisdiction shall find or rule or shall enter an order, judgment or decree that the 2008 Certificate Insurance Policy is not valid and binding on the 2008 Certificate Insurer or (ii) the 2008 Certificate Insurer will (A) claim in writing that the 2008 Certificate Insurance Policy is not valid and binding on the 2008 Certificate Insurer, (B) repudiate the 2008 Certificate Insurer's obligations under the 2008 Certificate Insurance Policy or (C) initiate legal proceedings seeking an adjudication that the 2008 Certificate Insurance Policy, or any material provision thereof regarding the payment of principal or interest on 2008 Certificates (including Liquidity Provider Certificates) is not valid and binding on the 2008 Certificate Insurer; or

(c) a proceeding is instituted in a court having jurisdiction in the premises seeking an order for relief, rehabilitation, reorganization, conservation, liquidation or dissolution in respect to the 2008 Certificate Insurer or for any substantial part of its property under any applicable bankruptcy, insolvency or other similar law now or hereafter in effect, or for the appointment of a receiver, liquidator, assignee, custodian, trustee or sequestrator (or other similar official) and such proceeding shall not have been dismissed within sixty (60) days or such court enters an order granting the relief sought in such proceeding; or the New York Department of Insurance shall declare a moratorium on the payment of the 2008 Certificate Insurer's debts, or the 2008 Certificate Insurer shall commence a voluntary case under any applicable bankruptcy, insolvency or other similar law now or hereafter in effect, shall consent to the entry of an order for relief in an involuntary case under any such law or shall consent to the appointment of or taking possession by a receiver, liquidator, assignee, trustee, custodian or sequestrator (or other similar official) of the 2008 Certificate Insurer or for any substantial part of its property, or shall make a general assignment for the benefit of creditors, or shall fail generally to pay its debts (provided for purposes of this definition, "debts" shall not include any obligation of the 2008 Certificate Insurer under any insurance policy or surety bond) as they become due, or an order for rehabilitation, liquidation or dissolution of the 2008 Certificate Insurer shall be issued.

"Interest Payment Date" means each date on which interest is to be paid and is: (i) with respect to the 2008 Certificates in a Daily Mode or a Weekly Mode, the first Business Day of each month; (ii) with respect to the 2008 Certificates in a Flexible Mode, each Mandatory Purchase Date applicable thereto; (iii) with respect to the 2008 Certificates in a Fixed Rate Mode or a Term Rate Mode, the first day of April or October, which is at least 3 months after the month in which such Long-Term Mode takes effect, and the first day of each April and October thereafter or, upon the receipt by the Trustee of a Favorable Opinion of Special Counsel, any other six-month interval chosen by the Authority (beginning with the first such day which is at least three months after the Mode Change Date) and, with respect to a Term Rate Mode, the final day of the current Interest Period if other than a regular six-month interval; (iv) (without duplication as to any Interest Payment Date listed above) any Mode Change Date, other than a change between a Daily Mode and a Weekly Mode, and each Maturity Date; and (v) with respect to any Liquidity Provider Certificates, the day set forth in the applicable Reimbursement Agreement.

"Interest Period" means, for the 2008 Certificates in a particular Mode, the period of time that the 2008 Certificates evidence interest at the rate (per annum) which becomes effective at the beginning of such period, and will include a Daily Rate Period, a Weekly Rate Period, a Flexible Rate Period, a Term Rate Period, and a Fixed Rate Period. Notwithstanding the preceding sentence, regardless of Mode, so long as any 2008 Certificate is a Liquidity Provider Certificate, the Interest Period will be determined in accordance with the applicable Liquidity Facility or the applicable Reimbursement Agreement.

“Liquidity Facility” means, as of any time, the Initial Liquidity Facility, the Replacement Liquidity Facility or an Alternate Liquidity Facility, as applicable, which provides for the payment of the purchase price of the 2008 Certificates upon the tender thereof in the event remarketing proceeds are insufficient therefor.

“Liquidity Facility Provider” means, with respect to the Replacement Liquidity Facility, the Bank, and with respect to any Alternate Liquidity Facility for the 2008 Certificates, a bank, insurance company, pension fund or other financial institution acceptable to the 2008 Certificate Insurer, including the Bank.

“Liquidity Provider Certificates” means any 2008 Certificates purchased by a Liquidity Facility Provider with funds drawn on or advanced under the Liquidity Facility provided by such Liquidity Facility Provider.

“Mandatory Purchase Date” means: (i) with respect to a Flexible Rate Certificate, the first Business Day following the last day of each Flexible Rate Period with respect to such Flexible Rate Certificate; (ii) for the 2008 Certificates in a Term Rate Mode, the first Business Day following the last day of each Term Rate Period for such 2008 Certificates; (iii) any Mode Change Date; (iv) any Substitution Date; (v) the fifth Business Day prior to an Expiration Date; (vi) the date specified by the Trustee following the occurrence of an event of default with respect to the Liquidity Facility or under the related Reimbursement Agreement which requires or gives the Liquidity Facility Provider the option to terminate the Liquidity Facility upon notice and requires that all Outstanding 2008 Certificates secured by such Liquidity Facility be tendered for purchase, which date will be a Business Day not less than 7 days after the Trustee’s receipt of notice of such event of default from the applicable Liquidity Facility Provider and in no event later than the Business Day preceding the termination date specified in the notice of event of default delivered to the Trustee by such Liquidity Facility Provider; (vii) for the 2008 Certificates in a Daily Mode or a Weekly Mode, any Business Day specified by the Authority in a notice delivered to the Trustee and consented to by the Liquidity Facility Provider, which Mandatory Purchase Date will be not less than twenty (20) days after the Trustee’s receipt of such notice from the Authority, and (viii) the Business Day prior to the Cancellation Date.

“Master Contract” means that certain Master Installment Purchase Contract, executed and entered into as a November 1, 1997, by and between the City and the Authority, as the same may be amended or supplemented from time to time.

“Maturity Date” means, with respect to the 2008 Certificates, the maturity date specified for the 2008 Certificates in the Trust Agreement or, if Serial Certificates or more than one Term Certificates are established for the 2008 Certificates pursuant to the Trust Agreement upon a change of the 2008 Certificates to a Fixed Rate Mode, the maturity dates established for such Serial Certificates or Term Certificates.

“Maximum Rate” or “Maximum Interest Rate” means, with respect to all 2008 Certificates other than Liquidity Provider Certificates, a rate of interest of 12% per annum, and with respect to Liquidity Provider Certificates, such rate not greater than 25% as is provided for in the applicable Liquidity Facility; provided, however, that such rate will not in any event exceed the highest rate then permitted by law.

“Mode” means, as the context may require, the Daily Mode, the Weekly Mode, the Flexible Mode, the Term Rate Mode, or the Fixed Rate Mode.

“Mode Change Date” means with respect to the 2008 Certificates in a particular Mode, the day on which another Mode for the 2008 Certificates begins.

“Moody’s” means Moody’s Investors Service Inc., a corporation duly organized and existing under and by virtue of the laws of the State of Delaware, and its successors or assigns, except that if such corporation will be dissolved or liquidated or will no longer perform the services of a municipal securities rating agency, then “Moody’s” will be deemed to refer to any other nationally recognized municipal securities rating agency selected by the Authority.

“1997 Certificates” means the \$25,585,000 Refunding Revenue Certificates of Participation (1997 Water Utility System Refinancing Project), evidencing and representing and proportionate interests of the owners thereof in the 1997 Payments to be made by the City.

“1997 Payments” means the installment payments required to be made by the City to the Authority under and pursuant to the 1997 Supplemental Contract.

“1997 Supplemental Contract” means the 1997 Supplemental Installment Purchase Contract, executed and entered into as of November 1, 1997, by and between the City and the Authority, supplementing the Master Contract.

“1997 Trust Agreement” means that certain Trust Agreement, dated as of November 1, 1997, by and between the Authority and State Street Bank and Trust Company, N.A., which has been succeeded by The Bank of New York Trust Company, N.A., as trustee, pursuant to which there was executed and delivered the 1997 Certificates.

“Notice Parties” means the Authority, the City, the Trustee, the Credit Enhancement Provider, if any, the Liquidity Facility Provider, if any, the Remarketing Agent, if any, and the Fixed Rate Remarketing Agent, if any.

“Opinion of Counsel” means a written opinion of counsel of recognized standing in the field of law being addressed in such opinion retained the Authority.

“Outstanding” when used as of any particular time with reference to 2008 Certificates, means (subject to the provisions of the Trust Agreement) all 2008 Certificates except (1) 2008 Certificates theretofore cancelled by the Trustee or surrendered to the Trustee for cancellation; (2) 2008 Certificates paid or deemed to have been paid within the meaning of the Trust Agreement; and (3) 2008 Certificates in lieu of or in substitution for which other 2008 Certificates will have been executed and delivered by the Trustee pursuant to the Trust Agreement.

“Owner” means any person who will be the registered owner of any Outstanding 2008 Certificate.

“Parity Reserve Fund” means the fund by that name continued pursuant to the Trust Agreement.

“Payment Agreement Payments” has the meaning given such term in the Master Contract.

“Payment Agreement Receipts” has the meaning given such term in the Master Contract.

“Permitted Investments” means any of the following obligations if and to the extent then permitted by law:

- (1) Federal Securities;
- (2) Obligations issued by the Resolution Funding Corporation and the Student Loan Marketing Association, or obligations, participations, or other instruments of or issued by, or fully guaranteed as to interest and principal by, the Government National Mortgage Association (excluding stripped mortgage backed securities which are valued at greater than par on the unpaid principal);
- (3) Bills of exchange or time drafts drawn on and accepted by a commercial bank (including the Trustee or any of its affiliates), otherwise known as bankers acceptances, which are eligible for purchase by the Federal Reserve System and which are drawn on any bank the short-term obligations of which are rated in the highest letter and numerical rating category as provided by Moody's and by S&P; provided, that purchases of eligible bankers acceptances may not exceed 270 days' maturity;
- (4) Commercial paper of "prime" quality of the highest ranking or of the highest letter and numerical rating category as provided by Moody's and by S&P, which commercial paper is limited to issuing corporations that are organized and operating within the United States of America and that have total assets in excess of \$500,000,000 and that have an "A1" or higher rating for the issuer's unsecured debentures, other than commercial paper, as provided by Moody's and by S&P; provided, that purchases of eligible commercial paper may not exceed 180 days' maturity nor represent more than 10% of the outstanding commercial paper of an issuing corporation;
- (5) Non-negotiable certificates of deposit issued by a state or national bank (including the Trustee or any of its affiliates) that have maturities of not more than 365 days or deposit accounts with a state or national bank and that are fully insured by the Federal Deposit Insurance Corporation or the short-term obligations of which state or national bank are rated no lower than "A1" by Moody's and "A+" by S&P;
- (6) Any repurchase agreement of any securities enumerated in subdivisions (1) and (2) with any state or national bank (including the Trustee or any of its affiliates) or government bond dealer reporting to, trading with, and recognized as a primary dealer by the Federal Reserve Bank of New York, which agreement is either (A) with any institution which has debt rated no lower than "A1" by Moody's and "A+" by S&P or whose commercial paper is rated no lower than "P-1" by Moody's and no lower than "A-1" by S&P; (B) with any corporation or other entity that falls under the jurisdiction of the Federal Bankruptcy Code; provided, that (a) the term of such repurchase agreement is less than one (1) year or due on demand; (b) the Trustee or a third party acting solely as agent for the Trustee has possession of the collateral; (c) the market value of the collateral (as determined at least once in every 14 days) exceeds the principal amount of the repurchase agreement plus accrued interest and the market value of the collateral is maintained at levels acceptable to Moody's and to S&P; (d) failure to maintain the requisite collateral levels will require the Trustee to liquidate the collateral immediately; and (e) the repurchase agreement securities are free and clear of any third-party lien or claim; or (C) with financial institutions insured by the Federal Deposit Insurance Corporation or any broker-dealer with "retail customers" which falls under the jurisdiction of the Securities Investors Protection Corporation; provided, that: (a) the market value of the collateral (as determined at least once in every 14 days) exceeds the principal amount of the repurchase agreement plus accrued interest and the market value of the collateral is maintained at levels acceptable to Moody's and to S&P; (b) the

Trustee or a third party acting solely as agent for the Trustee has possession of the collateral; (c) the Trustee has a perfected first priority security interest in the collateral; (d) the collateral is free and clear of third-party liens and in the case of a Securities Investors Protection Corporation broker was not acquired pursuant to a repurchase agreement or reverse repurchase agreement; and (e) failure to maintain the requisite collateral percentage will require the Trustee to liquidate the collateral immediately;

(7) Certificates, notes, warrants, bonds or other evidence of indebtedness of the State or any local agencies therein which are rated in the highest short-term rating category or within one of the three highest long-term rating categories by Moody's and by S&P (excluding securities that do not have a fixed par value and/or whose terms do not promise a fixed dollar amount at maturity or call date);

(8) For amounts less than \$100,000, interest-bearing demand or time deposits (including certificates of deposit) in a nationally or state-chartered bank fully insured by the Federal Deposit Insurance Corporation, including the Trustee or any affiliate thereof, and of which an aggregate total of \$100,000 is not exceeded in any one financial institution;

(9) Investments in units of a money-market fund portfolio that is rated in the highest letter and numerical rating category by Moody's and by S&P (including funds for which the Trustee, its affiliates or subsidiaries provide investment advisory or other management services) and that is composed of obligations guaranteed by the full faith and credit of the United States of America or repurchase agreements collateralized by such obligations;

(10) A guaranteed investment contract with a financial institution or insurance company (or guaranteed by a financial institution or insurance company) which has at the date of execution thereof an outstanding issue of unsecured, uninsured and unguaranteed debt obligations or a claims paying ability rated within the two highest rating categories of any Rating Agency;

(11) Other investments approved in writing by the 2008 Certificate Insurer (or if a Control Event has occurred, the Bank); and

(12) The Local Agency Investment Fund, the California Asset Management Program, or similar pooled fund operated by or on behalf of the State and which is authorized to accept investments by or on behalf of the Authority of the moneys held by the Trustee in any of the accounts or funds established pursuant to the Trust Agreement to the extent deposits and withdrawals may be made by the Trustee directly.

"Person" will mean an individual, a corporation, an association, a joint venture, a partnership, a trust, an unincorporated organization or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"Prepayment Date" means the date fixed for prepayment of any 2008 Certificate in any notice of prepayment given in accordance with the terms of the Trust Agreement.

"Purchase Date" means any Mandatory Purchase Date.

“Purchase Price” means an amount equal to the principal amount of the 2008 Certificates purchased on any Purchase Date, plus accrued interest to such Purchase Date (unless such Purchase Date is also an Interest Payment Date, in which case the Purchase Price will not include accrued interest, which will be paid in the normal course).

“Rating Agencies” means Moody’s and S&P, and their respective successors or assigns, or any other nationally recognized securities rating agency or agencies rating the 2008 Certificates at the request of the City.

“Rating Confirmation Notice” means a written notice from the Rating Agencies then rating the 2008 Certificates, confirming that the rating on the 2008 Certificates (without giving effect to any Liquidity Facility) will not be lowered or withdrawn (other than a withdrawal of a short-term rating upon a change to a Fixed Rate Mode) as a result of the action proposed to be taken.

“Record Date” means (i) with respect to the 2008 Certificates in a Short-Term Mode, the last Business Day before each Interest Payment Date; and (ii) with respect to the 2008 Certificates in a Long-Term Mode, the 15th day (whether or not a Business Day) of the month next preceding each Interest Payment Date.

“Reimbursement Agreement” means any reimbursement agreement, credit agreement, line of credit agreement, standby purchase agreement or other agreement, between a Credit Enhancement Provider or a Liquidity Facility Provider, as applicable, and the Authority and/or the City, as the same may be amended from time to time pursuant to its terms, including the Reimbursement Agreement, dated as of July 1, 2011, by and between the City and the Bank.

“Remarketing Agent” means each Person selected by the Authority to act as remarketing agent for the 2008 Certificates pursuant to the Trust Agreement and approved by the 2008 Certificate Insurer (or, if a Control Event has occurred, the Bank).

“Replacement Liquidity Facility” means the irrevocable, direct-pay letter of credit issued by the Bank with respect to the 2008 Certificates on the Substitution Date.

“Reserve Funding Instruments” will have the meaning given such term in the Trust Agreement, including the 2008 Parity Reserve Fund Insurance Policy.

“Reserve Fund Requirement” will have the meaning ascribed thereto in the Contract.

“S&P” means Standard & Poor’s Ratings Services, a division of The McGraw Hill Company, and its successors or assigns, except that if such entity will be dissolved or liquidated or will no longer perform the services of a municipal securities rating agency, then “S&P” will be deemed to refer to any other nationally recognized municipal securities rating agency selected by the Authority.

“Securities Depositories” means: The Depository Trust Company, 55 Water Street, 50<sup>th</sup> Floor, New York, New York 10041-0099, Attention: Call Notification Department, Fax: (212) 855-7232; or, in accordance with then-current guidelines of the Securities and Exchange Commission, such other securities depositories as the Authority may designate in a Certificate of the Authority to the Trustee.

“Serial Certificate” means any 2008 Certificate not subject to mandatory prepayment from Sinking Fund Payments.

“Sinking Fund Payments” means the payments required under the Trust Agreement to be deposited in the 2008 Sinking Fund Subaccount.

“Special Counsel” means any firm of nationally recognized municipal bond attorneys selected by the Authority and experienced in the issuance of municipal bonds and matters relating to the exclusion of the interest thereon from gross income for federal income tax purposes.

“State” means the State of California.

“Subrogated Certificate” means any Certificate of Participation with respect to which, pursuant to the Trust Agreement, the Bank or other credit enhancement provider, to the extent it has paid the principal of such Certificate of Participation from a drawing under the Replacement Liquidity Facility or other credit enhancement, has become subrogated to, and the assignee of, the rights to receive payment of such principal from the City pursuant to the Trust Agreement and has become the Owner of such Certificate of Participation.

“Substitution Date” means the date on which an Alternate Liquidity Facility is substituted for the Liquidity Facility then in effect.

“Supplemental Contract” will have the meaning given such term in the Contract.

“Supplemental Trust Agreement” means any trust agreement then in full force and effect which has been duly executed and delivered by the Authority and the Trustee amendatory of or supplemental to the Trust Agreement; but only if and to the extent that such Supplemental Trust Agreement is specifically authorized under the Trust Agreement.

“Tax Certificate” means, collectively, the Tax Certificate concerning certain matters pertaining to the use and investment of proceeds of the 2008 Certificates, executed and delivered by the City on the date of delivery of the 2008 Certificates, including any and all exhibits attached thereto.

“Term Certificates” means the 2008 Certificates subject to mandatory prepayment from Sinking Fund Payments.

“Term Rate” means the per annum interest rate for the 2008 Certificates in the Term Rate Mode determined pursuant to the Trust Agreement.

“Term Rate Mode” means the Mode during which the 2008 Certificates evidence interest at a Term Rate.

“Term Rate Period” means the period from (and including) the Mode Change Date or the date of initial conversion of the 2008 Certificates to a Term Rate Mode, as applicable, to (but excluding) the last day of the first period that 2008 Certificates will be in the Term Rate Mode as established by the Authority pursuant to the Trust Agreement and, thereafter, the period from (and including) the beginning date of each successive Interest Rate Period selected for the 2008 Certificates by the Authority pursuant to the Trust Agreement while the 2008 Certificates are in the Term Rate Mode to (but excluding) the commencement date of the next succeeding Interest Period, including another Term Rate Period. Except as otherwise provided in the Trust Agreement, an Interest Period for the 2008 Certificates in the Term Rate Mode must be at least 180 days in length.

“Trust Agreement” means that certain Trust Agreement, dated as of May 1, 2008, between the Authority and the Trustee, as originally executed and as it may from time to time be amended or

supplemented by all Supplemental Trust Agreements executed pursuant to the provisions of the Trust Agreement.

“Trustee” means The Bank of New York Mellon Trust Company, N.A., or any other association or corporation which may at any time be substituted in its place as provided in the Trust Agreement.

“2008 Certificate Insurance Policy” means the financial guaranty insurance policy issued by the 2008 Certificate Insurer guaranteeing the scheduled payment of principal of and interest evidenced and represented by the 2008 Certificates.

“2008 Certificate Insurer” means Assured Guaranty Corp., its successors and assigns.

“2008 Debt Service Fund” means the fund by that name established pursuant to the Trust Agreement.

“2008 Interest Account” means the account by that name established within the 2008 Debt Service Fund pursuant to the Trust Agreement.

“2008 Interest Rate Swap Agreement” has the meaning given such term in the 2008 Supplemental Contract.

“2008 Liquidity Facility Payment Account” means the account by that name established pursuant to the Trust Agreement.

“2008 Parity Reserve Fund Insurance Policy” means the reserve fund financial guaranty insurance policy issued by the 2008 Certificate Insurer and deposited in the Parity Reserve Fund pursuant to the Trust Agreement.

“2008 Payments” means the installment payments of interest, principal, and prepayment premium, if any, payable by the City under and pursuant to the 2008 Supplemental Contract.

“2008 Prepayment Subaccount” means the subaccount by that name established within the 2008 Principal Account of the 2008 Debt Service Fund pursuant to the Trust Agreement.

“2008 Principal Account” means the account by that name established within the 2008 Debt Service Fund pursuant to the Trust Agreement.

“2008 Project” means the refinancing of improvements to the Water Utility System described in Exhibit A to the 2008 Supplemental Contract.

“2008 Sinking Fund Subaccount” means the subaccount by that name within the 2008 Principal Account of the 2008 Debt Service Fund established pursuant to the Trust Agreement.

“2008 Supplemental Contract” means that certain 2008 Supplemental Installment Purchase Contract, dated as of May 1, 2008, by and between the City and the Authority, supplementing the Master Contract.

“Weekly Mode” means the Mode during which the 2008 Certificates evidence interest at the Weekly Rate.

“Weekly Rate” means the per annum interest rate with respect to the 2008 Certificates in the Weekly Mode determined pursuant to the Trust Agreement.

“Weekly Rate Period” means the period during which the 2008 Certificates evidence interest at a Weekly Rate, which will be the period commencing on Thursday of each week to and including Wednesday of the following week, except the first Weekly Rate Period which will be from the Mode Change Date for the 2008 Certificates to and including the Wednesday of the following week and the last Weekly Rate Period which will be from and including the Thursday of the week prior to the Mode Change Date to and including the day next preceding the Mode Change Date.

“Written Request of the Authority” means an instrument in writing signed by the Auditor and Treasurer of the Authority or by any other officer of the Authority duly authorized by the Authority for that purpose.

### **Equal Security**

In consideration of the acceptance of the 2008 Certificates by the Owners thereof, the Trust Agreement will be deemed to be and will constitute a contract between the Authority and the Owners from time to time of all 2008 Certificates authorized, executed, and delivered under the Trust Agreement and then Outstanding to secure the full and final payment of the interest, principal, and prepayment premiums, if any, evidenced and represented by the 2008 Certificates which may from time to time be authorized, executed, issued and delivered under the Trust Agreement, subject to the agreements, conditions, covenants and provisions contained in the Trust Agreement; and all agreements and covenants set forth in the Trust Agreement to be performed by or on behalf of the Trustee will be for the equal and proportionate benefit, protection and security of all Owners without distinction, preference or priority as to security or otherwise of any 2008 Certificates over any other 2008 Certificates by reason of the number or date thereof or the time of authorization, sale, execution, or delivery thereof or for any cause whatsoever, except as expressly provided in the Trust Agreement or therein.

### **2008 Payments; 2008 Project**

2008 Payments Held in Trust. The 2008 Payments will be held in trust by the Trustee for the benefit of the Owners from time to time of the 2008 Certificates and each Credit Enhancement Provider, but will nonetheless be disbursed, allocated and applied solely for the uses and purposes provided in the Trust Agreement.

Deposit of 2008 Payments. The Trustee agrees to establish, maintain and hold in trust a separate fund designated as the 2008 Debt Service Fund, for so long as any 2008 Certificates will be Outstanding under the Trust Agreement. All 2008 Payments (except as otherwise provided) received by the Trustee will be immediately deposited in the 2008 Debt Service Fund and will be disbursed and applied only as provided in the Trust Agreement.

Establishment and Maintenance of Accounts for Use of Money in the 2008 Debt Service Fund. All money in the 2008 Debt Service Fund will be set aside by the Trustee in the following respective special accounts within the 2008 Debt Service Fund (each of which is created by the Trust Agreement and each of which the Trustee agrees and covenants to maintain pursuant to the Trust Agreement) in the following order of priority:

- (a) 2008 Interest Account (with a 2008 Fees Subaccount therein), and
- (b) 2008 Principal Account (with a 2008 Prepayment Subaccount and a 2008 Sinking Fund Subaccount therein).

All money in each of such accounts and subaccounts will be held in trust by the Trustee for the benefit of the Owners and each Credit Enhancement Provider and will be applied, used and withdrawn only for the purposes authorized in the Trust Agreement.

(a) 2008 Interest Account. On the Delivery Date, the Trustee will deposit in the 2008 Interest Account any Payment Agreement Receipts relating to the 2008 Interest Rate Swap Agreement which the City has directed under the 2008 Interest Rate Swap Agreement to be transferred to the Trustee for deposit in the 2008 Interest Account and any amounts transferred to the Trustee pursuant to the 2008 Supplemental Contract for the payment of payments due under the 2008 Interest Rate Swap Agreement. On the Business Day immediately preceding each Interest Payment Date, the Trustee will set aside from the 2008 Debt Service Fund and deposit in the 2008 Interest Account that amount of money which is equal to the amount of interest evidenced and represented by the 2008 Certificates becoming due and payable on each such Interest Payment Date, unless such amounts are required to be used to reimburse the Bank pursuant to clause (c) below. The Trustee will also apply amounts on deposit in the 2008 Fees Subaccount to pay on behalf of the City, the Payment Agreement Payments required to be paid under the 2008 Interest Rate Swap Agreement and to pay the Remarketing Agent fees as the same will become due on each due date therefor until such 2008 Fees Subaccount will be depleted (expected to be on or about November 29, 2008). Investment earnings on amounts on deposit in the 2008 Fees Subaccount will be transferred to the City for deposit in the Revenue Fund.

No deposit need be made in the 2008 Interest Account if the amount contained therein (exclusive of amounts transferred for the payment of amounts due under the 2008 Interest Rate Swap Agreement) is at least equal to the aggregate amount of interest evidenced and represented by the 2008 Certificates becoming due and payable on such Interest Payment Date.

Except as otherwise provided in the Trust Agreement, all money in the 2008 Interest Account will be used and withdrawn by the Trustee solely for the purpose of paying the interest (including accrued interest evidenced and represented by any 2008 Certificates purchased or prepaid prior to their respective Certificate Payment Date) with respect to the 2008 Certificates as it will become due and payable, or for reimbursing the Bank and paying the Payment Agreement Payments due under the 2008 Interest Rate Swap Agreement as they will become due and payable.

(b) 2008 Principal Account. On the Business Day immediately preceding each October 1, commencing on October 1, 2008, the Trustee will set aside from the 2008 Debt Service Fund and deposit in the 2008 Principal Subaccount an amount of money equal to the principal amount evidenced and represented by the Outstanding Serial Certificates with a Certificate Payment Date of such October 1, and in the 2008 Sinking Fund Subaccount in the 2008 Principal Account the amount of all Sinking Fund Payments required to be made on such October 1.

Amounts to be applied to the optional prepayment of the principal component of the 2008 Certificates pursuant to the Trust Agreement will be deposited in the 2008 Prepayment Subaccount of the 2008 Principal Account.

No deposit need be made in the 2008 Principal Account if the amount contained therein is at least equal to the aggregate amount of the principal evidenced and represented by the Outstanding Serial Certificates with a Certificate Payment Date of such October 1 and the amount contained in the 2008 Sinking Fund Subaccount therein is at least equal to the aggregate amount of all Sinking Fund Payments required to be made on such October 1.

All money in the 2008 Principal Account will be used and withdrawn by the Trustee solely for the purpose of paying the principal evidenced and represented by the Serial Certificates as they will become due and payable, whether at their respective Certificate Payment Dates or on prior prepayment, and all money in the 2008 Sinking Fund Subaccount of the 2008 Principal Account will be used and withdrawn by the Trustee only to purchase or to prepay or to pay Term Certificates, and with respect to the 2008 Sinking Fund Subaccount, on each Sinking Fund Payment date, the Trustee will apply the Sinking Fund Payment required on that date to the prepayment (or payment at Certificate Payment Date, as the case may be) of the Term Certificates upon the notice and in the manner provided in the Trust Agreement; provided, that at any time prior to giving such notice of such prepayment, the Trustee may, upon the Written Request of the Authority and receipt of moneys sufficient therefor, purchase for cancellation Term Certificates in accordance with the Trust Agreement, and provided further that so long as the Liquidity Facility is in place, amounts in the 2008 Principal Account will be used as provided in clause (c) below.

(c) All monies in the 2008 Debt Service Fund, including the 2008 Interest Account and the 2008 Principal Account, will be used to reimburse any draws on the Liquidity Facility pursuant to the Trust Agreement.

Parity Reserve Fund. The Parity Reserve Fund created pursuant to the 1997 Trust Agreement is continued by the Trust Agreement. Pursuant to the Trust Agreement, the Trustee agrees and covenants to maintain the Parity Reserve Fund so long as the Contract has not been discharged in accordance with its terms or any 2008 Certificates remain Outstanding under the Trust Agreement. Amounts on deposit in the Parity Reserve Fund are pledged to the payment of the 1997 Certificates, the 2008 Certificates (including Liquidity Provider Certificates and Subrogated Certificates) and any other obligations hereafter issued in connection with a Supplemental Contract and will be applied only for such purposes as provided in the Trust Agreement. The Trustee will deposit in the Parity Reserve Fund from the proceeds of the 2008 Certificates, the amount specified in the Trust Agreement, such amount being sufficient to cause the balance on deposit in or credited to the Parity Reserve Fund, to be equal to the Reserve Fund Requirement upon delivery of the 2008 Certificates. The Trustee will deposit in the Parity Reserve Fund such other amounts transferred to the Trustee by the City pursuant to the Contract, as directed by the Authority in a Written Request of the Authority. Moneys on deposit in the Parity Reserve Fund will be transferred by the Trustee to the 2008 Debt Service Fund to pay principal and interest evidenced and represented by the 2008 Certificates on any Interest Payment Date or to reimburse the Liquidity Facility Provider for any unreimbursed drawing made under the Liquidity Facility to pay such principal and interest on any such Interest Payment Date in the event amounts on deposit therein are insufficient for such purposes. The Trustee will also, from such amounts on deposit in the Parity Reserve Fund, transfer or cause to be transferred to any applicable debt service fund established under the 1997 Trust Agreement and under any other trust agreement under which any obligations are issued in connection with a Supplemental Contract, without preference or priority between transfers made pursuant to this sentence and the preceding sentence, and in the event of any insufficiency of such moneys ratably without discrimination or preference, that sum or sums, if any, equal to the amount required to be deposited therein pursuant to such trust agreement under which any obligations are issued in connection with a Supplemental Contract. All investments in the Parity Reserve Fund will (notwithstanding anything in the 1997 Trust Agreement to the contrary) be valued on or before October 1 of each year at the lesser of the cost or market value thereof. Following such valuation, any moneys on deposit in the Parity Reserve Fund representing an excess of the Reserve Fund Requirement will be transferred by the Trustee to the City for deposit in the Revenue Fund. The Trustee may create such subaccounts in the Parity Reserve Fund as may be necessary or convenient for the purposes of the Trust Agreement.

The Reserve Fund Requirement may be provided by one or more surety bonds, insurance policies, or letters of credit as described in the definition of Reserve Fund Requirement (“Reserve Funding Instruments”) set forth in the Contract.

Notwithstanding anything to the contrary contained in the Trust Agreement, at any time one or more Reserve Funding Instruments are on deposit in the Parity Reserve Fund, the Trustee will: (i) withdraw and use all cash, if any, on deposit in the Parity Reserve Fund prior to using and withdrawing any amounts derived from payments under any Reserve Funding Instruments; and (ii) draw on all Reserve Funding Instruments on a pro rata basis based on the draw limit of each Reserve Funding Instrument. Amounts received by the Trustee from the City pursuant to the Master Contract as a replenishment of amounts withdrawn from the Parity Reserve Fund will be applied (i) first on a pro rata basis to reimburse draws on any Reserve Funding Instruments and (ii) to replenish cash withdrawn from the Parity Reserve Fund.

In the event the 2008 Certificate Insurance Policy is cancelled in accordance with the Reimbursement Agreement between the Bank and the City, any Reserve Funding Instrument provided by the 2008 Certificate Insurer will be cancelled concurrently therewith.

Establishment and Application of Costs of Issuance Fund. Pursuant to the Trust Agreement, the Trustee agrees to establish, maintain and hold in trust a separate fund designated as the Costs of Issuance Fund, which fund is created by the Trust Agreement and which fund the Authority agrees to maintain with the Trustee until November 29, 2008. The Trustee will deposit to the Costs of Issuance Fund the amounts specified in the Trust Agreement. All money in the Costs of Issuance Fund will be used and withdrawn by the Trustee to pay the Costs of Issuance relating to the 2008 Certificates upon receipt of a Written Request of the Authority filed with the Trustee, each of which will be sequentially numbered and will state the person to whom payment is to be made, the amount to be paid, the purpose for which the obligation was incurred and that such payment is a proper charge against said fund. On November 29, 2008, or upon the earlier Written Request of the Authority, any remaining balance in the Costs of Issuance Fund will be transferred to the City for deposit in the 2008 Debt Service Fund.

Deposit and Investments of Money in Accounts and Funds. All money held by the Trustee in any of the accounts or funds established pursuant to the Trust Agreement will be invested in Permitted Investments at the Written Request of the Authority filed with the Trustee which such Permitted Investments will, as nearly as practicable, mature on or before the dates on which such money is anticipated to be needed for disbursement under the Trust Agreement, and the Trustee will have no liability or responsibility for any loss resulting from any investment made in accordance with the Trust Agreement; provided, that if no such Written Request is received by the Trustee, the Trustee will invest such money in those Permitted Investments described in clause (9) of the definition thereof provided, however, that any such investment will be made by the Trustee only if, prior to the date on which such investment is to be made, the Trustee will have received a Written Request of the Authority specifying a specific money market fund and, if no such Written Request of the Authority is so received, the Trustee will hold such moneys uninvested. Except as otherwise provided in the Trust Agreement with respect to the Parity Reserve Fund, all interest or profits received on any money so invested will be deposited in the 2008 Debt Service Fund.

The Authority acknowledges that to the extent regulations of the Comptroller of the Currency or other applicable regulatory entity grant the Authority the right to receive brokerage confirmations of security transactions as they occur, the Authority specifically waives receipt of such confirmations to the extent permitted by law. The Trustee will furnish the Authority periodic cash transaction statements which include detail for all investment transactions made by the Trustee under the Trust Agreement.

The Trustee or any of its affiliates may act as principal or agent, sponsor, advisor or manager in connection with any investments made by the Trustee under the Trust Agreement. For investment purposes, the Trustee may commingle the funds and accounts established under the Trust Agreement, but will account for each separately.

The Trustee will not be liable for any loss from any Permitted Investment acquired, held, or disposed of at the written request of the Authority. Any Permitted Investments that are registered securities will be registered in the name of the Trustee.

Assignment to Trustee; Enforcement of Obligations.

(a) Pursuant to the Trust Agreement, the Authority transfers, assigns and sets over to the Trustee all of the 2008 Payments and any and all rights and privileges it has under the Contract, including, without limitation, the right to collect and receive directly all of the 2008 Payments, and any 2008 Payments collected or received by the Authority will be deemed to be held, and to have been collected or received, by the Authority as the agent of the Trustee, and will forthwith be paid by the Authority to the Trustee. The Trustee also will, subject to the provisions of the Trust Agreement, take all steps, actions and proceedings required to be taken as provided in any Opinion of Counsel delivered to it, reasonably necessary to maintain in force for the benefit of the Owners of the 2008 Certificates and each Credit Enhancement Provider the Trustee's rights in and priority to the following security granted to it for the payment of the 2008 Certificates: the Trustee's rights as assignee of the 2008 Payments under the Contract and as beneficiary of any other rights to security for the 2008 Certificates which the Trustee may receive in the future.

(b) The Trustee may, in performing the obligations set out above, rely and will be protected in acting or refraining from acting upon an Opinion of Counsel furnished by the City.

2008 Liquidity Facility Payment Account; Payment of Principal and Interest and Mandatory Purchase Price of the 2008 Certificates. The Trustee will establish and maintain a separate fund known as the "2008 Liquidity Facility Payment Account" and will, (i) in each Business Day preceding each Interest Payment Date of the 2008 Certificates, before 5:00 P.M. New York City time on such day, draw on the Liquidity Facility in accordance with the terms thereof so as to receive by 1:00 P.M. New York City time on said Interest Payment Date, an amount, in immediately available funds, equal to the amount of interest and principal, if any (including any Sinking Fund Payment) due on such date, payable with respect to the 2008 Certificates on such Interest Payment Date, and (ii) on each Mandatory Purchase Date, before 12:00 P.M. New York City time draw on the Liquidity Facility in accordance with the terms thereof so as to receive by 3:00 P.M. New York City time on said Interest Payment Date, an amount, in immediately available funds, equal to the amount of the interest and principal due on such date, payable with respect to the 2008 Certificates. All monies held in the 2008 Liquidity Facility Account will be held uninvested in trust for the benefit of the Owners of the 2008 Certificates.

Funds for the payment of interest and principal, if any, payable with respect to the 2008 Certificates on such Interest Payment Date or Mandatory Purchase Date will be derived from the immediately available funds on deposit in the 2008 Liquidity Facility Payment Account received from the Bank from draws under the Liquidity Facility, and not from amounts on deposit in the 2008 Interest Account, the 2008 Principal Account or any other account established under the Trust Agreement. The Liquidity Facility Provider will be reimbursed from such draws from amounts on deposit in the 2008 Interest Account, the 2008 Principal Account or, in the case of a Mandatory Purchase Date, amounts in the Remarketing Account, if any.

If the Liquidity Facility Provider makes a payment under the Liquidity Facility and is not reimbursed by the Trustee from amounts on deposit in the 2008 Interest Account or 2008 Principal Account or Parity Reserve Fund, its rights with respect to the 2008 Certificates so paid or interest thereon so paid will be as set forth in the Trust Agreement, including its rights to demand payment of such amounts under the 2008 Certificate Insurance Policy. If the Liquidity Facility Provider fails to pay under the Liquidity Facility upon the presentation of a proper draw request by the Trustee and the City has not defaulted under the related Reimbursement Agreement, to the extent available, amounts on deposit in the 2008 Interest Account, the 2008 Principal Account and the Parity Reserve Fund will be applied to the payment of regularly scheduled interest and principal payable on the applicable Interest Payment Date with respect to the 2008 Certificates.

### **Covenants of the Authority and the Trustee**

Compliance with Trust Agreement. The Trustee will not execute or deliver any 2008 Certificates in any manner other than in accordance with the provisions of the Trust Agreement; and the Authority will not suffer or permit any default by it to occur under the Trust Agreement, but will faithfully comply with, keep, observe and perform all the agreements and covenants to be observed or performed by it contained in the Trust Agreement and in the 2008 Certificates.

Observance of Laws and Regulations. The Authority and the Trustee will faithfully comply with, keep, observe and perform all valid and lawful obligations or regulations now or hereafter imposed on them by contract, or prescribed by any law of the United States of America or of the State of California, or by any officer, board or commission having jurisdiction or control, as a condition of the continued enjoyment of each and every franchise, right or privilege now owned or hereafter acquired by them, including their right to exist and carry on their respective businesses, to the end that such franchises, rights and privileges will be maintained and preserved and will not become abandoned, forfeited or in any manner impaired.

Accounting Records and Reports. The Trustee will keep or cause to be kept proper books of record and accounts in which complete and correct entries will be made of all transactions made by the Trustee relating to the receipts, disbursements, allocation and application of the 2008 Payments and the proceeds of the 2008 Certificates, and such books will be available for inspection by the Authority, at reasonable hours and under reasonable conditions. Not more than 180 days after the close of each Fiscal Year, the Trustee will furnish or cause to be furnished to the Authority and the 2008 Certificate Insurer a complete financial statement covering receipts, disbursements, allocation and application of 2008 Payments received by the Trustee for such Fiscal Year. The Authority will keep or cause to be kept such information as required under the Tax Certificate.

Prosecution and Defense of Suits. The Authority will defend against every suit, action or proceeding at any time brought against the Trustee upon any claim to the extent arising out of the receipt, application or disbursement of any of the 2008 Payments and the proceeds of the 2008 Certificates or to the extent involving the failure of the Authority to fulfill its obligations under the Trust Agreement; provided that the Trustee or any affected Owner at its election may appear in and defend any such suit, action or proceeding. The Authority will indemnify and hold harmless the Trustee against any and all liability claimed or asserted by any person to the extent arising out of such failure by the Authority, and will indemnify and hold harmless the Trustee against any attorney's fees or other expenses which it may incur in connection with any litigation to which it may become a party by reason of its actions under the Trust Agreement, except for any loss, cost, damage or expense resulting from the active or passive negligence, willful misconduct or breach of duty by the Trustee. Notwithstanding any contrary provision of the Trust Agreement, this covenant will remain in full force and effect even though all 2008 Certificates secured by the Trust Agreement may have been fully paid and satisfied.

Amendments to Contract. Except for any Supplemental Contract delivered in accordance with the terms of the Contract, the Authority will not supplement, amend, modify or terminate any of the terms of the Contract, or consent to any such supplement, amendment, modification or termination, without the prior written consent of the Trustee, which such consent will be given only if (a) such supplement, amendment, modification or termination will not materially adversely affect the interests of the Owners or result in any material impairment of the security given for the payment of the 2008 Certificates, or (b) the Trustee first obtains the written consent of the Owners of a majority in aggregate principal amount evidenced and represented by the 2008 Certificates then Outstanding to such supplement, amendment, modification or termination; provided, that no such supplement, amendment, modification or termination will reduce the amount of 2008 Payments to be made to the Authority or the Trustee by the City pursuant to the Contract, or extend the time for making such 2008 Payments in any manner that would require the amendment of the Trust Agreement in any manner not in compliance with the Trust Agreement, or permit the creation of any lien prior to or on a parity with the lien created by the Trust Agreement on the 2008 Payments without the written consent of all of the Owners of the 2008 Certificates then Outstanding.

Recording and Filing. The Trustee upon receipt of a Written Request of the Authority, at the expense of the Authority, will file, record, register, renew, refile and rerecord all such documents, including financing statements (or continuation statements in connection therewith), all in such manner, at such times and in such places as may be required and to the extent permitted by law in order to fully perfect, preserve and protect the security of the Owners and the rights and interests of the Trustee; provided, however, that the Trustee will not be required to execute a special or general consent to service of process, or to qualify as a foreign corporation in connection with any such filing, recording, registration, refile or rerecording in any jurisdiction in which it is not now so subject.

Further Assurances. Whenever and so often as reasonably requested to do so by the Trustee or any Owner, the Authority will promptly execute and deliver or cause to be executed and delivered all such other and further assurances, documents or instruments, and promptly do or cause to be done all such other and further things as may be necessary or reasonably required in order to further and more fully vest in the Trustee and the Owners all rights, interests, powers, benefits, privileges and advantages conferred or intended to be conferred upon them by the Trust Agreement.

## **The Trustee**

The Trustee. The Bank of New York Trust Company, N.A., will serve as the Trustee for the purpose of receiving all money which the Authority is required to deposit with the Trustee under the Trust Agreement and for the purpose of allocating, applying and using such money as provided in the Trust Agreement and for the purpose of paying the interest and principal and prepayment premiums, if any, evidenced and represented by the 2008 Certificates presented for payment, and for the purpose of canceling all paid or prepaid 2008 Certificates as provided in the Trust Agreement. The Authority agrees that it will at all times maintain a Trustee having a corporate trust office in either San Francisco, California or Los Angeles, California.

The Authority may at any time, unless there exists any Event of Default as defined in the Trust Agreement, remove the Trustee initially appointed and any successor thereto and may appoint a successor or successors thereto by an instrument in writing; provided that any successor appointed under the Trust Agreement will be approved by the 2008 Certificate Insurer and will be a bank, national banking association with trust powers or trust company doing business and having a principal office in either San Francisco, California or Los Angeles, California, having (or if such bank, national banking association or trust company is a member of a bank holding company system, its bank holding company has) a combined capital (exclusive of borrowed capital) and surplus of at least \$50,000,000 and subject to supervision or examination by federal or state authority. If such bank, national banking association or

trust company publishes a report of condition at least annually, pursuant to law or to the requirements of any supervising or examining authority above referred to, then for the purpose of this provision the combined capital and surplus of such bank, national banking association or trust company will be deemed to be its combined capital and surplus as set forth in its most recent report of condition so published. The Trustee may at any time resign by giving written notice of such resignation to the Authority and by mailing to the Owners notice of such resignation. Upon receiving such notice of resignation, the Authority will promptly appoint a successor Trustee by an instrument in writing. Any removal or resignation of a Trustee and appointment of a successor Trustee will become effective only upon the acceptance of appointment by the successor Trustee. If, within 30 days after notice of the removal or resignation of the Trustee no successor Trustee will have been appointed and will have accepted such appointment, the removed or resigning Trustee may petition any court of competent jurisdiction for the appointment of a successor Trustee, which court may thereupon, after such notice, if any, as it may deem proper and prescribe and as may be required by law, appoint a successor Trustee having the qualifications required by the Trust Agreement. Any successor trustee will signify its acceptance of the duties under the Trust Agreement by an instrument in writing provided to the Authority and the Notice Parties.

Liability of the Trustee. The recitals of facts, agreements and covenants in the Trust Agreement and in the 2008 Certificates will be taken as recitals of facts, agreements and covenants of the Authority, and the Trustee assumes no responsibility for the correctness of the same or makes any representation as to the sufficiency or validity of the Trust Agreement or of the 2008 Certificates, or will incur any responsibility in respect thereof other than in connection with the rights or obligations assigned to or imposed upon it in the Trust Agreement, in the 2008 Certificates or in law or equity. The Trustee will not be liable in connection with the performance of its duties under the Trust Agreement except for its own active or passive negligence or willful misconduct.

The Trustee will not be liable for any error of judgment made in good faith by a responsible officer, unless it will be proved that the Trustee was negligent in ascertaining the pertinent facts.

The Trustee will not be liable with respect to any action taken or omitted to be taken by it in good faith in accordance with the direction of the Owners of not less than a majority in aggregate principal amount of the 2008 Certificates at the time Outstanding, relating to the time, method and place of conducting any proceeding for any remedy available to the Trustee, or exercising any trust or power conferred upon the Trustee under the Trust Agreement.

The Trustee will be under no obligation to exercise any of the rights or powers vested in it by the Trust Agreement at the request, order or direction of any of the Owners pursuant to the provisions of the Trust Agreement unless such Owners will have offered to the Trustee reasonable security or indemnity against the costs, expenses and liabilities that may be incurred therein or thereby. The Trustee has no obligation or liability to the Owners for the payment of interest, principal or prepayment premium, if any, evidenced and represented by the 2008 Certificates from its own funds; but rather the Trustee's obligations will be limited to the performance of its duties under the Trust Agreement.

The Trustee will not be deemed to have knowledge of any default under the Trust Agreement or default under the Contract unless and until it will have actual knowledge thereof or will have received written notice thereof at its Corporate Trust Office. Except as otherwise expressly provided in the Trust Agreement, the Trustee will not be bound to ascertain or inquire as to the performance or observance of any of the terms, conditions, covenants or agreements in the Trust Agreement or of any of the documents executed in connection with the 2008 Certificates or as to the existence of a default under the Trust Agreement.

The Trustee will not be considered in breach of or in default in its obligations under the Trust Agreement or progress in respect thereto in the event of enforced delay (“unavoidable delay”) in the performance of such obligations due to unforeseeable causes beyond its control and without its fault or negligence, including, but not limited to, acts of God or of the public enemy or terrorists, acts of a government, acts of the other party, fires, floods, epidemics, quarantine restrictions, strikes, freight embargoes, earthquakes, explosion, mob violence, riot, inability to procure or general sabotage or rationing of labor, equipment, facilities, sources of energy, material or supplies in the open market, litigation or arbitration involving a party or others relating to zoning or other governmental action or inaction pertaining to the project, malicious mischief, condemnation, and unusually severe weather or delays of suppliers or subcontractors due to such causes or any similar event and/or occurrences beyond the control of the Trustee.

### **Amendment of the Trust Agreement**

Amendment of the Trust Agreement. The Trust Agreement and the rights and obligations of the Authority and of the Owners may be amended at any time by a Supplemental Trust Agreement which will become binding when the written consents of the Owners of a majority in aggregate principal amount of the 2008 Certificates then Outstanding, exclusive of 2008 Certificates disqualified as provided in Trust Agreement, are filed with the Trustee; provided, that before executing any such Supplemental Trust Agreement the Trustee may first obtain at the Authority’s expense an Opinion of Counsel that such Supplemental Trust Agreement complies with the provisions of the Trust Agreement, on which opinion the Trustee may conclusively rely. No such amendment will (1) extend the Certificate Payment Date of, or change the payment dates of, or reduce the rate of interest or principal or prepayment premium, if any, evidenced and represented by any 2008 Certificate without the express written consent of the Owner of such Certificate, or (2) reduce the percentage of 2008 Certificates required for the written consent to any such amendment, or (3) modify any rights or obligations of the Trustee without its prior written assent thereto.

The Trust Agreement and the rights and obligations of the Authority and of the Owners may also be amended at any time by a Supplemental Trust Agreement which will become binding upon adoption without the consent of any Owners, but only to the extent permitted by law, for any purpose that will not materially adversely affect the interests of the Owners, including (without limitation) for any one or more of the following purposes:

- (a) to add to the agreements and covenants required in the Trust Agreement to be performed by the Authority other agreements and covenants thereafter to be performed by the Authority, or to surrender any right or power reserved in the Trust Agreement to or conferred in the Trust Agreement on the Authority;
- (b) to make such provisions for the purpose of curing any ambiguity or of correcting, curing or supplementing any defective provision contained in the Trust Agreement or in regard to questions arising under the Trust Agreement which the Authority may deem desirable or necessary and not inconsistent with the Trust Agreement;
- (c) to add to the agreements and covenants required in the Trust Agreement, such agreements and covenants as may be necessary to qualify the Trust Agreement under the Trust Indenture Act of 1939;
- (d) to make any amendments or supplements necessary or appropriate to preserve or protect the exclusion of interest evidenced and represented by the 2008 Certificates from

gross income for federal income tax purposes under the Code or the exemption of such interest from State of California personal income taxes;

(e) to make such amendments or supplements as may be necessary or appropriate to maintain any then current rating on the 2008 Certificates by any of the Rating Agencies;

(f) to add to the rights of the Trustee;

(g) to modify, alter, amend or supplement the Trust Agreement in any other respect, including amendments which would otherwise be described in the Trust Agreement, if the effective date of such amendments is a date on which all 2008 Certificates affected thereby are subject to mandatory tender for purchase pursuant to the provisions of the Trust Agreement or if notice of the proposed amendments is given to Owners of the affected 2008 Certificates at least thirty (30) days before the proposed effective date of such amendments and, on or before such effective date, such Owners have the right to demand purchase of their 2008 Certificates pursuant to the provisions of the Trust Agreement; or

(h) for any other purpose that does not materially and adversely affect the interests of the Owners of the 2008 Certificates.

Amendment by Mutual Consent. Subject to certain provisions in the Trust Agreement related to the 2008 Certificate Insurance Policy, the Trust Agreement does not prevent any Owner from accepting any amendment as to the particular 2008 Certificates held by him, provided that due notation thereof is made on such 2008 Certificates.

Consent of the Liquidity Facility Provider. Notwithstanding anything to the contrary contained in the Trust Agreement, the Trust Agreement may not be amended without the prior written consent of the Liquidity Facility Provider.

Notice. The Trustee will give notice to the Rating Agencies of any amendments pursuant to the Trust Agreement.

### **Events of Default and Remedies of Owners**

Events of Default: Acceleration; Waiver of Default. If an Event of Default (as that term is defined in the Contract) will happen, then such Event of Default will constitute a default under the Trust Agreement, and in each and every such case during the continuance of such Event of Default the Trustee after receiving indemnification to its satisfaction or the Owners of not less than a majority in aggregate principal amount of the 2008 Certificates then Outstanding will exercise the remedies provided to the Authority in the Contract; provided, that nothing contained in the Trust Agreement will affect or impact the right of action of any Owner to institute suit directly against the City to enforce payment of the obligation evidenced and represented by such Owner's 2008 Certificates. Upon the occurrence of any Event of Default, the Trustee will give notice to the Credit Facility Provider and the Liquidity Facility Provider.

In determining whether a payment default has occurred under the Trust Agreement or whether a payment on the 2008 Certificates has been made under the Trust Agreement, no effect will be given to payments made under the 2008 Certificate Insurance Policy.

Other Remedies of the Trustee. The Trustee will have the right:

- (a) by mandamus or other action or proceeding or suit at law or in equity to enforce the Authority's rights under the Contract against the City or any director, officer or employee thereof, and to compel the City or any such director, officer or employee to perform or carry out its or his duties under law and the agreements and covenants required to be performed by it or him contained in the Contract;
- (b) by suit in equity to enjoin any acts or things which are unlawful or violate the rights of the Trustee; or
- (c) by suit in equity upon the happening of any Event of Default under the Trust Agreement to enforce the Authority's rights under the Contract to require the City and its directors, officers and employees to account as the trustee of an express trust.

Non-Waiver. A waiver of any default or breach of any duty or contract by the Trustee will not affect any subsequent default or breach of duty or contract or impair any rights or remedies on any such subsequent default or breach of duty or contract. No delay or omission by the Trustee to exercise any right or remedy accruing upon any default or breach of duty or contract will impair any such right or remedy or will be construed to be a waiver of any such default or breach of duty or contract or any acquiescence therein, and every right or remedy conferred upon the Trustee by law or by the Trust Agreement may be enforced and exercised from time to time and as often as will be deemed expedient by the Trustee.

If any action, proceeding or suit to enforce any right or to exercise any remedy is abandoned or determined adversely to the Trustee, the Trustee, and the City will be restored to their former positions, rights and remedies as if such action, proceeding or suit had not been brought or taken.

Remedies Not Exclusive. No remedy in the Trust Agreement conferred upon or reserved to the Trustee or the Owners is intended to be exclusive of any other remedy, and each such remedy will be cumulative and will be in addition to every other remedy given thereunder or now or hereafter existing in law or in equity or by statute or otherwise and may be exercised without exhausting and without regard to any other remedy conferred by law.

No Liability by the City to the Owners. Except for the payment when due of the 2008 Payments and the performance of the other agreements and covenants required to be performed by it contained in the Contract, the City will not have any obligation or liability to the Owners with respect to the Trust Agreement or the preparation, execution, delivery or transfer of the 2008 Certificates or the disbursement of the 2008 Payments by the Trustee to the Owners, or with respect to the performance by the Trustee of any right or obligation required to be performed by it contained in the Trust Agreement.

No Liability by the Trustee to the Owners. Except as expressly provided in the Trust Agreement, the Trustee will not have any obligation or liability to the Owners with respect to the payment when due of the 2008 Payments by the City, or with respect to the performance by the City of the other agreements and covenants required to be performed by it contained in the Contract.

Control of Remedies by Credit Facility Provider or Liquidity Facility Provider. As long as no Control Event has occurred, notwithstanding anything in the Trust Agreement to the contrary, the 2008 Certificate Insurer will have the right to direct all remedies upon the occurrence of an Event of Default. If a Control Event has occurred and the Bank's Credit Enhancement is in effect, notwithstanding anything in the Trust Agreement to the contrary, the Bank will have the right to direct all remedies upon the

occurrence of an Event of Default. If a Control Event has occurred and the Bank's Credit Enhancement is no longer in effect, notwithstanding anything in the Trust Agreement to the contrary, the Liquidity Facility Provider will have the right to direct all remedies upon the occurrence of an Event of Default.

Notwithstanding the foregoing, if a Liquidity Facility is in effect, and the Provider thereof has failed to honor its payment obligations under the Liquidity Facility in respect of the purchase price of Certificates upon tender thereof, fifty-one percent (51%) of the Certificate holders of the Certificates enhanced by such Liquidity Facility (excluding Certificates owned by the City and Bank Certificates), will have the right at any time, by an instrument or instruments in writing executed and delivered to the Trustee, to direct the method and place of conducting all proceedings to be taken in connection with the enforcement of such payment obligations; provided that such direction will be in accordance with applicable law.

Application of Funds in case of an Event of Default. All moneys received by the Trustee pursuant to any right given or action taken under the provisions of the Trust Agreement will be deposited into the 2008 Debt Service Fund and will be applied by the Trustee in the following order upon presentation and surrender of the several 2008 Certificates:

First, Costs and Expenses: to the payment of reasonable fees and expenses of the Trustee (including reasonable fees and disbursements of its counsel) incurred in and about the performance of its powers and duties under the Trust Agreement;

Second, Interest: to the payment to the persons entitled thereto of all installments of interest then due or which have accreted in the order of the maturity of such installment, and, if the amount available shall not be sufficient to pay in full any installment or installments maturing on the same date, then to the payment thereof ratably, according to the amounts due thereon, to the persons entitled thereto, without any discrimination or preference; and

Third, Principal: to the payment to the persons entitled thereto of the unpaid principal of any 2008 Certificates that will have become due, whether at maturity or by call for prepayment, in the order of their due dates, with interest on the overdue principal and interest at a rate equal to the rate paid with respect to the 2008 Certificates and, if the amount available will not be sufficient to pay in full all the amounts due with respect to the 2008 Certificates on any date, together with such interest, then to the payment thereof ratably, according to the amounts of principal due on such date to the persons entitled thereto, without any discrimination or preference.

## **Defeasance**

Discharge of Trust Agreement. When the obligations of the City under the Contract will cease pursuant to the Contract (except for the right of the Trustee and the obligation of the City to have the money and Federal Securities mentioned therein applied to the payment of 2008 Payments as therein set forth), and (i) the 2008 Certificates are in Fixed Rate Mode at the time moneys or Federal Securities are deposited, (ii) the deposit of money and Federal Securities is sufficient to pay the 2008 Certificates at the Maximum Rate to the earlier of the first possible tender or redemption date, (iii) the City will have received a Rating Confirmation Notice on any 2008 Certificate that will remain Outstanding following such redemption, and (iv) all other sums payable under the Trust Agreement, including to the 2008 Certificate Insurer and Bank, have been paid, then and in such case the obligations created by the Trust Agreement will thereupon cease, terminate and become void except for the right of the Owners and the obligation of the Trustee to apply such moneys and Federal Securities to the payment of the 2008 Certificates as set forth in the Trust Agreement and the right of the Trustee to collect any fees or expenses

due thereunder and the Trustee will turn over to the City, as an overpayment of 2008 Payments, all balances remaining in any other funds or accounts other than moneys and Federal Securities held for the payment of the 2008 Certificates at maturity or on prepayment, which moneys and Federal Securities will continue to be held by the Trustee in trust for the benefit of the Owners and will be applied by the Trustee to the payment, when due, of the principal and interest and premium if any represented by the 2008 Certificates, and after such payment, the Trust Agreement will become void.

If moneys or Federal Securities are deposited with and held by the Trustee as provided in the Trust Agreement, the Trustee will mail a notice, first-class postage prepaid, to the Owners at the addresses listed on the registration books kept by the Trustee pursuant to the Trust Agreement, stating that (a) moneys or Federal Securities are so held by it, and (b) that the Trust Agreement has been released in accordance with the provisions of the Trust Agreement.

Notice of discharge of the Trust Agreement will be provided to the Rating Agencies by the Trustee.

Deposit of Money or Securities with Trustee. Whenever in the Trust Agreement or the Contract it is provided or permitted that there be deposited with or held in trust by the Trustee money or securities (certified to be sufficient by a report of an Independent Certified Public Accountant) in the necessary amount to pay or prepay any 2008 Certificates, the money or securities to be so deposited or held may include money or securities held by the Trustee in the funds and accounts established pursuant to the Trust Agreement and will be:

- (a) lawful money of the United States of America in an amount equal to the principal amount represented by such 2008 Certificates and all unpaid interest represented thereby to maturity, except that, in the case of 2008 Certificates which are to be prepaid prior to maturity and in respect of which notice of such prepayment will have been given as provided in the Trust Agreement or provision satisfactory to the Trustee will have been made for the giving of such notice, the amount to be deposited or held will be the principal amount plus accrued interest to such date of prepayment plus a prepayment premium, if any, represented by such 2008 Certificates; or
- (b) Federal Securities which are not subject to redemption except by the holder thereof prior to maturity (including any such securities issued or held in book-entry form) or municipal obligations which have been defeased under irrevocable escrow instructions with Federal Securities and which are rated in the highest rating category by the Rating Agencies, the principal of and interest on which when due will provide, in its opinion of an Independent Certified Public Accountant, delivered to the Trustee, money sufficient to pay the principal plus prepayment premium, if any, plus all accrued interest to maturity or to the prepayment date, as the case may be, represented by the 2008 Certificates to be paid or prepaid, as such amounts become due, provided that, in the case of 2008 Certificates which are to be prepaid prior to the maturity thereof, notice of such prepayment will have been given as provided in the Trust Agreement or provision satisfactory to the Trustee will have been made for the giving of such notice;

provided, in each case, that the Trustee will have been irrevocably instructed (by the terms of the Trust Agreement and the Contract or by Written Request of the City) to apply such money to the payment of such principal plus prepayment premium, if any, plus interest represented by such 2008 Certificates.

Unclaimed Money. Notwithstanding anything contained in the Trust Agreement to the contrary, any money held by the Trustee in trust for the payment and discharge of any of the 2008 Certificates

which remains unclaimed for two years after the date when such 2008 Certificates have become due and payable, either at their stated Certificate Payment Dates or by call for prepayment prior to Certificate Payment Date, if such money was held by the Trustee at such date, or for two years after the date of deposit of such money if deposited with the Trustee after the date when such Certificates have become due and payable, will be repaid by the Trustee to the City as its absolute property free from trust, and the Trustee will thereupon be released and discharged with respect thereto and the Owners will look only to the City for the payment of the 2008 Payments evidenced and represented by such 2008 Certificates; provided, however, that before being required to make any such payment to the City, the Trustee will, at the request of and at the expense of the City, cause to be mailed to all Owners and the Securities Depositories and the Information Services a notice that such money remains unclaimed and that, after a date named in such notice, which date will not be less than 30 days after the date of the first publication of each such notice, the balance of such money then unclaimed will be returned to the City.

#### **Additional Provisions Relating to the 2008 Certificate Insurance Policy**

(a) Subject to the Trust Agreement, the 2008 Certificate Insurer will be deemed to be sole Owner of the 2008 Certificates it insures for the purpose of exercising any voting right or privilege or giving any consent or direction or taking any other action that the 2008 Certificate Owners are entitled to take pursuant to the Trust Agreement, including any consent to any modification, amendment or supplement to the Trust Agreement pursuant to the Trust Agreement.

(b) Notwithstanding anything in the Trust Agreement to the contrary the 2008 Certificate Insurer will be deemed to be the Owners of all of the 2008 Certificates for purposes of (a) exercising all remedies and directing the Trustee to take actions or for any other purposes following an Event of Default (as defined in the Trust Agreement), and (b) granting any consent, direction or approval or taking any action permitted or required by the Owners of the 2008 Certificates.

(c) Notwithstanding anything in the Trust Agreement to the contrary so long as the 2008 Certificate Insurance Policy will be in full force and effect and the 2008 Certificate Insurer will not be in default of any of its obligations thereunder, upon the occurrence and continuance of an Event of Default, the Trustee may, with the consent of the 2008 Certificate Insurer, and will at the direction of the 2008 Certificate Insurer or the Bondholders with the prior written consent of the 2008 Certificate Insurer, by written notice to the Authority and the 2008 Certificate Insurer, as applicable (i) declare the principal of the 2008 Certificates immediately due and payable, whereupon that portion of the principal of the 2008 Certificates thereby coming due and the interest thereon accrued to the date of payment will, without further action, become and be immediately due and payable, anything in the Trust Agreement or the 2008 Certificates to the contrary notwithstanding or (ii) annul any declaration of acceleration.

#### **Additional Provisions with respect to Rights of the Bank**

(a) To the extent the Bank pays the principal of or interest on the 2008 Certificates from one or more drawings under its Credit Enhancement and has not been reimbursed for such payment by the Authority or the Trustee, on behalf of the Authority, in accordance with the terms of the Reimbursement Agreement between the Bank and the City, (i) such amounts of principal of and interest on such 2008 Certificates will be deemed not to have been paid for purposes of the Trust Agreement and such 2008 Certificates will remain Outstanding and will continue to be due and owing until paid or otherwise satisfied; (ii) all rights of the Owners of such 2008 Certificates with respect to receiving payment of such principal from the Authority will, without any further action on the part of such Owners or the Trustee, be assigned to the Bank and the Bank will become subrogated to such rights; (iii) as to any such payment of principal of the 2008 Certificates from a drawing under the Bank's Credit Enhancement, the Bank will become the Owner of such 2008 Certificate, which will be evidenced as set forth in the next sentence; and

(iv) as to any such payment of interest on such 2008 Certificates from a drawing under the Bank's Credit Enhancement, the Bank will become the owner of all rights to such interest, constituting the Assigned Rights to Interest with respect thereto. The Trustee will designate any portion of payment of principal on 2008 Certificates paid from one or more drawings under the Bank's Credit Enhancement, whether by virtue of mandatory sinking fund pro rata redemption, maturity or other advancement of maturity, on its books as a reduction in the principal amount of 2008 Certificates registered to the then current Owner, whether DTC or its nominee or otherwise, and will issue, as a replacement 2008 Certificate, a Subrogated Certificate to the Bank, registered in the name of the Bank, in a principal amount equal to the amount of principal so paid (without regard to Authorized Denominations); provided that the Trustee's failure to so designate any payment or issue any Subrogated Certificate will have no effect on the amount of principal or interest payable by the Authority on any 2008 Certificate, the subrogation rights of the Bank or the Bank's ownership of such 2008 Certificate to the extent principal thereof has been paid from a drawing under the Bank's Credit Enhancement.

(b) In addition, to the extent the Bank pays the principal of or interest on 2008 Certificates from one or more drawings under the Bank's Credit Enhancement and has not been reimbursed from such payment by the Authority or the Trustee, on behalf of the Authority, in accordance with the terms of the Reimbursement Agreement between the Bank and the City, the Bank will be subrogated to the rights of the Owners of such 2008 Certificates with respect to the 2008 Certificate Insurance Policy in respect of any such payment of principal or interest that is insured under the 2008 Certificate Insurance Policy (a "Covered Payment"); provided, however, that the Bank's subrogation rights with respect to the 2008 Certificate Insurance Policy in respect of the foregoing payments of principal and interest are subject to the terms and conditions of the 2008 Certificate Insurance Policy.

(c) To exercise such rights of subrogation as to a Covered Payment, the Bank must notify the Trustee and the 2008 Certificate Insurer on or before 5:00 p.m. New York City time on the date that is 30 days after a Covered Payment has been made that the Bank is making a claim (a "Claim") under the 2008 Certificate Insurance Policy, which claim will (i) specifically reference the policy number of the 2008 Certificate Insurance Policy and will be presented to the 2008 Certificate Insurer at its address specified in the Trust Agreement or pursuant to the Trust Agreement, (ii) state the date of the Covered Payment, (iii) state the amount of the Covered Payment, and (iv) in all cases comply with the requirements of the Trust Agreement and the 2008 Certificate Insurance Policy. Upon payment of a Claim, these provisions will apply to the same extent as if the 2008 Certificate Insurer had made such payment directly on the related Series of 2008 Certificates. In the event the Bank does not make a claim on or before 5:00 p.m. New York City time on the date that is 30 days after a Covered Payment, the 2008 Certificate Insurer will have no further obligation to the Bank with respect thereto and a principal amount of the related Series of Certificates equal to the principal that has been paid by the Bank will be deemed to be fully discharged in accordance with the Trust Agreement.

(d) At all times from and after the occurrence of a Control Event with respect to the 2008 Certificate Insurance Policy, the Bank will be an expressly intended third party beneficiary of the Trust Agreement and will be deemed to be the sole Owner of the 2008 Certificates for the purpose of exercising any voting right or privilege or giving any consent or direction or taking any other action that the Owners of the 2008 Certificates are entitled to exercise, give or take pursuant to this Trust Agreement with respect to (i) Events of Default and remedies under the Trust Agreement and under the Contract, (ii) the duties and obligations of the Trustee, and (iii) granting or withholding any consent wherever Owner consent is required.

**APPENDIX E**  
**FORM OF LETTER OF CREDIT**

Irrevocable Transferable Letter of Credit

July 14, 2011  
U.S. \$48,501,822  
No. CPCS-923992

The Bank of New York Mellon Company, N.A.,  
as trustee (the "*Trustee*") and Agent under the  
Amended and Restated Trust Agreement,  
Trust Agreement dated as of July 14, 2011  
(the "*Trust Agreement*") between the Modesto  
Public Financing Authority (the "*Authority*")  
and the Trustee  
555 Kearny Street, Suite 600  
San Francisco, CA 94108

Attention: Corporate Trust Department

Ladies and Gentlemen:

We hereby establish in your favor as Trustee for the benefit of the holders of the Authority's Water Revenue Refunding Certificates of Participation 2008 Series A (the "*Certificates*"), our irrevocable transferable Letter of Credit No. CPCS-923992 for the account of the City of Modesto (the "*Applicant*"), whereby we hereby irrevocably authorize you to draw on us from time to time, from and after the date hereof to and including the earliest to occur of our close of business on: (i) July 14, 2014 (as extended from time to time, the "*Stated Expiration Date*"), (ii) the earlier of (A) the date which is five (5) days following the Conversion Date (as defined in the Trust Agreement) of all of the Certificates as such date is specified in a certificate in the form of Annex A hereto (the "*Conversion Date*") to a rate of interest other than a Daily Rate (as defined in the Trust Agreement) or the Weekly Rate (as defined in the Trust Agreement) or (B) the date on which the Bank honors a drawing under the Letter of Credit on or after the Conversion Date, (iii) the date which is five (5) days following receipt from you of a certificate in the form set forth as Annex B hereto, and (iv) the date which is ten (10) days following receipt by you of a written notice from us stating that such notice is delivered pursuant to Section 6.3(a) or Section 6.5(b), as the case may be, of the Reimbursement Agreement, dated as of July 1, 2011, between the Applicant and us (such agreement, the "*Reimbursement Agreement*"; such notice, a "*Default Notice*") and specifying the occurrence of an Event of Default or a Rating Event under the Reimbursement Agreement and directing you to cause a mandatory purchase of the Certificates (the "*Termination Date*"), a maximum aggregate amount not exceeding Forty Eight Million Five Hundred One Thousand Eight Hundred Twenty Two United States Dollars (U.S. \$48,501,822) (the "*Original Stated Amount*") to pay principal of and accrued interest with respect to, or the purchase price of, the Certificates in accordance with the terms hereof (said U.S. \$48,501,822 having been calculated to be equal to Forty Seven Million Six Hundred Twenty Five Thousand United States Dollars (U.S. \$47,625,000), the outstanding principal amount of the Certificates, plus Eight Hundred Seventy Six Thousand Eight Hundred Twenty Two United States Dollars

(U.S. \$876,822) (the “*Interest Component*”), which is 56 days’ accrued interest with respect to said principal amount of the Certificates at the rate of twelve percent (12%) per annum calculated on a 365 days basis (the “*Cap Interest Rate*”).

This credit is available to you against presentation of the following documents (the “*Payment Documents*”) presented to JPMorgan Chase Bank, N.A. (the “*Bank*”) as described below:

A certificate (with all blanks appropriately completed) (i) in the form attached as Annex C hereto to pay accrued interest with respect to the Certificates (an “*Interest Drawing*”), (ii) in the form attached as Annex D hereto to pay the principal amount of and accrued interest with respect to the Certificates in respect of any payment of the principal of the Certificates (including payments of principal at maturity and upon redemption) (a “*Principal Drawing*”), provided that in the event the date of payment coincides with an Interest Payment Date (as defined in the Trust Agreement), the Principal Drawing shall not include any accrued interest with respect to the Certificates (which interest is payable pursuant to an Interest Drawing), or (iii) in the form attached as Annex E hereto to pay the purchase price of Certificates which have not been remarketed or which are not required to be remarketed (a “*Liquidity Drawing*”), provided that in the event the purchase date coincides with an Interest Payment Date, the Liquidity Drawing shall not include any accrued interest with respect to the Certificates (which interest is payable pursuant to an Interest Drawing), each certificate to state therein that it is given by your duly authorized representative and dated the date such certificate is presented hereunder. No drawings shall be made under this Letter of Credit for Liquidity Provider Certificates (as defined in the Trust Agreement) or Certificates registered in the name of the Applicant.

All drawings shall be made by presentation of each Payment Document by facsimile (at facsimile number (312) 954-6163 or alternately to (312) 954-3140), Attention: Standby Service Unit, without further need of documentation, including the original of this Letter of Credit, it being understood that each Payment Document so submitted is to be the sole operative instrument of drawing.

We agree to honor and pay the amount of any Interest Drawing, Principal Drawing or Liquidity Drawing if presented in compliance with all of the terms of this Letter of Credit. If such drawing, other than a Liquidity Drawing, is presented at or prior to 5:00 P.M., Eastern time, on a Business Day, payment shall be made to the account number or address designated by you of the amount specified, in immediately available funds, by 1:00 P.M., Eastern time, on the following Business Day. If any such drawing, other than a Liquidity Drawing, is presented after 5:00 P.M., Eastern time, on a Business Day, payment shall be made to the account number or address designated by you of the amount specified, in immediately available funds, by 1:00 P.M., Eastern time, on the second following Business Day. If a Liquidity Drawing is presented at or prior to 12:30 P.M., Eastern Time, on a Business Day, payment shall be made to the account number or address designated by you of the amount specified, in immediately available funds, by 2:30 P.M., Eastern time, on the same Business Day. If a Liquidity Drawing is presented after 12:30 P.M., Eastern time, payment shall be made to the account number and at such bank designated by you of the amount specified, in immediately available funds, by 2:30 P.M., Eastern time, on the following Business Day. Payments made hereunder shall be made by wire transfer to you or by deposit into your account with us in accordance with the instructions

specified by you in the drawing certificate relating to a particular drawing hereunder. “*Business Day*” means any day other than (i) a Saturday or Sunday, (ii) a day on which banking institutions in the city or cities in which the principal corporate trust office of the Trustee (as defined in the Trust Agreement) or the Trustee is located or banking institutions in New York, New York are authorized or required by law to close, (iii) in the case of the Bank, a day on which banking institutions in the city in which the office of the Bank at which drawings under the Letter of Credit are to be presented is located are authorized or required by law to close or (iv) any day on which the New York Stock Exchange is closed.

The Available Amount (as hereinafter defined) will be reduced automatically by the amount of any drawing hereunder; *provided, however*, that the amount of any Interest Drawing hereunder that is not accompanied by a Principal Drawing or Liquidity Drawing shall be automatically reinstated immediately on the fifth day after demand for payment is honored by us unless you receive a Default Notice (which may include delivery by telecopier, telex, prepaid telegram or other telecommunication) on or before the close of business on such date. After payment by us of a Liquidity Drawing, the obligation of the Bank to honor drawings under this Letter of Credit will be automatically reduced by an amount equal to the Original Purchase Price (as defined below) of any Certificates (or portions thereof) purchased pursuant to said drawing. In addition, prior to the Conversion Date, in the event of the remarketing of the Certificates (or portions thereof) previously purchased with the proceeds of a Liquidity Drawing, our obligation to honor drawings hereunder shall be automatically reinstated concurrently upon receipt by the Bank, or the Trustee on the Bank’s behalf, of an amount equal to the Original Purchase Price of such Certificates (or portion thereof) plus accrued interest thereon as required under the Reimbursement Agreement as specified in a certificate in the form of Annex I hereto; the amount of such reinstatement shall be equal to the Original Purchase Price of such Certificates (or portions thereof). “*Original Purchase Price*” shall mean the principal amount of any Certificate purchased with the proceeds of a Liquidity Drawing plus the amount of accrued interest with respect to such Certificate paid with the proceeds of a Liquidity Drawing (and not pursuant to an Interest Drawing) upon such purchase.

Upon receipt by us of a certificate of the Trustee in the form of Annex F hereto, the Available Amount to be drawn hereunder will automatically and permanently be reduced by the amount specified in such certificate. Such reduction shall be effective as of the next Business Day following the date of delivery of such certificate. Upon any permanent reduction of the Available Amount to be drawn under this Letter of Credit, as provided herein, we will deliver to you an amendment to this Letter of Credit substantially in the form of Annex J hereto to reflect any such reduction. The “*Available Amount*” shall mean the Original Stated Amount (i) less the amount of all prior reductions pursuant to Interest Drawings, Principal Drawings or Liquidity Drawings, (ii) less the amount of any reduction thereof pursuant to a certificate in the form of Annex F hereto, (iii) plus the amount of all reinstatements as above provided.

Prior to the Termination Date, we may extend the Stated Expiration Date from time to time at the request of the Applicant by delivering to you an amendment to this Letter of Credit in the form of Annex H hereto designating the date to which the Stated Expiration Date is being extended. Each such extension of the Stated Expiration Date shall become effective on the Business Day following delivery of such notice to you and thereafter all references in this Letter of Credit to

the Stated Expiration Date shall be deemed to be references to the date designated as such in such notice. Any date to which the Stated Expiration Date has been extended as herein provided may be extended in a like manner.

Upon the Termination Date this Letter of Credit shall automatically terminate and be delivered to the Bank for cancellation. Failure to deliver said Letter of Credit will have no effect on the Termination Date, and the Letter of Credit will still be considered terminated.

This Letter of Credit is transferable to any transferee who has succeeded you as Trustee under the Trust Agreement, and may be successively transferred. Any transfer request must be affected by presenting to us the attached form of Annex G signed by the transferor and the transferee together with the original Letter of Credit. Upon our endorsement of such transfer, the transferee instead of the transferor shall, without necessity of further action, be entitled to all the benefits of and rights under this Letter of Credit in the transferor's place; *provided* that, in such case, any certificates of the Trustee to be provided hereunder shall be signed by one who states therein that he is a duly authorized officer or agent of the transferee.

Communications with respect to this Letter of Credit shall be addressed to us at JPMorgan Chase Bank, N.A., 131 South Dearborn, 5<sup>th</sup> Floor, Mail Code IL1-0236, Chicago, Il 60603-5506, Attention: Standby Letter of Credit Unit, specifically referring to the number of this Letter of Credit. For telephone assistance, please contact the Standby Client Service Unit at 1-800-634-1969, select Option 1, and have this Letter of Credit number available.

Except as expressly stated herein, this Letter of Credit is governed by, and construed in accordance with the International Standby Practices, ICC Publication No. 590 (the "ISP98"). As to matters not governed by the ISP98, this Letter of Credit shall be governed by and construed in accordance with the laws of the State of New York, including without limitation the Uniform Commercial Code as in effect in the State of New York, without regard to principals of conflict of laws.

All payments made by us hereunder shall be made from our funds and not with the funds of any other Person.

*(Signature Page Follows)*

This Letter of Credit sets forth in full the terms of our undertaking, and such undertaking shall not in any way be modified or amended by reference to any other document whatsoever except the attached annexes.

Very truly yours,

JPMORGAN CHASE BANK, N.A.

By: \_\_\_\_\_

Name:

Title:

ANNEX A  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992

NOTICE OF CONVERSION DATE

[Date]

JPMorgan Chase Bank, N.A.  
131 South Dearborn  
5th Floor, Mail Code IL1-0236  
Chicago, IL 60603-5506

Attn: Standby Letter of Credit Unit

Ladies and Gentlemen:

Reference is hereby made to that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "*Letter of Credit*"), which has been established by you for the account of the City of Modesto, in favor of the Trustee.

The undersigned hereby certifies and confirms that the Conversion Date of all of the Certificates to an interest rate other than a Daily Rate (as defined in the Trust Agreement) or a Weekly Rate (as defined in the Trust Agreement) has occurred on [insert date], and, accordingly, said Letter of Credit shall terminate 5 days after such Conversion Date in accordance with its terms.

All defined terms used herein which are not otherwise defined herein shall have the same meaning as in the Letter of Credit.

The Bank of New York Mellon Company,  
N.A., as Trustee

By: \_\_\_\_\_  
[Title of Authorized  
Representative]

**ANNEX B**  
**TO**  
**JPMORGAN CHASE BANK, N.A.**  
**LETTER OF CREDIT**  
**No. CPCS-923992**

NOTICE OF TERMINATION

[Date]

JPMorgan Chase Bank, N.A.  
131 South Dearborn  
5th Floor, Mail Code IL1-0236  
Chicago, IL 60603-5506

Attn: Standby Letter of Credit Unit

Ladies and Gentlemen:

Reference is hereby made to that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "*Letter of Credit*"), which has been established by you for the account of the City of Modesto, in favor of the Trustee.

The undersigned hereby certifies and confirms that (i) no Certificates (as defined in the Letter of Credit) remain outstanding within the meaning of the Trust Agreement, (ii) all drawings required to be made under the Trust Agreement and available under the Letter of Credit have been made and honored, or (iii) a substitute letter of credit has been issued to replace the Letter of Credit pursuant to the Trust Agreement, and, accordingly, the Letter of Credit shall be terminated in accordance with its terms.

All defined terms used herein which are not otherwise defined shall have the same meaning as in the Letter of Credit.

The Bank of New York Mellon Company,  
N.A., as Trustee

By \_\_\_\_\_  
[Title of Authorized  
Representative]

INTEREST DRAWING CERTIFICATE

JPMorgan Chase Bank, N.A.  
(facsimile number (312) 954-6163  
alternately to (312) 954-3140)

Attn: Standby Letter of Credit Unit

The undersigned individual, a duly authorized representative of The Bank of New York Mellon Company, N.A., as Trustee (the “Beneficiary”), hereby CERTIFIES on behalf of the Beneficiary as follows with respect to (i) that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the “Letter of Credit”), issued by JPMORGAN CHASE BANK, N.A. (the “Bank”) in favor of the Beneficiary; (ii) those certain Certificates (as defined in the Letter of Credit); and (iii) that certain Trust Agreement (as defined in the Letter of Credit):

1. The Beneficiary is the Trustee (as defined in the Letter of Credit) under the Trust Agreement.

2. The Beneficiary is entitled to make this drawing in the amount of U.S. \$ \_\_\_\_\_ under the Letter of Credit pursuant to the Trust Agreement with respect to the payment of interest due with respect to all Certificates outstanding on the Interest Payment Date (as defined in the Trust Agreement) occurring on [insert applicable date], other than Liquidity Provider Certificates (as defined in the Trust Agreement) and Certificates registered in the name of the Applicant (as defined in the Letter of Credit).

3. The amount of the drawing is equal to the amount required to be drawn by the Trustee pursuant to the Trust Agreement.

4. The amount of the drawing made by this Certificate was computed in compliance with the terms of the Trust Agreement and, when added to the amount of any other drawing under the Letter of Credit made simultaneously herewith, does not exceed the Available Amount (as defined in the Letter of Credit).

5. Payment by the Bank pursuant to this drawing shall be made to \_\_\_\_\_, ABA Number \_\_\_\_\_, Account Number \_\_\_\_\_, Attention: \_\_\_\_\_, Re: \_\_\_\_\_.

(Signature Page Follows)

**ANNEX C  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992  
(CONTINUED)**

IN WITNESS WHEREOF, this Certificate has been executed this \_\_\_\_ day of \_\_\_\_\_, 201\_.

The Bank of New York Mellon Company,  
N.A., as Trustee

By \_\_\_\_\_  
[Title of Authorized  
Representative]

PRINCIPAL DRAWING CERTIFICATE

JPMorgan Chase Bank, N.A.  
(facsimile number (312) 954-6163  
alternately to (312) 954-3140)

Attn: Standby Letter of Credit Unit

The undersigned individual, a duly authorized representative of The Bank of New York Mellon Company, N.A., as Trustee (the "*Beneficiary*"), hereby CERTIFIES on behalf of the Beneficiary as follows with respect to (i) that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "*Letter of Credit*"), issued by JPMORGAN CHASE BANK, N.A. (the "*Bank*") in favor of the Beneficiary; (ii) those certain Certificates (as defined in the Letter of Credit); and (iii) that certain Trust Agreement (as defined in the Letter of Credit):

1. The Beneficiary is the Trustee (as defined in the Letter of Credit) under the Trust Agreement.

2. The Beneficiary is entitled to make this drawing in the amount of U.S. \$ \_\_\_\_\_ under the Letter of Credit pursuant to the Trust Agreement.

3. (a) The amount of this drawing is equal to (i) the principal amount of Certificates to be paid (whether at maturity or by redemption) pursuant to the Trust Agreement on [insert applicable date] (the "*Principal Date*"), other than Liquidity Provider Certificates (as defined in the Trust Agreement) and Certificates registered in the name of the Applicant (as defined in the Letter of Credit), plus (ii) interest with respect to such Certificates accrued from the immediately preceding Interest Payment Date (as defined in the Trust Agreement) to the Principal Date, provided that in the event the Principal Date coincides with an Interest Payment Date this drawing does not include any accrued interest with respect to such Certificates.

(b) Of the amount stated in paragraph 2 above:

(i) U.S. \$ \_\_\_\_\_ is demanded in respect of the principal amount of the Certificates referred to in subparagraph (a) above; and

(ii) U.S. \$ \_\_\_\_\_ is demanded in respect of accrued interest with respect to such Certificates.

4. Payment by the Bank pursuant to this drawing shall be made to \_\_\_\_\_, ABA Number \_\_\_\_\_, Account Number \_\_\_\_\_, Attention: \_\_\_\_\_, Re: \_\_\_\_\_.

**ANNEX D**  
**TO**  
**JPMORGAN CHASE BANK, N.A.**  
**LETTER OF CREDIT**  
**No. CPCS-923992**  
**(CONTINUED)**

5. The amount of the drawing made by this Certificate was computed in compliance with the terms and conditions of the Trust Agreement and, when added to the amount of any other drawing under the Letter of Credit made simultaneously herewith, does not exceed the Available Amount (as defined in the Letter of Credit).

6. Upon payment of the amount drawn hereunder, the Bank is hereby directed to permanently reduce the Available Amount by U.S. \$[insert amount of reduction] and the Available Amount shall thereupon equal U.S. \$[insert new Available Amount]. The Available Amount has been reduced by an amount equal to the principal of Certificates paid with this drawing and an amount equal to 56 days' interest thereon at the Cap Interest Rate (as defined in the Letter of Credit).

7. Of the amount of the reduction stated in paragraph 6 above:

(i) U.S. \$\_\_\_\_\_ is attributable to the principal amount of Certificates redeemed or paid at maturity; and

(ii) U.S. \$\_\_\_\_\_ is attributable to interest with respect to such Certificates (*i.e.*, 56 days' interest thereon at the Cap Interest Rate).

8. The amount of the reduction in the Available Amount has been computed in accordance with the provisions of the Letter of Credit.

9. Following the reduction, the Available Amount shall be at least equal to the aggregate principal amount of the Certificates outstanding (to the extent such Certificates are not Liquidity Provider Certificates (as defined in the Trust Agreement) or Certificates registered in the name of the Applicant (as defined in the Letter of Credit) plus 56 days' interest thereon at the Cap Interest Rate.

\*10. Upon application of the proceeds drawn hereunder, no Certificates will remain Outstanding (as defined in the Trust Agreement).

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\* To be included in certificate only if no Certificates will remain Outstanding after application of the proceeds of the Principal Drawing.

**ANNEX D**  
**TO**  
**JPMORGAN CHASE BANK, N.A.**  
**LETTER OF CREDIT**  
**No. CPCS-923992**  
**(CONTINUED)**

IN WITNESS WHEREOF, this Certificate has been executed this \_\_\_\_\_ day of  
\_\_\_\_\_, \_\_\_\_\_.

The Bank of New York Mellon Company,  
N.A., as Trustee

By \_\_\_\_\_  
[Title of Authorized  
Representative]

LIQUIDITY DRAWING CERTIFICATE

JPMorgan Chase Bank, N.A.  
(facsimile number (312) 954-6163  
alternately to (312) 954-3140)

Attn: Standby Letter of Credit Unit

The undersigned individual, a duly authorized representative of The Bank of New York Mellon Company, N.A., as Trustee (the “Beneficiary”), hereby CERTIFIES on behalf of the Beneficiary as follows with respect to (i) that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the “Letter of Credit”), issued by JPMORGAN CHASE BANK, N.A. (the “Bank”) in favor of the Beneficiary; (ii) those certain Certificates (as defined in the Letter of Credit); and (iii) that certain Trust Agreement (as defined in the Letter of Credit):

1. The Beneficiary is the Trustee under the Trust Agreement.

2. The Beneficiary is entitled to make this drawing under the Letter of Credit in the amount of U.S. \$\_\_\_\_\_ with respect to the payment of the purchase price of Certificates tendered for purchase in accordance with the Trust Agreement and to be purchased on [insert applicable date] (the “Purchase Date”) which Certificates have not been remarketed as provided in the Trust Agreement or the purchase price of which has not been received by the Trustee (as defined in the Letter of Credit) on said Purchase Date.

3. (a) The amount of the drawing is equal to (i) the principal amount of Certificates to be purchased pursuant to the Trust Agreement on the Purchase Date, other than Liquidity Provider Certificates (as defined in the Trust Agreement) and Certificates registered in the name of the Applicant (as defined in the Letter of Credit), plus (ii) interest with respect to such Certificates accrued from the immediately preceding Interest Payment Date (as defined in the Trust Agreement) (or if none, the date of issuance of the Certificates) to the Purchase Date, provided that in the event the Purchase Date coincides with an Interest Payment Date this drawing does not include any accrued interest with respect to such Certificates.

(b) Of the amount stated in paragraph (2) above:

(i) U.S. \$\_\_\_\_\_ is demanded in respect of the principal portion of the purchase price of the Certificates referred to in subparagraph (2) above; and

(ii) U.S. \$\_\_\_\_\_ is demanded in respect of payment of the interest portion of the purchase price of such Certificates.

ANNEX E  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992  
(CONTINUED)

4. The amount of the drawing made by this Certificate was computed in compliance with the terms and conditions of the Trust Agreement and, when added to the amount of any other drawing under the Letter of Credit made simultaneously herewith, does not exceed the Available Amount (as defined in the Letter of Credit).

5. The Beneficiary will register or cause to be registered in the name of the Bank, upon payment of the amount drawn hereunder, Certificates (or beneficial interests therein) in the principal amount of the Certificates being purchased with the amounts drawn hereunder in accordance with the requirements of the Custodian Agreement dated as of July 1, 2011, among The Bank of New York Mellon Company, N.A. (as custodian), the Applicant (as defined in the Letter of Credit) and the Bank.

6. Payment by the Bank pursuant to this drawing shall be made to \_\_\_\_\_, ABA Number \_\_\_\_\_, Account Number \_\_\_\_\_, Attention: \_\_\_\_\_, Re: \_\_\_\_\_.

IN WITNESS WHEREOF, this Certificate has been executed this \_\_\_\_ day of \_\_\_\_\_, \_\_\_\_\_.

The Bank of New York Mellon Company,  
N.A., as Trustee

By \_\_\_\_\_  
[Title of Authorized  
Representative]

REDUCTION CERTIFICATE

JPMorgan Chase Bank, N.A.  
131 South Dearborn  
5th Floor, Mail Code IL1-0236  
Chicago, IL 60603-5506

Attn: Standby Letter of Credit Unit

The undersigned individual, a duly authorized representative of The Bank of New York Mellon Company, N.A., as Trustee (the "*Beneficiary*"), hereby CERTIFIES on behalf of the Beneficiary as follows with respect to (i) that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "*Letter of Credit*"), issued by JPMORGAN CHASE BANK, N.A. (the "*Bank*") in favor of the Beneficiary; (ii) those certain Certificates (as defined in the Letter of Credit); and (iii) that certain Trust Agreement (as defined in the Letter of Credit):

1. The Beneficiary is the Trustee under the Trust Agreement.
2. Upon receipt by the Bank of this Certificate, the Available Amount (as defined in the Letter of Credit) shall be permanently reduced by U.S.\$\_\_\_\_\_ and the Available Amount shall thereupon equal U.S. \$ \_\_\_\_\_. U.S. \$ \_\_\_\_\_ of the new Available Amount is attributable to interest.
3. The amount of the reduction in the Available Amount has been computed in accordance with the provisions of the Letter of Credit.
4. Following the reduction, the Available Amount shall be at least equal to the aggregate principal amount of the Certificates outstanding, other than Liquidity Provider Certificates (as defined in the Trust Agreement) and Certificates registered in the name of the Applicant (as defined in the Letter of Credit) plus 56 days' interest thereon at the Cap Interest Rate (as defined in the Letter of Credit).

IN WITNESS WHEREOF, this Certificate has been executed this \_\_\_\_\_ day of \_\_\_\_\_, \_\_\_\_\_.

The Bank of New York Mellon Company,  
N.A., as Trustee

By \_\_\_\_\_  
[Title of Authorized  
Representative]

ANNEX G  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992

REQUEST FOR TRANSFER

JPMorgan Chase Bank, N.A.  
131 South Dearborn  
5th Floor, Mail Code IL1-0236  
Chicago, IL 60603-5506

Date: \_\_\_\_\_

Attn: Standby Letter of Credit Unit

Re: JPMorgan Chase Bank, N.A. Irrevocable Standby Letter of Credit No. CPCS-923992

We, the undersigned "Transferor", hereby irrevocably transfer all of our rights to draw under the above referenced Letter of Credit ("Credit") in its entirety to:

NAME OF TRANSFEREE

\_\_\_\_\_  
(Print Name and complete address of the Transferee) "Transferee"

ADDRESS OF TRANSFEREE

\_\_\_\_\_

CITY, STATE/COUNTRY ZIP

\_\_\_\_\_

In accordance with ISP98, Rule 6, regarding transfer of drawing rights, all rights of the undersigned Transferor in the Credit are transferred to the Transferee, who shall have the sole rights as beneficiary thereof, including sole rights relating to any amendments whether increases or extensions or other amendments and whether now existing or hereafter made. All amendments are to be advised directly to the Transferee without necessity of any consent of or notice to the undersigned Transferor.

The original Credit, including amendments to this date, is attached and the undersigned Transferor requests that you endorse an acknowledgment of this transfer on the reverse thereof. The undersigned Transferor requests that you notify the Transferee of this Credit in such form and manner as you deem appropriate, and the terms and conditions of the Credit as transferred. The undersigned Transferor acknowledges that you incur no obligation hereunder and that the transfer shall not be effective until you have expressly consented to the transfer by notice to the Transferee.

If you agree to these instructions, please advise the Transferee of the terms and conditions of this transferred Credit and these instructions.

**ANNEX G**  
**TO**  
**JPMORGAN CHASE BANK, N.A.**  
**LETTER OF CREDIT**  
**No. CPCS-923992**  
**(CONTINUED)**

Payment of transfer fee of U.S \$3,000 is for the account of the Applicant who agrees to pay you on demand any expense or cost you may incur in connection with the transfer. Receipt of such shall not constitute consent by you to the transfer.

Transferor represents and warrants that (a) the Transferee is the Transferor's successor trustee under the Trust Agreement, (b) the enclosed Credit is original and complete, and (c) there is no outstanding demand or request for payment or transfer under the Credit affecting the rights to be transferred.

The Effective Date shall be the date hereafter on which Transferring Bank effects the requested transfer by acknowledging this request and giving notice thereof to Transferee.

**WE WAIVE ANY RIGHT TO TRIAL BY JURY THAT WE MAY HAVE IN ANY ACTION OR PROCEEDING RELATING TO OR ARISING OUT OF THIS TRANSFER.**

This Request is made subject to ISP98 and is subject to and shall be governed by the laws of the State of New York, without regard to principles of conflict of laws.

*(Signature Page Follows)*

**ANNEX G**  
**TO**  
**JPMORGAN CHASE BANK, N.A.**  
**LETTER OF CREDIT**  
**No. CPCS-923992**  
**(CONTINUED)**

Sincerely yours,

\_\_\_\_\_  
(Print Name of Transferor)

\_\_\_\_\_  
(Transferor's Authorized Signature)

\_\_\_\_\_  
(Print Authorized Signers Name and Title)

\_\_\_\_\_  
(Telephone Number/Fax Number)

SIGNATURE GUARANTEED  
Signature(s) with title(s) conform(s) with that/those on file with us for this individual, entity or company and signer(s) is/are authorized to execute this agreement.

\_\_\_\_\_  
(Print Name of Bank)

\_\_\_\_\_  
(Address of Bank)

\_\_\_\_\_  
(City, State, Zip Code)

\_\_\_\_\_  
(Print Name and Title of Authorized Signer)

\_\_\_\_\_  
(Authorized Signature)

\_\_\_\_\_  
(Telephone Number)

\_\_\_\_\_  
(Date)

Acknowledged:

\_\_\_\_\_  
(Print Name of Transferee)

\_\_\_\_\_  
(Transferee's Authorized Signature)

\_\_\_\_\_  
(Print Authorized Signers Name and Title)

\_\_\_\_\_  
(Telephone Number/Fax Number)

SIGNATURE GUARANTEED  
Signature(s) with title(s) conform(s) with that/those on file with us for this individual, entity or company and signer(s) is/are authorized to execute this agreement.

\_\_\_\_\_  
(Print Name of Bank)

\_\_\_\_\_  
(Address of Bank)

\_\_\_\_\_  
(City, State, Zip Code)

\_\_\_\_\_  
(Print Name and Title of Authorized Signer)

\_\_\_\_\_  
(Authorized Signature)

\_\_\_\_\_  
(Telephone Number)

\_\_\_\_\_  
(Date)

**ANNEX G  
TO  
JPMORGAN CHASE BANK, N.A.  
LETTER OF CREDIT  
No. CPCS-923992  
(CONTINUED)**

Acknowledged as of \_\_\_\_\_, 201\_:

JPMorgan Chase Bank, N.A.

By: \_\_\_\_\_

Name:

Title:

**ANNEX H**  
**TO**  
**JPMORGAN CHASE BANK, N.A.**  
**LETTER OF CREDIT**  
**No. CPCS-923992**

NOTICE OF EXTENSION AMENDMENT

\_\_\_\_\_

The Bank of New York Mellon Company, N.A.  
555 Kearney Street, Suite 600  
San Francisco, California 94108

Attention: Corporate Trust Department

Ladies and Gentlemen:

Reference is hereby made to that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "*Letter of Credit*"), established by us in your favor as Beneficiary. We hereby notify you that, in accordance with the terms of the Letter of Credit and that certain Reimbursement Agreement dated as of July 1, 2011, between the City of Modesto and us, the Stated Expiration Date (as defined in the Letter of Credit) has been extended to

\_\_\_\_\_.

This letter shall be attached to the Letter of Credit and made a part thereof.

JPMorgan Chase Bank, N.A.

By: \_\_\_\_\_  
Name:  
Title:

REINSTATEMENT CERTIFICATE

JPMorgan Chase Bank, N.A.  
(facsimile number (312) 954-6163  
alternately to (312) 954-3140)

Attn: Standby Letter of Credit Unit

The undersigned hereby certifies to JPMorgan Chase Bank, N.A. (the "Bank"), with reference to Irrevocable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "Letter of Credit") issued by the Bank in favor of the Trustee, that:

1. The undersigned is the Trustee under the Trust Agreement.
  
2. The Trustee has previously made a Liquidity Draw under the Letter of Credit on \_\_\_\_\_ in the amount of U.S. \$ \_\_\_\_\_ (representing U.S. \$ \_\_\_\_\_ of principal and U.S. \$ \_\_\_\_\_ of interest) with respect to the purchase price of Certificates which are Liquidity Provider Certificates (as defined in the Trust Agreement).
  
3. The Bank of New York Mellon Company, N.A., as Trustee and custodian under the Custodian Agreement, dated as of July 1, 2011, among The Bank of New York Mellon Company, N.A., the Applicant (as defined in the Letter of Credit) and the Bank has received proceeds from the sale of remarketed Liquidity Provider Certificates originally purchased with the proceeds of the above described Liquidity Drawing and as of the date hereof holds U.S. \$ \_\_\_\_\_ (representing U.S. \$ \_\_\_\_\_ of principal and U.S. \$ \_\_\_\_\_ of interest) with respect to the sale of such Liquidity Provider Certificates.
  
4. In accordance with the terms of the Letter of Credit, the Available Amount (as defined in the Letter of Credit) is hereby automatically reinstated to the extent of the lesser of (i) the proceeds of such remarketed Liquidity Provider Certificates (as described in paragraph 3 above), or (ii) the amount of the Liquidity Drawing described above, all in accordance with the terms of the Letter of Credit and this notice.

IN WITNESS WHEREOF, the undersigned has executed and delivered this Certificate this \_\_\_\_ day of \_\_\_\_\_, \_\_\_\_\_.

The Bank of New York Mellon Company,  
N.A., as Trustee

By \_\_\_\_\_  
[Title of Authorized  
Representative]

**ANNEX J**  
**TO**  
**JPMORGAN CHASE BANK, N.A.**  
**LETTER OF CREDIT**  
**No. CPCS-923992**

NOTICE OF REDUCTION AMENDMENT

[Date]

The Bank of New York Mellon Company, N.A.  
555 Kearney Street, Suite 600  
San Francisco, California 94108

Attention: Corporate Trust Department

Ladies and Gentlemen:

Reference is hereby made to that certain Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011 (the "Letter of Credit"), established by us in your favor as Beneficiary. We hereby notify you that, in accordance with the terms of the Letter of Credit, the Available Amount (as defined in the Letter of Credit) has been reduced to U.S.

\$ \_\_\_\_\_, of which U.S. \$ \_\_\_\_\_ is attributable to principal and U.S.  
\$ \_\_\_\_\_ is attributable to interest.

This letter shall be attached to the Letter of Credit and made a part thereof.

JPMorgan Chase Bank, N.A.

By: \_\_\_\_\_  
Name:  
Title:

**APPENDIX F**  
**ANNUAL REPORT FILING**  
**FOR FISCAL YEAR ENDED JUNE 30, 2010**

**CITY OF MODESTO**  
**CONTINUING DISCLOSURE REQUIREMENTS INFORMATION (continued)**  
**Year Ended June 30, 2010**

1997 Water Utility System Refinancing Project, Refunding Revenue Certificates of Participation  
Water Revenue Refinancing Certificates of Participation, 2008 Series A  
Modesto Irrigation District Financing Authority Domestic Water Project Refunding Revenue Bonds, Series 1998D<sup>(1)</sup>  
Modesto Irrigation District Financing Authority Domestic Water Project Revenue Bonds, Series 2007E<sup>(1)</sup>

Reserve Account Requirement as of 6/30/10	\$4,610,578
Surety Policy Value:	(2,082,513) Provided by FGIC
Balance in Parity Reserve Account as of 6/30/10	<u>(1,858,322)</u>
Shortfall/(Excess) Reserve Coverage:	<u><u>669,743</u></u>

Balance in Rate Stabilization Account as of 6/30/10: 3,000,000

<u>Ten Largest Customers of Water Utility System, Year Ended 6/30/10</u>					
<u>Customer</u>	<u>Business Type</u>	<u>Usage (ccf) (2)</u>	<u>% of Total Usage</u>	<u>Water Sales Revenue (\$)</u>	<u>% of Total Water Sales Revenue</u>
1) City of Modesto	Local Government	418,286	1.44%	\$759,779	1.52%
2) Signature Fruit Co, LLC	Cannery	491,435	1.69%	644,383	1.29%
3) Modesto City Schools	Education	385,633	1.33%	619,042	1.24%
4) Stanislaus Food Products	Cannery	346,940	1.20%	468,984	0.94%
5) Foster Farms	Dairy Processor	330,064	1.14%	430,271	0.86%
6) Modesto Irrigation Dist	Power Company	198,817	0.69%	285,468	0.57%
7) Stanislaus Housing Authority	Housing Authority	161,363	0.56%	271,324	0.54%
8) Stanislaus County Building MAI	County Offices	126,208	0.43%	206,937	0.41%
9) Sylvan Union School Dist	Education	125,689	0.43%	203,885	0.41%
9) Yosemite Comm Coll Dist	Education	109,723	0.38%	199,493	0.40%
Total Top Ten		<u>2,694,158</u>	<u>9.29%</u>	<u>\$4,089,566</u>	<u>8.18%</u>

Total Flat/Metered Revenues (Water Sales) \$50,015,340  
 (1) Grover Landscaping maintains City parks  
 (2) "ccf" means "hundred cubic feet"

Water Sales Revenue, Year Ended 6/30/10

Residential - flat rates	\$21,256,928
Commercial, industrial and municipal - metered rates	<u>28,758,412</u>
Total Water Sales	<u><u>\$50,015,340</u></u>

The average monthly flat rate service charge for residential customers is \$42.31

Current Water Rates as of 07/01/09- Commercial Accounts

<u>Meter Size</u>	
3/4"	\$13.71
1"	19.45
1 1/2"	33.66
2"	50.79
3"	96.51
4"	147.88
6"	290.51
8"	461.75
10"	661.58
12"	1,232.31

In addition to these minimum charges, commercial accounts are charged \$1.28 per 100 cubic feet of water used.

The Annual Budget of the City of Modesto is available from the City of Modesto Finance Department.

(1) Water Fund parity debt obligations, issued by the Modesto Irrigation District Financing Authority, on behalf of the City, and pursuant to the 1992 Treatment and Delivery Agreement between the District and the City. As of 6/30/10, the balance of the 1998 Bonds was \$67,435,000 and the balance of the 2007 Bonds was \$93,190,000. (continued)

**CITY OF MODESTO**  
**CITY WATER- HISTORICAL DEBT SERVICE COVERAGE**  
**CONTINUING DISCLOSURE REQUIREMENTS**  
**Last Six Fiscal Years**

	<u>Fiscal Year 2005</u>	<u>Fiscal Year 2006</u>	<u>Fiscal Year 2007</u>	<u>Fiscal Year 2008</u>
<b>GROSS OPERATING REVENUES</b>				
Charges for Services	\$ 31,315,920	\$ 42,639,348	\$ 49,289,417	\$ 51,433,282
DBCP Settlement	2,960,781	1,334,259		
Connection Charges	1,371,958	1,728,873	2,023,224	1,539,039
Interest and Rental Income	279,616	534,234	2,279,905	2,187,439
Gain/(Loss) on Disposition of Capital Assets				(10,300)
Draw from (Deposit to) Rate Stab, Fund	0	(153,200)	15,616	245,760
Miscellaneous				
<b>GROSS OPERATING REVENUES</b>	<u>35,928,275</u>	<u>46,083,514</u>	<u>53,608,162</u>	<u>55,395,220</u>
<b>OPERATING EXPENSES:</b>				
Total operating expenses	29,227,465	28,672,955	32,466,468	34,676,952
Less: Depreciation	(2,305,953)	(2,383,566)	(2,396,440)	(2,276,755)
T&DA debt service paid to MID(1)	(6,705,344)	(6,690,994)	(6,687,444)	(6,681,894)
Property taxes	82,673	84,556	85,487	86,733
Plus: Operating Transfers	<u>218,902</u>	<u>95,385</u>	<u>65,000</u>	<u>65,000</u>
<b>TOTAL OPERATING EXPENSES</b>	<u>20,517,743</u>	<u>19,778,336</u>	<u>23,533,071</u>	<u>25,870,036</u>
<b>NET OPERATING REVENUES</b>	15,410,532	26,305,178	30,075,091	29,525,184
<b>TOTAL DEBT SERVICE</b>				
Revenue obligations:				
1997 Certificates of Participation	1,784,908	1,790,658	1,794,120	1,791,930
2008 Revenue Certificates of Participation			1,082,432	1,982,256
Treatment & Delivery Agreement	6,705,344	6,690,994	6,687,444	6,681,894
CDWR Loan	<u>264,654</u>	<u>264,654</u>	<u>264,719</u>	<u>264,719</u>
<b>TOTAL DEBT SERVICE</b>	<u>\$ 8,754,906</u>	<u>\$ 8,746,306</u>	<u>\$ 9,828,715</u>	<u>\$ 10,720,799</u>
<b>DEBT SERVICE COVERAGE</b>				
(Net Operating Revenues/ Total Debt Service)	1.76	3.01	3.06	2.75

Note: The City has elected to show only six years of data for this schedule.

	Fiscal Year 2009	Fiscal Year 2010
\$	53,107,853	54,208,363
	852,532	576,651
	2,282,750	888,774
	(47,023)	(19,875)
	110,839	-
	<u>56,306,951</u>	<u>56,115,591</u>
	37,206,969	43,351,954
	(2,359,091)	(5,427,915)
	(6,672,406)	(6,681,894)
	89,219	92,291
	<u>569,315</u>	<u>1,197,325</u>
	28,834,006	32,531,761
	27,472,945	23,583,830
	1,867,883	1,891,599
	2,262,117	2,141,401
	6,672,406	6,681,894
	<u>263,079</u>	<u>262,989</u>
\$	11,065,485	\$ 10,977,883
	2.48	2.15

**CITY OF MODESTO**  
**CITY WATER UTILITY SYSTEM**  
**PROJECTED OPERATING RESULTS**  
**CONTINUING DISCLOSURE REQUIREMENTS**  
**Next Five Fiscal Years**

	<u>2011</u>	<u>2012</u>
GROSS OPERATING REVENUES	\$	\$
Charges for Services	\$52,291,046	\$52,653,630
DBCP Settlement		
Interest and Rental Income	553,801	520,379
Gain/(Loss) on Disposition of Capital Assets		
Draw from (Deposit to) Rate Stab, Fund		
FUND 6101 Development fees & interest	360,257	360,257
Service Credits	2,106,146	2,148,269
Misc Revenue	52,200	53,244
GROSS OPERATING REVENUES	<u>55,363,450</u>	<u>55,735,779</u>
OPERATING EXPENSES:		
Total operating expenses	32,317,454	32,948,471
Less: Depreciation		
Less: Litigation Costs	-428,869	-600,000
T&DA debt service paid to MID(1)		
Property taxes		
Plus: Operating Transfers	<u>765,000</u>	<u>765,000</u>
TOTAL OPERATING EXPENSES	<u>32,653,585</u>	<u>33,113,471</u>
NET OPERATING REVENUES	22,709,865	22,622,308
TOTAL DEBT SERVICE		
Revenue obligations:		
1997 Certificates of Participation	1,794,013	1,795,513
2008 Revenue Certificates of Participation	2,271,034	2,259,523
2007 Treatment & Delivery Agreement COP's	4,123,147	4,123,147
1998 Treatment & Delivery Agreement	6,670,769	6,670,894
CDWR Loan	264,719	264,719
ARRA funding CDPH	<u>0</u>	<u>0</u>
TOTAL DEBT SERVICE	\$ 15,123,682	\$ 15,113,796
DEBT SERVICE COVERAGE		
(Net Operating Revenues/ Total Debt Service)	1.50	1.50

NOTE: Data on schedule revised November 1, 2010

NOTE: The City has elected to show only five years of data for this schedule.

NOTE: Additional financial information is available at the City of Modesto webpage [www.modestogov.com](http://www.modestogov.com)

NOTE: Projected years have been revised due to several capital improvement projects being reclassified to operating expenses.

	<u>2013</u>	<u>2014</u>	<u>2015</u>
\$	\$53,706,702	\$ 54,780,836	55,876,453
	400,621	377,238	453,255
	360,257	360,257	360,257
	2,191,234	2,235,059	2,279,760
	54,309	55,395	56,503
	<u>56,713,123</u>	<u>57,808,785</u>	<u>59,026,228</u>
	33,749,140	34,543,335	35,428,518
	-600,000	-600,000	-600,000
	765,000	765,000	765,000
	<u>33,914,140</u>	<u>34,708,335</u>	<u>35,593,518</u>
	22,798,983	23,100,450	23,432,710
	1,799,388	1,799,822	1,801,653
	2,271,045	2,257,959	2,831,111
	4,123,147	4,123,147	4,123,147
	6,666,644	6,655,160	6,655,554
	264,719	264,719	132,359
	0	36,614	36,614
\$	<u>15,124,943</u>	<u>15,137,421</u>	<u>15,580,438</u>
	1.51	1.53	1.50

**CITY OF MODESTO**  
**CITY WATER UTILITY SYSTEM STATISTICS**  
**CONTINUING DISCLOSURE REQUIREMENTS**  
**Year Ended June 30, 2010**

**CITY WATER UTILITY SYSTEM STATISTICS**  
**(Calendar Years 2005 through 2010)**

	2005	2006	2007	2008	2009	2010
Number of Service Accounts	74,779.0	75,227.0	76,661.0	76,852.0	76,899.0	76,508.0
Total Water Production (MG)(1)	25,720.0	25,660.0	25,886.0	25,182.0	23,824.0	21,712.0
Capacity (MGD)(2)	166.0	166.0	166.0	166.0	166.0	166.0
Peak Daily Distribution (MGD)	129.8	125.0	115.4	116.5	113.0	110.0
Average Daily Distribution (MGD)	70.4	69.8	70.9	68.8	65.3	59.5

(1) "MG" means million gallons.

(2) "MGD" means million gallons daily.

**CITY WATER UTILITY SYSTEM**  
**Service Area Total Production (Billion Gallons)**  
**(Calendar Years 2005 through 2010)**

Year Ending December 31	Well Water	Surface Water	Total
2005	15.13	10.59	25.72
2006	14.69	10.92	25.61
2007	13.97	11.92	25.89
2008	14.74	10.44	25.18
2009	14.14	9.69	23.83
2010	11.32	10.39	21.71

**CITY WATER UTILITY SYSTEM**  
**Comparison of**  
**Average Monthly, Water Rates**  
**Flat Rate (1" Service)**  
**As of July 1,2009**

<u>City</u>	<u>Flat Rate Typical Home</u>
<b>Modesto</b>	<b>\$37.23-\$42.31</b>
Stockton(1)	44.25
Tracy(2)	56.65
Turlock(3)	31.50
Sacramento	29.87
Merced	45.93

(1) All water is metered. A monthly base rate of \$22.75 plus an estimated monthly consumption of 25 units (CCF) (consumption charges is \$0.82 per ccf), are used to calculate the average monthly water charges.

(2) Rates change depending on season; summer rates (May-October) and winter rates (November-April).

(3) Based on a typical 7 room dwelling (one living room, 3 bedrooms 2 bathrooms and 1 kitchen) and a lot size 7,500 sqf.

**CITY OF MODESTO**  
**CONTINUING DISCLOSURE REQUIREMENTS**  
**Year Ended June 30, 2010**

The following table sets forth connection fees for all users except multi-family units by meter size for year 2009-2010

**CITY WATER UTILITY SYSTEM**  
**Connection Fees for All users**  
**Except Multiple Family Units**  
**(Fiscal Year 2009-2010)**

<u>Meter Size</u>	<u>Connection Fees</u>
5/8" meter**	\$2,175
1" meter	5,436
1-1/2" meter	10,873
2" meter	17,395
3" meter	34,789
4" meter	54,359
6" meter	108,717
8" meter	173,947
10" meter	250,049
12" meter	467,482

\*\*NOTE- Single-family residences qualify for the 5/8" connection fee only under the following conditions:

Single story, single-family residences on a lot of 4,000 square feet or less.

Two-story single family residence on a lot of 4,000 square feet or less, provided the request for such a service accompanied by a report from a licensed professional engineer that certifies that the 5/8" service is adequate to meet the needs of the proposed dwelling.

A 5/8" "service" shall not be allowed for a single-family dwellings of greater than 2 stories on lots less than 4,000 square feet.

**CITY OF MODESTO**  
**CONTINUING DISCLOSURE REQUIREMENTS INFORMATION**  
Year Ended June 30, 2010

**CITY WATER UTILITY SYSTEM**  
**Sale of Water**  
**(Fiscal Year Ended June 30, 2010)\***

	2005	2006	2007	2008	2009	2010
Revenues (\$000)						
Residential (Flat Rates)	\$19,117	\$26,591	\$30,716	\$31,495	\$30,585,450	\$21,256,928
Commercial, Industrial and Municipal (Metered)	10,847	14,516	17,006	17,890	20,445,393	28,758,412
Total Water Sales	<u>\$29,964</u>	<u>\$41,107</u>	<u>\$47,722</u>	<u>\$49,385</u>	<u>\$51,030,843</u>	<u>\$50,015,340</u>

The table below sets forth the adopted single family residential flat rates approved through fiscal year 2008-09.

**CITY WATER UTILITY SYSTEM**  
**Monthly Single Family Residential Flat Water Rates (1)**

Lot Size	Effective July1,2005	Effective July 1, 2006	Effective July 1,2007	Effective July 1, 2008	Effective July 1, 2009
0-5,000 sq. ft. lot	\$29.36	\$33.77	\$35.45	\$37.23	\$37.23
5,001-7,000 sq. ft. lot	33.37	38.38	40.30	42.31	42.31
7,001-11,000 sq. ft. lot	39.60	45.54	47.82	50.21	50.21
11,001-17,000 sq. ft. lot	42.40	48.34	50.76	53.30	53.30
over 17,000 sq. ft. lot	49.42	56.84	59.68	62.66	62.66

(1) Single family residential properties with water meters that are read for billing purposes, are charged the meter water rate.

NOTE: The City has elected to show only five years of data for these schedules.

NOTE: Additional financial information available at [www.modestogov.com](http://www.modestogov.com)

**CITY OF MODESTO**  
**CONTINUING DISCLOSURE REQUIREMENTS INFORMATION**  
**Year Ended June 30, 2010**

The following table sets forth the adopted monthly service charge and volume charge for commercial accounts through fiscal year 2009/10.

**CITY WATER UTILITY SYSTEM**  
**Water Rates and Charges**  
**Commercial Accounts**

	<b>Effective July 1, 2005</b>	<b>Effective July 1, 2006</b>	<b>Effective July 1, 2007</b>	<b>Effective July 1, 2008</b>	<b>Effective July 1, 2009</b>
<b>Volume-based Rate (\$/hcf)</b>	\$1.01	\$1.16	\$1.22	\$1.28	\$1.28
<b>Fixed Monthly Meter Charge (in addition to volume-based charges)</b>					
5/8"-3/4" meter	\$10.82	\$12.44	\$13.06	\$13.71	\$13.71
1" meter	15.34	17.64	18.52	19.45	19.45
1-1/2" meter	26.55	30.53	32.06	33.66	33.66
2" meter	40.06	46.06	48.37	50.79	50.79
3" meter	76.12	87.53	91.91	96.51	96.51
4" meter	116.63	134.13	140.83	147.88	147.88
6" meter	229.14	263.51	276.68	290.51	290.51
8" meter	364.19	418.82	439.76	461.75	461.75
10" meter	521.80	600.07	630.08	661.58	661.58
12" meter	971.95	1,117.74	1,173.62	1,232.31	1,232.31

Note: The City has elected to show only five years of data for these schedules  
Note: Additional financial information is available at [www.modestogov.com](http://www.modestogov.com)

\$47,625,000  
CITY OF MODESTO, CALIFORNIA  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

CERTIFICATE REGARDING CITY RESOLUTION

I, Stephanie Lopez, hereby certify that I am the City Clerk of the City of Modesto (the “City”), a charter city and municipal corporation duly organized under the Constitution and the laws of the State of California, and that as such I am authorized to execute this Certificate on behalf of the City.

I hereby further certify that the attached resolution is a full, true and correct copy of Resolution No. 2014-213 (the “Resolution”), adopted at the regular meeting of the City Council of the City held on June 3, 2014, of which meeting all of the members of the City Council of the City had due notice and at which a quorum was present and acting throughout.

I hereby further certify that I have carefully compared the same with the original Resolution so adopted at said meeting and that it is a full, true and correct copy of said Resolution; and that said Resolution has not been amended, modified or rescinded since the date of adoption and is now in full force and effect.

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Dated: June 5, 2014

CITY OF MODESTO

By: Stephanie Lopez  
Stephanie Lopez  
City Clerk

RESOLUTION TO COME -

Per Modesto Clerk's Office on 6/5/2014 – The Resolution is still out for signature and will be available in one week's time.

\$47,625,000  
CITY OF MODESTO, CALIFORNIA  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

CERTIFICATE REGARDING AUTHORITY RESOLUTION

I, Stephanie Lopez, hereby certify that I am the Secretary of the Commission of the Modesto Public Financing Authority (the "Authority"), a joint exercise of powers authority organized under the laws of the State of California, and that as such I am authorized to execute this Certificate on behalf of the Authority.

I hereby further certify that the attached resolution is a full, true and correct copy of Resolution No. \_\_-2014 (the "Resolution"), adopted at the special meeting of the Commission of the Authority held on June 3, 2014, of which meeting all of the members of the Governing Board had due notice and at which a quorum was present and acting throughout.

I hereby further certify that I have carefully compared the same with the original Resolution so adopted at said meeting and that it is a full, true and correct copy of said Resolution; and that said Resolution has not been amended, modified or rescinded since the date of adoption and is now in full force and effect.

[THE REMAINDER OF THIS PAGE INTENTIONALLY LEFT BLANK.]

Dated: June 5, 2014

MODESTO PUBLIC FINANCING AUTHORITY

By: Stephanie Lopez  
Stephanie Lopez  
Secretary

RESOLUTION TO COME -

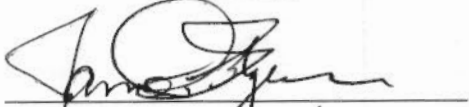
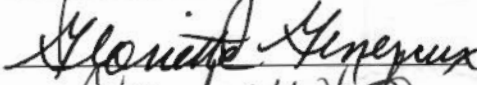
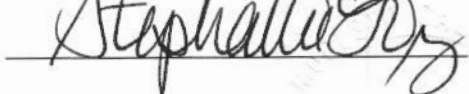
Per Modesto Clerk's Office on 6/5/2014 – The Resolution is still out for signature and will be available in one week's time.

\$47,625,000  
CITY OF MODESTO, CALIFORNIA  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

CLOSING, SIGNATURE AND INCUMBENCY CERTIFICATE OF THE CITY

The undersigned, the Interim City Manager, Finance Director and City Clerk, respectively, of the City of Modesto (the "City"), a charter city and municipal corporation duly organized and existing under the laws of the State of California, hereby certify on behalf of the City, in connection with the City's Water Revenue Certificates of Participation, 2008 Series A (the "Certificates"), as follows:

1. The officers identified below are duly authorized by the City Council of the City to execute on behalf of the City, certain documents, certificates and agreements relating to the Certificates and that pursuant to such authority certain documents, certificates and agreements have been executed by such persons, and attested to by the signature of the City Clerk of the City, and, each of the undersigned by their signature confirms that the other signatures set forth below are genuine:

<u>Name</u>	<u>Official Title</u>	<u>Signature</u>
James N. Holgersson	Interim City Manager	
Gloriette Genereux	Finance Director	
Stephanie Lopez	City Clerk	

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2. The undersigned further certify that the following persons are now, and at all times since June 1, 2014 have been, the duly appointed or elected, qualified and acting members of the City Council:

<u>Name</u>	<u>Office</u>
Garrad Marsh	Mayor
John Gunderson	Councilmember
Tony Madrigal	Councilmember
Dave Lopez	Councilmember
Bill Zoslocki	Councilmember
Jenny Kenoyer	Councilmember
David Cogdill	Councilmember

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Dated: June 5, 2014

CITY OF MODESTO

By: *Gloriette Genevex*  
Gloriette Genevex  
Finance Director

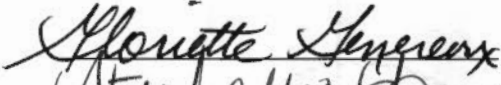
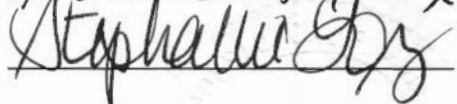
By: *Stephanie Lopez*  
Stephanie Lopez  
City Clerk

\$47,625,000  
CITY OF MODESTO, CALIFORNIA  
WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A

CLOSING, SIGNATURE AND INCUMBENCY CERTIFICATE OF THE AUTHORITY

The undersigned, the Auditor and Treasurer, Secretary and Assistant Counsel to Authority, respectively, of the Modesto Public Financing Authority (the "Authority"), a joint exercise of powers authority organized under the laws of the State of California, hereby certify on behalf of the Authority, in connection with the City's Water Revenue Certificates of Participation, 2008 Series A (the "Certificates"), as follows:

1. The officers identified below are duly authorized by the Commission of the Authority (the "Commission") to execute on behalf of the Authority, certain documents, certificates and agreements relating to the Certificates, and that pursuant to such authority certain documents, certificates and agreements have been executed by such persons, and attested to by the signature of the Secretary of the Commission, and, each of the undersigned by their signature confirms that the other signatures set forth below are genuine:

<u>Name</u>	<u>Official Title</u>	<u>Signature</u>
Gloriette Genereux	Auditor and Treasurer	
Stephanie Lopez	Secretary	

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2. The undersigned further certify that the following persons are now, and at all times since June 1, 2014 have been, the duly appointed or elected, qualified and acting members of the Commission of the Authority:

<u>Name</u>	<u>Position</u>
Garrad Marsh	Chairperson
John Gunderson	Vice Chairperson
Tony Madrigal	Member
Dave Lopez	Member
Bill Zoslocki	Member
Jenny Kenoyer	Member
David Cogdill	Member

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Dated: June 5, 2014

MODESTO PUBLIC FINANCING AUTHORITY

By: *Gloriette Genereux*  
Gloriette Genereux  
Auditor and Treasurer

By: *Stephanie Lopez*  
Stephanie Lopez  
Secretary

***NOTICE OF EXTENSION OF CREDIT FACILITY***

***\$47,625,000***

***CITY OF MODESTO, CALIFORNIA***

***WATER REFUNDING REVENUE CERTIFICATES OF PARTICIPATION  
2008 SERIES A***

**NOTICE IS HEREBY GIVEN** to the parties listed on Exhibit A hereto and the Holders of the above captioned certificates (the “Certificates”) pursuant to the applicable provisions of the governing documents of the Bonds that the Stated Expiration Date of Irrevocable Transferable Letter of Credit No. CPCS-923992 dated July 14, 2011, has been extended to July 14, 2017. No mandatory tender for purchase of any outstanding Certificates will be effected by such extension.

By: The Bank of New York Mellon Trust Company, N.A.,  
as Trustee

Dated: June 6, 2014

**EXHIBIT A  
NOTICE PARTIES**

**Authority**

Modesto Public Financing Authority  
c/o City of Modesto  
1010 Tenth Street, Suite 5200  
Modesto, CA 95353  
Attention: Auditor and Treasurer  
Telephone: (209) 577-5371  
Facsimile: (209) 571-5880

**City**

City of Modesto  
1010 Tenth Street, Suite 5200  
Modesto, CA 95353  
Attention: Finance Director  
Telephone: (209) 577-5371  
Facsimile: (209) 571-5880

**Rating Agencies**

Standard and Poor's  
Attn: Muni Structured Finance  
55 Water Street, 38th Floor  
New York, New York 10041  
Telephone: (212) 438-2000  
Email: Pubfin\_structured@standardandpoors.com

Moody's Investors Services  
7 World Financial Center  
New York, New York 10007  
Attention: Public Finance Department  
Facsimile: (212) 553-4090

**Certificate Insurer**

Assured Guaranty Corp.  
1325 Avenue of the Americas  
New York, New York 10019  
Attention: General Counsel  
Facsimile: (212) 581-3268

Assured Guaranty  
1325 Avenue of the Americas  
New York, New York 10019  
Attention: Risk Management Department – Public  
Finance Surveillance  
Facsimile: (212) 581-3268

**Remarketing Agent**

J.P. Morgan Securities LLC  
383 Madison Avenue, Floor 8  
New York, New York 10179  
Attention: Municipal Short Term Desk  
Telephone: (212) 834-7224  
Facsimile: (917) 456-3541

**CITY OF MODESTO  
SERIES 2008 WATER CERTIFICATES OF PARTICIPATION  
LETTER OF CREDIT EXTENSION**

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**DISTRIBUTION LIST  
(As of May 8, 2014)**

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**ISSUER**

**City of Modesto Department of Finance**

**Gloriette Genereux**, *Director of Finance*

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Fax: (209) 571-5880

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Fax: (209) 571-5880

**Diane Rambo**, *Executive Assistant*

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Tel: (209) 577-5369

Fax: (209) 571-5880

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San Francisco, CA 94104

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Cell: (415) 516-2779

Fax: (415) 397-4621

Theresa Willey, Secretary to Eric Tashman

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**Gisele Rainer**

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**Preston Swapp**

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Tel: (415) 772-7427

**Tara Mendez**

Email: [tmendez@sidley.com](mailto:tmendez@sidley.com)

Tel: (415) 772-7498

**CITY OF MODESTO  
SERIES 2008 WATER CERTIFICATES OF PARTICIPATION  
LETTER OF CREDIT EXTENSION**

Page 2

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50 California Street, Suite 2300  
San Francisco, CA 94111

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Tel: (415) 982-5544  
Fax: (415) 982-4513

**Sam Becerra**, *Senior Managing Consultant*  
Email: [becerras@pfm.com](mailto:becerras@pfm.com)

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Fax: (415) 982-4513

**Kevin Dong**, *Analyst*  
Email: [dongk@pfm.com](mailto:dongk@pfm.com)

Tel: (415) 982-5544  
Fax: (415) 982-4513

**FACILITY PROVIDER**

**J.P. Morgan**  
383 Madison Ave., 8<sup>th</sup> Floor (NY1-M076)  
New York, NY 10179

**James G. Millard**, *Executive Director*  
Email: [james.g.millard@jpmchase.com](mailto:james.g.millard@jpmchase.com)

Tel: (212) 270-2198  
Fax: (917) 456-3538

**Michael P. Hayes**  
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Tel: (212) 270-1050

**David J. Campbell**  
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Tel: (212) 270-0567  
Fax: (917) 456-3212

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Tel: (212) 270-0763  
Fax: (917) 456-3212

**BANK COUNSEL**

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1800 Century Park East, 8<sup>th</sup> Floor  
Los Angeles, CA 90067-1501

**Neil W. Rust**  
Email: [NRust@mcguirewoods.com](mailto:NRust@mcguirewoods.com)

Tel: (310) 315-8240  
Fax: (310) 956-3106

**CITY OF MODESTO  
SERIES 2008 WATER CERTIFICATES OF PARTICIPATION  
LETTER OF CREDIT EXTENSION**

Page 3

**REMARKETING AGENT**

**J.P. Morgan Securities LLC**  
383 Madison Avenue, 8<sup>th</sup> Floor  
New York, NY 10179

**Peter McCarthy**  
Email: [peter.mccarthy@jpmorgan.com](mailto:peter.mccarthy@jpmorgan.com)

Tel: (212) 834-7224  
Fax: (917) 456-3541

**TRUSTEE**

**The Bank of New York Mellon Trust Company, N.A.**  
100 Pine Street, Suite 3100  
San Francisco, CA 94111

**Sheila A. Bowman, VP**  
Email: [Sheila.Bowman@NYMellon.com](mailto:Sheila.Bowman@NYMellon.com)

Tel: (415) 263-2426  
Fax: (415) 399-1647

**Eladia Burgos**  
Email: [eladia.burgos@bnymellon.com](mailto:eladia.burgos@bnymellon.com)

**Chris Davy**  
Email: [chris.davy@bnymellon.com](mailto:chris.davy@bnymellon.com)

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[michael.p.hayes@jpmorgan.com](mailto:michael.p.hayes@jpmorgan.com); [david.j.campbell@jpmchase.com](mailto:david.j.campbell@jpmchase.com);  
[Selina.Au.Yang@jpmorgan.com](mailto:Selina.Au.Yang@jpmorgan.com); [NRust@mcguirewoods.com](mailto:NRust@mcguirewoods.com); [peter.mccarthy@jpmorgan.com](mailto:peter.mccarthy@jpmorgan.com);  
[Sheila.Bowman@NYMellon.com](mailto:Sheila.Bowman@NYMellon.com); [eladia.burgos@bnymellon.com](mailto:eladia.burgos@bnymellon.com); [chris.davy@bnymellon.com](mailto:chris.davy@bnymellon.com)