2013-2014

OPERATING BUDGET

CITY MANAGER'S
2013-2014
BUDGET MESSAGE

CITY MANAGER'S 2013-2014 BUDGET MESSAGE



May 1, 2013

Honorable Mayor and City Council:

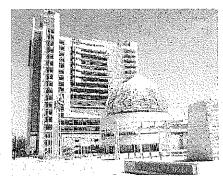
I am relieved and grateful to present another balanced budget that builds on the progress achieved in the current year and reflects the benefits resulting from the difficult decisions in recent years. The City Manager's 2013-2014 Proposed Operating Budget continues our commitment to the prudent rebuilding of services that we were able to start last year. It also continues our multi-year approach to ensuring fiscal stability by setting aside reserves that are sufficient to address the small projected General Fund shortfall in 2014-2015.

With strategic fiscal reform, moderate increases in revenues from a stronger economy, and the very careful management of expenses, the City's budget continues to stabilize with revenues and expenditures in close alignment. As a result, we were not faced with the challenge of closing a massive shortfall as we had to do every year, but one, over the past 11 years. With the improved forecast this year, I am proposing a budget that holds the line with a limited number of new proposals, avoids service cuts, and allows for small potential increases in employee compensation. These small compensation increases have been made possible, however, due to funds that are currently only available because of the lowering or elimination of certain significant costs. Were it not for these changes, these resources would not be available as discussed later in this message. The Proposed Budget also includes specific reductions in areas where service delivery efficiencies and cost savings can be obtained with no service level impacts.

Despite our good progress, significant work toward long-term fiscal reform remains ahead of us until we achieve a more desirable level of budget stability, with services at a higher level than currently provided. We still continue to have significant budgetary challenges and uncertainties facing us, and our current reduced service levels fall short of community expectations.

With those challenges in mind and the many competing demands for limited resources, we used a balanced approach to develop the Proposed Budget that focuses on the following goals:

- Achieving budget and service level stability;
- Targeting investments to meet priority needs of the community; and
- Continuing service delivery efficiencies and strategies for cost reduction and revenue growth.



Community Budget Meetings

May 1 - May 30

Budget Decision Milestones

May 8-16

City Council Study Sessions on 2013-2014 Proposed Budgets

May 14/June 10

Public Hearings on the 2013-2014 Proposed Budgets and Fees and Charges

May 31

2013-2014 Mayor's June Budget Message Released

June 11

City Council Review and Approval of the 2013-2014 Mayor's June Budget Message

June 18

Adoption of the 2013-2014 Capital and Operating Budgets, 2014-2018 Capital Improvement Program, and the 2013-2014 Fees and Charges

General Fund Budget is Stabilizing

Over the next five years, very small shortfalls and a surplus are projected annually as shown in Table 1 below. These variances represent less than 1% of the projected General Fund budget (revenues and expenditures).

	ental Surplu	eneral Fund s/(Shortfall) (Table 1)		s)¹	-
	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018
Incremental Surplus/(Shortfall)	(\$3.8 M) ²	(\$13.7 M)	\$2.0 M	(\$4.7 M)	(\$6.0 M)
% of Annual Budget	(0.21%)	(0.78%)	0.11%	(0.25%)	(0.31%)

- Includes proposed Employee Compensation Planning Reserve, as well as salary steps for eligible non-management employees and management performance pay, and anticipated savings from first-year implementation of some elements of the Fiscal Reform Plan and Measure B retirement changes approved by voters in June 2012. Does not include impacts associated with elements of the Fiscal Reform Plan/Measure B that are not yet implemented; tax increment funding for the Successor Agency to the Redevelopment Agency, a public entity, regarding the outcome of litigation with the County of Santa Clara related to the PERS and Water District levies; costs associated with fully funding the annual required contributions for police and fire retiree health care; costs associated with restoration of key services funded on a one-time basis in 2012-2013; costs associated with the restoration of key services to January 2011 levels; costs associated with unmet/deferred infrastructure and maintenance needs; or one-time revenues/expenses.
- This figure excludes the Development Fee Programs and was revised from the \$5.5 million shortfall presented in the February 2013 Forecast as a result of the continued analysis and updating of projected revenues and expenditures. With a surplus of \$1.2 million in the Development Fee Programs, the net General Fund shortfall addressed in the 2013-2014 Proposed Budget totals \$2.6 million.

Balanced Approach to Achieving Stability and Meeting Service Delivery Needs

Consistent with the 2012-2013 Adopted Budget, as directed by the City Council's approval of the 2013-2014 Mayor's March Budget Message, this Proposed Budget includes a two-year approach to balancing this year's budget. To this end, we have set aside \$13.7 million in one-time funds to address the projected shortfall in 2014-2015. The Proposed Budget also reflects the ongoing commitment to operate the four new branch libraries and a new community center that we were able to finally open in the current year. These neighborhood enhancements were constructed with General Obligation bonds approved by San José voters in 2000 and were completed up to three years ago.

This Proposed Budget includes the following welcome news:

- We will continue to address the most immediate and critical of the City's unmet or deferred
 infrastructure needs through one-time funding, although the backlog of maintenance and
 replacement remains very long.
- We will provide for limited service enhancements, including the opening of the South San José Police Substation that will improve police service levels and deliver better operational efficiencies for the department. The new substation was built with General Obligation bonds approved by voters in 2001, and the building was completed over two years ago.

2013-2014 PROPOSED OPERATING BUDGET MESSAGE

Balanced Approach to Achieving Stability and Meeting Service Delivery Needs (Cont'd.)

- We will set aside one-time reserve funding for budget stabilization, potential legal obligations to the City associated with the elimination of the Redevelopment Agency and the creation of the Successor Agency to the Redevelopment Agency, Essential Services, as well as potential expenses related to the ongoing implementation of the Fiscal Reform Plan.
- We will continue services that had been funded on a one-time basis in 2012-2013.
- We will add resources to meet the increased demand for development services and to invest in systems to improve efficiencies for these services in the future.
- We will continue to identify and implement service delivery alternatives that will provide efficiencies to help us reduce costs and/or improve service levels and their quality.
- We will set aside \$11.1 million for an Employee Compensation Reserve so that we can start addressing the painful cuts endured by employees in recent years, and to enhance the City's ability to be a competitive and attractive employer for the talented and skilled staff we need to deliver community services.

Planning for Uncertainties

While there is always a certain level of uncertainty in the development of a budget, two elements incorporated into the Proposed Budget are the subject of current litigation that could have a significant impact on our budget balancing plan. These include legal challenges to elements of retirement reform, including those approved by San José voters with the passage of Measure B in June 2012. In addition, litigation with the County of Santa Clara related to the withholding of Successor Agency to the Redevelopment Agency tax increment associated with the PERS and Water District levies is not yet resolved. In light of these major uncertainties, we have developed two contingency plans totaling \$33.5 million (of which \$22.7 million would need to be rebalanced ongoing) to address potential adverse decisions that could create a shortfall in the 2013-2014 Proposed Budget. These contingency plans are summarized in the Budget Strategies discussion below and included as Exhibits 1 and 2 to this document.

Continued Focus on Fiscal Reform Plan Efforts

The elements in the Proposed Budget represent genuine progress, but they are also a reminder that we must remain very disciplined and committed to the path of fiscal reform. Unfortunately, we still do not have the financial capacity to restore key service levels that we cut in recent years back to prior levels, and then continue to sustain them for the long term. We are addressing only a small part of our significant backlog of infrastructure and maintenance needs. Although this budget does include a small reserve to provide potential raises for our employees, it would not fully restore the significant reductions in compensation sacrificed by our City employees. We will continue to be understaffed in key areas, including those that provide direct services to our community as well as those that provide internal support to our operating departments.

Retirement costs, including both pension and retiree healthcare, remain a major cost factor in this budget. For 2013-2014, retirement costs are projected to total \$212.9 million in the General Fund,

Continued Focus on Fiscal Reform Plan Efforts (Cont'd.)

which is almost 14% above the 2012-2013 level of \$187.1 million. Retirement costs represent 23% of total General Fund expenditures in the 2013-2014 Proposed Budget. In the 2014-2018 Forecast, General Fund retirement costs are projected to increase an additional 21% from 2013-2014 to 2017-2018.

Controlling the growth in retirement costs remains a critical priority for the City in order to achieve financial stability and ensure appropriate levels of service to the community. Measure B was designed to control these costs, and it amended the City Charter in order to reduce costs of the City's pension plans for current and future employees. Elements of Measure B have been challenged with litigation, and final rulings by the courts could occur in the coming year or beyond. When finally implemented, the pension plan for existing employees will increase the employee share towards the cost of the current level of pension benefits or create a new "opt-in" plan for current employees that would reduce both the costs and benefits for participating employees going forward. General Fund savings estimated at approximately \$48 million annually would be realized from the increase in the employee contributions after the planned four-year implementation period. Because this change has not yet been implemented, however, these savings have not been factored into this Proposed Budget.

For non-sworn employees hired on or after September 30, 2012, a second-tier pension benefit went into effect that will address the long-term financial sustainability of the City's retirement benefit. A Tier 3 is also an option that was put in place for unrepresented management and professional employees hired into Unit 99 on or after February 3, 2013. Tier 3 provides for a defined contribution plan in lieu of participating in Tier 2 of the Federated Retirement Plan. The Administration also has been in negotiations with the two public safety unions to establish a second-tier pension benefit for newly hired sworn staff. The City and the San Jose Police Officers' Association (SJPOA) recently reached an agreement establishing a Tier 2 program for new employees represented by the SJPOA, which will soon be implemented. The City and the San José Firefighters have been unable to reach an agreement and the City has a motion to compel arbitration pending. While the City faces challenges in implementing retirement reform, I am confident that we are on the right path for moderating the growth in retirement costs, and the steps we have already taken have been necessary and effective.

Pursuing additional revenues is also a major strategy to help achieve budget stability. Despite the ongoing recovery of the Silicon Valley economy, the City's revenue collections do not always keep pace due to the outdated structure of many of our revenues. San José, like many cities, relies heavily on Sales Tax and Property Tax receipts to support General Fund services. We are projecting modest revenue increases, but cities in general continue to lose ground with the shift to a service-based economy as those services are not taxed. With property taxes, Proposition 13 passed by the voters in 1978 limits the growth in receipts and constrains the ability of cities to increase them. The City's two largest General Fund revenue sources, sales and property taxes, account for approximately half of our General Fund revenues, and together they pay for only 80% of our Police and Fire services combined.

We have made extraordinary progress in cost containment through painful cuts to service levels, employee staffing levels, and employee compensation, as well as leading the State and nation in

Continued Focus on Fiscal Reform Plan Efforts (Cont'd.)

meaningful retirement reform. However, we have not yet taken comparable steps to increase revenues, although we continue to aggressively and strategically seek economic development that has the long term potential to generate revenue. Both the 2008 General Fund Structural Deficit Elimination Plan and the Fiscal Reform Plan approved in May 2011 identified new revenue as a key part of the City's long-term strategy to enable the City to rebuild its capacity and begin to restore service levels, but this budget does not assume any increase in local taxes, with the exception of the Marijuana Business Tax, bringing that tax rate from 7% to 10% of gross receipts. The City Council may consider opportunities for bringing additional revenues to the voters in the coming year.

Total Proposed Budget

In the 2013-2014 Proposed Budget, the total net funding is \$2.6 billion for all City funds (General, Special, and Capital). This is \$136.8 million (4.9%) below the 2012-2013 Adopted Budget (Table 2 below). The major factors contributing to this decline include: 1) the Proposed Budget does not yet include funds that will be rebudgeted and added to the final Adopted Budget to complete multi-year projects; and 2) a smaller Airport Capital Program which has contributed to a large decline in Capital Funds.

2013-2014 Proposed Budget — All Funds (Table 2)				
	2012–2013 Adopted	2013–2014 Proposed	% Change	
General Fund	\$ 966,690,580	\$934,008,927	(3.4%)	
Special Funds	1,472,249,982	1,514,091,407	2.8%	
<less: operating="" transfers=""></less:>	(521, 7 99,24 3)	(547,757,849)	5.0%	
Net Operating Funds	1,917,141,319	1,900,342,485	(0.9%)	
Capital Funds	863,721,527	748,245,102	(13.4%)	
<less: capital="" transfers=""></less:>	(3,941,000)	(8,482,000)	115.2%	
Net Capital Funds	85 9 ,78 0 , 527	739,763,102	(14.0%)	
Total	\$ 2,776,921,846	\$2,640,105,587	(4.9%)	

Position Impacts

This Proposed Budget includes increases to staffing levels to support police services, development fee programs, continuation of one-time activities funded in 2012-2013, and limited enhancements to other critical services. At the same time, however, targeted reductions are proposed in other programs where alternative models for service delivery that are more cost-effective have been identified or special funding is no longer available. Overall, the level of staffing will increase by a net 129 positions, from 5,522 full time equivalent positions in the 2012-2013 Adopted Budget to 5,651 positions in the 2013-2014 Proposed Budget as shown in the Table 3 below. This 2.3% increase still leaves City staffing 24% below its peak of almost 7,500 positions in 2001-2002.

Position Impacts (Cont'd.)

Changes in Position Count from 2012-2013 Adopted to 2013-2014 Proposed Budget (Table 3)		
2012-2013 Adopted Budget	5,522 positions	
2013-2014 Base Budget Changes	20 positions	
2013-2014 Proposed Budget Changes	109 positions	
Total Net Position Changes	129 positions	
2013-2014 Proposed Budget	5,651 positions	

Employee Compensation

As a service organization, City employees are critical in the delivery of quality services to our community. In order to maintain service level stability, it is very important that we retain and attract quality employees. In recognition of this important goal, the 2013-2014 Proposed Budget includes funding \$14.28 million in the General Fund (\$19.43 million in all funds) for compensation increases as shown in the Table 4 below.

2013-2014 Proposed Budget Funding for Compensation Increases (Table 4)			
	General Fund	All Funds	
Employee Compensation Planning Reserve*	\$11.10 M	\$14.78 M	
Automatic Step Increases	2 .04 M	2.31 M	
Management Pay for Performance	1.14 M	2.34 M	
2013-2014 Compensation Increases	\$14.28 M	\$19.43 M	

^{*} The allocation of the Employee Compensation Planning Reserve is subject to negotiations with the City's bargaining units.

Balancing the Budget

As displayed in Table 5 on the following page, the 2013-2014 Proposed General Fund Budget Balancing Plan includes recommendations that address the overall \$2.6 million shortfall, which includes a general shortfall of \$3.8 million combined with a \$1.2 million surplus for the cost-recovery Development Fee Programs. This table shows the matrix of balancing strategies and the dollars associated with each action. A complete discussion of the balancing strategies can be found in Attachment A and throughout the Proposed Budget. Attachment B also responds to the directives contained in the Mayor's March Budget Message that was approved by the City Council. Proposed Budget actions that respond to City Auditor referrals is included in Attachment C.

2013-2014 Proposed Operating Budge General Fund Budget Balancing Plan (in ((Table 5))	persona are en Pres	
	2 0′	13-2014	On	going
2013-2014 General Fund Shortfall	(\$	3,844)	(\$	3,844)
Development Fee Program Impact	•	1,222		1,222
Revised Base Budget Forecast	(\$	2,622)	(\$	2,622)
Balancing Strategy				
Source of Funds				
Available Fund Balance:				
2013-2014 Future Deficit Reserve Elimination	\$	29,400	\$	0
SARA City Subsidy (12-13/13-14 cash flow)		6,400		0
Police Department Overtime Reserve		4,000		Ö
Tobacco Settlement Revenue		3 ,500		. 0
Development Fee Reserves		2,569	İ	2,268
Additional 2012-2013 Ending Fund Balance		5,150		0
Grants/Reimbursements/Fees:				
SAFER Grant 2010 Extension		2,313	İ	0
Development Fee Program Technology Fee		717		717
Other Reimbursements/Fee Activity		915		548
Other Revenue Changes:				
Medical Marijuana Tax Rate Increase (7% to 10%)		1,500		1,500
Vendor Payment Automation/Revenue Sharing		250		500
Transfers and Reimbursements:				
Overhead Reimbursements		855		790
Transfers from Other Funds		(786)		100
Subtotal Source of Funds	\$	56,783	\$	6,423
Use of Funds				
2014-2015 Future Deficit Reserve	\$	13,700	\$	0
Unmet/Deferred Infrastructure and Maintenance		15,160	1	0
Service Level Enhancements		10, 3 17		5,717
Other Reserves (Budget Stabilization, SARA City Legal Obligations, Essential Services, Fiscal Reform Plan Implementation)		9,850		0
2012-2013 One-Time Funded Services		6,602		3 ,146
Development and Other Fee Programs/Grants		4,821		3,822
Use of Reserves (Committed Additions/Deferred Infrastructure)		(2,634)		(2,782)
Service Delivery Efficiencies/Cost Reductions		(3,655)	_	(6,102)
Subtotal Use of Funds	\$	54,161	\$	3,801
Total Balancing Strategy	\$	2,622	\$	2,622
Remaining Balance	\$	0	\$	0

In preparing the 2013-2014 Proposed Operating Budget, the Administration followed budget balancing strategy guidelines in the City Manager's Budget Request for Fiscal Year 2013-2014 and adopted by the City Council as part of the approval of the Mayor's March Budget Message. As we continue to stabilize the City's budget and implement elements of the Fiscal Reform Plan, it is important that the City take a holistic approach regarding the restoration of services as additional

resources become available. The Service Restoration Decision-Making Framework and the City Council-approved Guiding Principles for Restoring City Service Levels provide the broader context for analyzing potential service restorations. These guidelines, framework, and principles are included in Exhibit 3 to this message.

The Service Restoration Decision Making Framework provides a multi-pronged approach that considers various factors, including the adequacy of resources for strategic support, infrastructure and maintenance; efficient service delivery methods; service delivery goals and current performance status; service level sustainability; and staffing. The Guiding Principles for Restoring City Service Levels approved last year by the City Council provide direction to help the City determine not only the appropriate service levels and most cost-effective method for service delivery, but also critical areas for investment. The principles extend beyond the January 1, 2011 service restoration goals identified in the Fiscal Reform Plan (included in Exhibit 3) to include further considerations such as infrastructure maintenance, technology improvements, and alternative service delivery models. These principles fall into three general categories: ensure the fiscal soundness of the City; choose investments that achieve significant outcomes; and improve the efficiency and effectiveness of service delivery.

As mentioned previously, three main themes were central in the development of the 2013-2014 Proposed Budget:

- Achieve budget and service level stability;
- Targeting investments to meet priority needs of the community; and
- Continue service delivery efficiencies and strategies for cost reduction and revenue growth.

Detailed information about budget proposals and performance outcomes is included in the sections for specific City Service Areas and departments.

BUDGET/SERVICE LEVEL STABILITY

As the City's budget continues to stabilize, it is important to ensure that this hard-earned achievement can be maintained for the delivery of priority services to our community. To this end, we recommend several actions in the Proposed Budget, including: establishing a 2014-2015 Future Deficit Reserve; continuing services funded on a one-time basis in 2012-2013; and increasing earmarked reserves to address potential funding needs. In addition, two contingency plans have been developed to address uncertainty regarding the outcome of litigation involving some retirement changes as well as litigation with the County of Santa Clara associated with distribution of tax increment that was withheld from the Successor Agency to the Redevelopment Agency.

The 2013-2014 Proposed Budget also includes an Employee Compensation Planning Reserve to allow for modest compensation increases. Any allocation of these funds will be determined through the negotiation process with the City's bargaining units that is currently underway. We included this reserve for the first time in many years in recognition of our need to remain competitive as an employer in a fiscally responsible manner so that we can continue to retain and attract the talent and skills necessary for quality service delivery. I regard this as an essential component for our long-term

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Balancing the Budget (Cont'd.)

organizational stability. No service reductions were necessary in 2013-2014 to accommodate this reserve funding. However, the budget included \$20 million in savings from the elimination of the Supplemental Retiree Benefit Reserve and implementation of lowest cost healthcare plan changes. Without this \$20 million in savings, the Employee Compensation Planning Reserve would not have been able to be included in the 2013-2014 General Fund Forecast. These savings are currently the subject of litigation.

Following is a discussion of some of the major budget actions that support continued budget and service level stability.

- 2014-2015 Future Deficit Reserve: Establishes a 2014-2015 Future Deficit Reserve of \$13.7 million to address the projected shortfall for 2014-2015 that was presented in the 2014-2018 General Fund Five-Year Forecast. This Reserve will provide for budget stability over the next two years.
- Continue Services Funded on a One-Time Basis in 2012-2013: The following services were funded on a one-time basis in 2012-2013. The majority of these proposals are recommended to be continued with ongoing funding in the Proposed Budget.
 - San Jose BEST and Safe Summer Initiative Programs As directed by the City Council through approval of the 2013-2014 Mayor's March Budget Message, includes funding of \$3.0 million in 2013-2014, of which \$500,000 is ongoing, and adds 4.5 positions. With the ongoing funding, a total of \$3.5 million is proposed over a two-year period to continue the City's strong support of gang prevention, intervention and suppression programs for youth through the collaborative efforts of the Mayor's Gang Prevention Task Force. With the recommended budget action, the ongoing allocation of \$2.6 million will again be increased by \$1.5 million in both 2013-2014 and 2014-2015, consistent with the 2012-2013 Budget. An additional \$500,000 would also be available on an ongoing basis starting in 2014-2015 to support these efforts.
 - Semior Wellness and Transportation Services Continues ongoing funding of \$460,000, including the addition of 1.0 Mobility Manager, for senior wellness and transportation services that was added one-time in 2012-2013. With the continuation of funding, transportation and senior nutrition options will be provided at the 14 senior community centers as well as a variety of recreation classes and resources targeted for this community.
 - Community Action and Pride (CAP) Grants Provides one-time funding of \$200,000 to continue the CAP Grant Program through 2014-2015, with \$100,000 allocated to each year. This program provides small grants to San José neighborhood groups to fund activities and projects that result in cleaner, safer, and more engaged communities.
 - Parks, Recreation and Neighborhood Services (PRNS) Volunteer Management Unit— Continues staffing additions (1.25 positions) ongoing to support the PRNS Department volunteer efforts. This program leverages approximately 24,000 volunteer hours annually.
 - Summer Recreational Swim Program for the Evergreen Community Continues funding
 on an ongoing basis to support a summer recreational swim program for the Evergreen
 community.

- San Jose Downtown Association Maintains funding for the San Jose Downtown Association (SJDA) at \$320,000 for 2013-2014 to continue its partnership with the City in activating and promoting Downtown. SJDA provides services related to downtown business retention and recruitment, promotion, and event production. (Special Funds)
- Economic Development Incentive Fund Continues one-time funding for economic development support and incentives in the amount of \$750,000. This funding will allow the City to continue planning and competing for development projects that will generate revenue and create jobs.
- Neighborhood Business Districts Continues funding of \$5,000 on an ongoing basis to each
 of nine City-recognized Neighborhood Business Districts in the City of San José, for total
 funding of \$45,000. This funding will provide small businesses the resources needed to organize
 important community and cultural events.
- Medical Marijuana Program Continues 7.5 positions (Finance, Planning, Building and Code Enforcement, Police, City Attorney's Office, and City Manager's Office) on an ongoing basis to support the Medical Marijuana Program as well as 0.5 position to support the Gaming Unit at a cost of \$1.3 million. The Medical Marijuana Program ensures collection of the Marijuana Business Tax and compliance with various City codes. This program will continue to be evaluated as related federal, state, and local legal issues evolve.
- Legal Support Staffing Continues funding on an ongoing basis for 2.0 positions that provide legal support related to the Successor Agency to the former Redevelopment Agency and the Oversight Board, increase capacity for legal transactional services to various departments, and provide support related to fiscal reform, as needed and appropriate. Also continues funding for 2.0 positions on a one-time basis to provide legal support to the Environmental Service and Public Works capital programs (Partial Capital Funds)
- Office of the City Clerk Staffing Continues 2.0 positions on an ongoing basis to assist with compliance monitoring for campaign finance, statements of economic interest, and lobbyist and City Council disclosures; support the Mayor and City Council in areas of budget, grants, and human resources; and process City contracts, grants, and agreements.
- Office of Employee Relations Fiscal Reform Staffing Continues 2.0 positions in the Office
 of Employee Relations to ensure sufficient resources are dedicated to the Fiscal Reform Plan
 efforts and labor relations issues.
- Sanitary Sewer Maintenance Management Staffing Makes permanent 4.0 positions (1.0 Analyst, 1.0 Associate Engineering Technician, 1.0 Information System Analyst, and 1.0 Systems Application Programmer) that were funded on a temporary basis in 2012-2013 in order to continue to reduce Sanitary Sewer Overflows (SSOs). (Special Funds)

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- Other Reserves: The 2013-2014 Proposed Budget includes funding to increase reserves to better position the City to address potential funding needs.
 - Budget Stabilization Reserve Establishes a Budget Stabilization Reserve of \$4.0 million to help ensure resources are available to address unforeseen changes in revenues or expenditures in any given year. Given the size of the City's budget and the relatively small General Fund Contingency Reserve, this proposed reserve is considered a prudent investment, serving as a small buffer, or bridge funding to balance the budget, if necessary. In the future, the Administration recommends that the City Council consider changing the Operating Budget and Capital Improvement Program Policy (Council Policy 1-18) to broaden the use and distribution of excess fund balance to allow for any available funds in any year to be allocated to a Budget Stabilization Reserve, as appropriate.
 - Successor Agency Legal Obligations Reserve An increase in the Successor Agency City Legal Obligations Reserve of \$2.5 million will bring the total reserve to \$10.0 million. Funds are recommended to be set aside in an amount equivalent to the value of loans made between the City and former Redevelopment Agency as part of the SERAF Loan in 2011. Although loans such as these were invalidated by AB X1 26, the approval of AB 1484 outlined that such loans may be deemed an enforceable obligation if they meet certain requirements. As the Administration continues to work through these requirements and seek clarification from the state, this action proactively sets aside funds since these loans are due and payable by June 30, 2015.
 - Fiscal Reform Plan Implementation Reserve Increases the Fiscal Reform Plan Implementation Reserve by \$1.35 million (from \$150,000 to \$1.5 million in 2013-2014).
 Additional funding will continue to be used for costs associated with implementing the Fiscal Reform Plan, particularly for costs related to litigation.
- Contingency Plans: The Administration has developed two contingency plans to address uncertainty related to the outcomes of (1) litigation related to various retirement reform efforts and (2) litigation with the County of Santa Clara related to the withholding of Successor Agency to the Redevelopment Agency (SARA) tax increment associated with the PERS and Water District levies. Depending on the outcome of these issues, these proposals may be shifted between the contingency plans, particularly if only the contingency plan related to retirement reform litigation is needed.
 - \$20 Million General Fund Contingency Plan The 2014-2018 General Fund Forecast included approximately \$20 million of ongoing General Fund savings from the elimination of the Supplemental Retirce Benefit Reserve (SRBR) and implementation of the lowest cost healthcare plan changes. These changes have been legally challenged and the SRBR is part of a trial related to Measure B in the Superior Court in July 2013. In the 2013-2014 Mayor's March Budget Message, the Administration was directed to develop a list of \$20 million of proposed ongoing and/or one-time expenditures that will not be implemented until at least 60 days after a favorable verdict is received. Exhibit 1 provides the list of budget proposals that meet this City Council direction. The largest components of this plan include the Employee Compensation Planning Reserve (\$11.1 million), the Budget Stabilization Reserve (\$4.0 million), the opening of the South San José Police Substation (net \$2.1 million after closure costs), and the Police Community Service Officers Staffing (\$1.1 million).

SARA PERS Levy/Water District Levy General Fund Contingency Plan – The 2013-2014 Proposed Budget assumes that the County of Santa Clara will not be allowed to withhold Successor Agency property tax increment to fund the County employees' retirement plan (the "PERS Levy") and Water District levy. As a result of a tentative ruling in the Sacramento Superior Court this spring, this budget presumes that the County will be ordered to remit funds withheld for the PERS and Water District levies to SARA beginning in 2012-2013 (\$7.65 million) and ongoing (approximately \$7.5 million annually). With additional tax increment available to fund SARA obligations, the anticipated General Fund subsidy of \$15.0 million in 2013-2014 can be reduced by \$13.5 million in 2013-2014 and \$2.7 million ongoing. However, if the Court ultimately determines that the County can withhold this tax increment, no change to the 2013-2014 General Fund subsidy will result. We have developed a contingency plan (Exhibit 2) that outlines General Fund budget reductions of \$13.5 million in 2013-2014 and \$2.7 million ongoing that would be necessary if SARA does not prevail. The largest components of this plan include the Police Communications Building Unmet/Deferred Infrastructure and Maintenance investments (\$3.6 million), the Operating/Capital Budget System Replacement Reserve (\$2.9 million), the SARA Legal Obligations Reserve (\$2.5 million), and the Homeless Response Team Reserve for 2014-2015 (\$1.5 million).

Targeted Investments to Meet Community Needs

With the financial condition of the City somewhat improving, we have identified a limited amount of funding for targeted investments to meet community needs. Following is a discussion of some of the recommended major budget actions for this purpose.

- Unmet/Deferred Infrastructure and Maintenance: A wide range of one-time and ongoing funding proposals will address critical replacement, repair, and maintenance at City facilities and for infrastructure. These efforts are necessary to reduce potential risk of failure, damage, or higher costs in the future.
 - Police Communications and Police Administration Buildings Adds one-time funding of \$6.6 million to address several critical infrastructure needs at the Police Communications Building, including upgrading the fire protection system that is 25 years old and has on average three false alarms a month, upgrading critical electrical systems, replacing a chiller that is 25 years old, performing waterproofing on the concrete exterior, and designing a redundant electric circuitry power system. An additional \$2.0 million is recommended to address critical needs at the Police Administration Building, including replacing a chiller that is over 40 years old, replacing two elevator controllers that have the original control systems from the 1970's, replacing the Heating, Ventilation and Air Conditioning (HVAC) controls, performing waterproofing on the concrete exterior, and replacing and reconfiguring lighting at the firing range.
 - City Hall Waterproofing Provides one-time funds of \$1.6 million to develop a plan to
 address water infiltration in the parking and basement level of City Hall, implement corrective
 actions, and ensure that power supply equipment is not compromised.

- Operating/Capital Budget Systems Replacement Reserve Establishes a \$2.85 million reserve for the replacement of the City's Operating and Capital budgeting systems. The Operating Budget System was first developed in the 1980's and lacks the basic functionality of systems that are now available. The Capital Budget System was developed in the early 2000's and, while an improvement from the Operating System, lacks functionality and integration with other systems. With the existing system, an excessive amount of staff resources throughout the City are necessary to produce the annual budget as the system does not capture all of the budget data, does not have effective user interfaces, does not provide effective tools to manage the budget development process, and does not allow the leveraging of the budget information. Because the existing operating system has undergone a series of incremental revisions over more than a decade, the system architecture does not easily allow changes and there is a risk that the system will not be able to meet changing data requirements.
- Preventative Maintenance Program Adds one-time funding of \$1.3 million and 3.0 one-time positions to extend the current Preventative Maintenance Program that was included in the 2012-2013 Adopted Budget. This action will allow the overall preventative maintenance of City facilities to be maintained for another year at the industry standard of 80% for work orders pertaining to HVAC, plumbing, lighting, energy management systems, roofing, generators, and emergency fire alert systems.
- Street Tree Maintenance Adds one-time funding of \$160,000 to remove dead or dying trees in several key locations, particularly palm trees, throughout the City. In the 2012-2013 Adopted Budget, one-time funding of \$500,000 was added for the structural pruning of approximately 5,000 (or 50%) of the 10,000 City-owned trees in median islands and roadside properties which were in need of pruning.
- Sanitary Sewer, Storm Sewer, and Municipal Water Equipment and Fleet Replacement –
 Adds 1.0 Senior Mechanic and one-time funding to add four combination cleaning vehicles for
 the Sewer Maintenance Program, as well as aging and outdated vehicles that support the Sanitary
 Sewer and Storm Sewer Programs. Also replaces four vehicles and adds a trailer to support the
 Municipal Water System operations. (Special Funds)
- Other Investments Other investments are recommended to maintain the City's facilities and technology infrastructure, including: computer server replacements and network upgrades; a real estate services document imaging and records retention system; and the renovation of the City Hall Bamboo Courtyard.
- Service Level Enhancements: A limited number of service enhancements are recommended to address the most urgent service delivery needs.
 - South San José Police Substation Provides funds for the January 2014 Phase I opening of the South San José Police Substation that will allow the Police Department to shift the Southern Patrol Division (approximately 270 sworn positions) to the facility in order to improve response times and service to the southern part of the City. This Phase I opening does not include public access to the facility. This action adds 14.0 positions and \$2.3 million in 2013-2014 (\$2.2 million ongoing). The \$2.3 million in 2013-2014 will be added to the \$3.2 million that has been funded or is expected to be funded from various law enforcement grants, bringing total resources to open the facility to \$5.5 million.

- Homeless Response Team Provides funding of \$3.3 million over a two-year period to address concerns about the growing and visible homeless encampments throughout the community. This includes the addition four Park Rangers and one Community Coordinator to provide enforcement of the encampments along Coyote Creek and near Guadalupe River Park, facilitate encampment clean-ups, and provide on-site assistance for waste disposal contractors. A Program Manager, funded by the Housing Trust Fund, will be added to focus on the broader issues of homeless encampments, impacts on neighborhoods, and connecting encampment residents with services and housing. Funding will also be allocated to property storage, waste clean-ups, security services, encampment physical deterrents such as fencing, and outreach services to distribute information, materials and supplies and to provide transportation to shelter or housing for encampment residents.
- Police Community Service Officers Staffing Adds 21.0 Community Service Officers (CSOs) as of January 2014. These positions will perform non-sworn technical and administrative support services including interviewing witnesses, photographing crime scenes, collecting evidence, taking telephone reports, conducting follow-up investigations, and fingerprinting. Each of the three patrol divisions will be assigned seven CSOs. These positions will respond to lower priority non-enforcement calls, thereby increasing capacity for existing sworn Police Officer positions to respond to higher priority calls and conduct more proactive police work.
- Police Crime Prevention Adds 3.0 Crime Prevention Specialists (CPS) in order to increase community outreach, disseminate crime prevention information to City residents, and respond to residents' concerns about crime. The additional 3.0 CPS will allow the Crime Prevention Unit to provide each of the three Patrol Divisions with 2.0 CPS as well as 1.0 CPS for citywide coordination of training and presentations.
- Police Automated Field Reporting/Records Management System (AFR/RMS) Maintenance and Operation Adds funding to the Police Department, partially offset by an earmarked reserve established in the 2014-2018 Forecast, to support maintenance and operating costs for the new Records Management System (RMS) that was implemented in July 2012 and the Automated Field Reporting (AFR) that will be implemented by July 2013. This system will create Department-wide efficiencies in the time spent by sworn positions for regular job duties.
- Police Sworn and Civilian Recruitment Activities and Firefighter Recruit Testing Adds one-time funding of \$325,000 for recruiting and hiring efforts for Police Department sworn and civilian vacancies. An additional \$125,000 is recommended for outreach, recruitment, and testing to establish a new Firefighter Recruit eligibility list that was last created in 2008.
- Police Crime Analysis Staffing Adds 1.0 position to support the IMPACT (Investing in Management, Police, Accountability, Community, and Technology) Program in order to more effectively analyze crime data and better link crime analysis, community policing, and crime prevention programs.
- Fire Cardiac Monitors/Defibrillators Adds funding of \$195,000 to purchase seven cardiac monitor/defibrillator units. Grant funds were used to replace cardiac monitor/defibrillators for the front-line apparatus; however, with the reconfiguration of apparatus and the inclusion of squad cars, an additional seven cardiac monitor/defibrillator units are needed.

- Fire Functional Movement Screening and Testing Adds one-time funding of \$100,000 for
 Fire Department personnel to become peer trainers to help reduce the frequency of injuries caused by strains and sprains and reduce resulting workers' compensation claims costs.
- La Raza Roundtable/Harvard Study Consensus Building Project Continues matching funding of \$50,000 with Santa Clara County for facilitation of the Harvard Study Consensus Process to create transformative multisystem change aimed at eliminating Latino overrepresentation in the criminal justice, juvenile justice and child welfare systems.
- Senior Nutrition Program Meal Enhancements Adds ongoing funding of \$100,000 to support meal enhancements at the 14 senior nutrition program sites.
- Anti-Graffiti Program Adds ongoing funding of \$75,000 to implement a two-year strategy to enhance the Anti-Graffiti Program. In the first year, funding will be allocated to increase the graffiti abatement zones covered within the 24-hour response area in the City and to market volunteer opportunities. In the second year, with the anticipated increase in volunteers and enhanced level of graffiti abatement, it is expected that the expanded graffiti abatement zones will require only routine maintenance for graffiti removal. This will enable a year two shift of the additional program support funds to partner service providers, such as Conservation Corp or Green Cadre, and to part-time staff support to manage the extra volunteers recruited.
- Microsoft Office Upgrade Adds funding to upgrade the City's Microsoft Office 2003 Suite
 to an Office 365 subscription model. The City's current Office 2003 version is three full
 generations behind the proposed version.
- Center for Employment Training Adds one-time funding of \$250,000 for the Center for Employment Training (CET) as directed and approved by the City Council as part of the 2013-2014 Mayor's March Budget Message. In 2008, CET received a Federal grant of \$3 million to renovate its buildings that required a 40% local match. With the dissolution of the Redevelopment Agency, local funding (\$950,000) is no longer available. This action will help CET achieve the required \$2 million local match.
- Active Transportation Program and Pedestrian Safety Adds resources to develop and implement pedestrian crossing improvements on major roads and manage the City's Active Transportation Program, which promotes safe walking and bicycle commuting. (Capital Funds)
- LED Streetlight Conversion Staffing Adds 1.0 position, supported by capital funds, to manage the LED Streetlight conversion program as well as to pursue future grant opportunities and other potential financing strategies to accelerate the conversion of the City's streetlight inventory. (Capital Funds)
- Transportation Staffing Adds resources to support pavement maintenance management and
 engineering, local transportation projects and policy oversight, transportation development
 program staffing, regional transportation projects staffing, and parking program/special events
 management staffing. (Capital/Special Funds)

- Radar Speed Display Signs Adds one-time funding of \$100,000 to install five new radar feedback speed limit signs to help reduce traffic speeds and improve safety, tentatively planned at the following locations: Blossom Hill Road (2 signs) west of Camden Avenue and east of Leigh Avenue; Taylor Street (2 signs) west of Route 87 and east of Coleman Avenue; and Hellyer Avenue (1 sign) west of Route 101 and east of Senter Road.
- Environmental Services Technical and Administrative Staffing Adds staffing to support solid waste contract compliance, Administrative Services Division oversight, Municipal Water and Water Pollution Control Plant engineering staffing, and Recycle Plus transition project staffing. (Special Funds)
- Airport Councils North America Conference Adds \$75,000 for the 2013 Airport Councils International World/North American (ACI-NA) Annual Conference and Exhibition which will be held at the San José Convention Center from September 23 through September 25, 2013. In addition, to support the event, which is expecting over 5,100 hotel rooms to be booked, Team San José, San José Convention and Visitors Bureau, and Hotel Business Improvement District in partnership with Airport are contributing resources to fund the conference. (Special Funds)
- Other Investments Adds resources to: address the increased demand for employment and classification services as well as provide support for workforce planning and human resources analytics; perform an internal financial controls evaluation; ensure Minimum Wage Ordinance compliance; and perform ballot measure polling for potential revenue measures.
- Development Fee Programs and Other Fee/Grant Programs: Several recommended budget actions are included for the four Development Fee Programs and other fee and grant programs with a net-zero impact on the General Fund.
 - Development Fee Programs New resources are included in the Development Fee Programs (Building, Planning, Public Works, Fire) to ensure increasing demands can be met within expected service delivery timeframes. This includes the addition of approximately 30 positions, overtime funding for after-hours inspections, and administrative support. No general fee increases are necessary in order to meet the increased development services activities. However, a new Technology Fee (2% fee on permits) is proposed to support technology initiatives for these programs. It is anticipated that approximately \$700,000 would be generated in 2013-2014 for these initiatives.
 - Other Fee/Grant Programs In addition, several other fee-supported additions as well and revenue generating proposals are included, including positions to support the Sidewalk Repair Program, additional Animal Care and Services staffing to support the contract with the City of Milpitas, additional revenue-generating proposals in the Parks, Recreation and Neighborhood Services Department, and additional City Hall facility rental staffing. In addition, adjustments to the Fire Non-Development Fee Program are recommended to achieve 100% cost recovery.
- Essential Services Reserve: Establishes a one-time Essential Services Reserve of \$2.0 million to fund services that are of importance to the community. These funds will be allocated by the City Council later in the 2013-2014 Budget process.

Continue Service Delivery Efficiencies and Cost Reduction/Revenue Strategies

As was the case in 2012-2013, this Proposed Budget generally maintains current levels of services and staffing. However, we continue to identify opportunities to implement new models for delivering services that may cause position impacts in specific programs. The Administration will continue to work toward minimizing potential layoffs triggered by these changes by taking advantage of vacancies and appropriate redeployment of employees. A number of cost reduction and revenue strategies are also incorporated into the Proposed Budget.

- Service Delivery Efficiencies: The following list contains examples of changes in service delivery models that are designed to improve efficiency, reduce costs, and enhance service levels.
 - Workers' Compensation Service Delivery Pilot Program Implements the Workers' Compensation Service Delivery model pilot approved by the City Council on October 30, 2012. During this two-year pilot, approximately 40-50% of the Workers' Compensation claims administration services will be provided by a third party administrator (TPA). With \$19.5 million in workers' compensation claims costs assumed in 2013-2014, the goal of this pilot will be to determine if the overall cost of the program can be reduced.
 - work2future Service Delivery Model Change Eliminates 25.0 positions and adds 1.0 Accountant I/II position in the work2future Division (current total of 41.3 positions) that is supported by the Workforce Investment Act Fund as part of a recommended phased transition of direct client services from the City to a third party administrator (TPA). The work2future Division provides workforce development services through case management, workshops, training, job fairs, and special recruitments to 5,000 10,000 unemployed workers in Santa Clara County annually. By transitioning the direct client services function to a TPA, it is anticipated that the TPA will be able to provide this service in a more cost-effective manner and mitigate the effects of reduced federal funding. Under this new service delivery model, the TPA will have greater flexibility in aligning resources to address specialized program needs, changing funding levels, and variable workload demands. The remaining 17.3 work2future City staff will be responsible for fiscal and program management, monitoring and reporting and interface with the State's Job Training Automation system, labor market information management, small business services, and staff support for the work2future Board. (Special Funds)
 - Regional Wastewater Facility Trainee Staffing Adds 7.0 Plant Attendant positions and eliminates 4.0 vacant journey-level Plant Mechanic positions in order to 1) create additional points of entry into the Regional Wastewater Facility Mechanic classification series and 2) help obtain a qualified candidate pool for existing Plant Operator Trainee (O.I.T), Apprentice Plant Mechanic (M.I.T.), Electrician, Instrument Control Technician and Heavy Equipment Operator positions. The Plant Attendants will assist Plant Mechanics by performing the lower level tasks and will learn various job functions as they rotate through the various Plant work groups. (Special Funds)

- Police Overtime Allocates \$4.0 million from the Police Department Overtime Earmarked Reserve, established in the 2012-2013 Mid-Year Review. Although the Department is conducting recruit academies to hire for sworn vacancies, the Department is anticipated to begin 2013-2014 with at least 80 sworn vacancies. As an interim strategy to meet service delivery needs until the Department is staffed at authorized levels, the overtime funding will be used in 2013-2014 to continue backfilling for vacant patrol positions while they are being hired and trained, maintain targeted enforcement of high crime activity through suppression cars, conduct high profile investigations, and backfill for civilian vacancies as needed.
- Police Contractual Backgrounding Services Adds one-time funding of \$385,000 for contractual backgrounding services, bringing total funding to \$1.0 million, to address the increased activity level anticipated in 2013-2014 due to the high number of vacancies. Prior to contracting out background services in 2012-2013, 12 sworn positions were temporarily reassigned from other areas within the Police Department to conduct backgrounds and were not able to perform front-line police work.
- Cost Reductions/Revenue Strategies: The Proposed Budget incorporates a limited number of cost reductions as well as includes additional funding sources.
 - Successor Agency to the Redevelopment Agency As a result of a tentative ruling in the Superior Court in Sacramento County, it is anticipated that the County of Santa Clara will be ordered to remit funds withheld for PERS and Water District levies beginning in 2012-2013 (\$7.65 million) and ongoing (approximately \$7.5 million annually) to the Successor Agency. This additional funding is expected to be received in 2013-2014 and will reduce the anticipated General Fund subsidy to the Successor Agency by \$13.5 million, from \$15.0 million to \$1.5 million, in 2013-2014. This additional tax increment available to the Successor Agency will not be sufficient to cover administrative costs given their place in the current priority of obligations. The ongoing savings as a result of this decision is \$2.7 million in 2014-2015.
 - Successor Agency to the Redevelopment Agency Transition Continues the transition of
 the Successor Agency, phasing out, where appropriate, related Successor Agency administration,
 including staffing, and adding 2.5 positions to the Finance Department for net savings of
 \$426,000.
 - Children's Health Initiative Transitions responsibility for the Children's Health Initiative to the County of Santa Clara. The City's current annual allocation of \$2.1 million provides health insurance access to children of Santa Clara County with family income that falls below the federal poverty level. With the recent passage of the County's Measure A sales tax increase, it is anticipated that the County will be able to assume these costs with no reductions to the program.
 - Housing Rehabilitation Loan and Grant Program Eliminates 5.0 positions supported by Housing Funds in the Rehabilitation Loan and Grant Program as a result of reduced tax increment funding due to the dissolution of the San Jose Redevelopment Agency, decreased entitlement funding in the Community Development Block Grant (CDBG) Program due to the federal sequestration, and the strict requirements of the use of CalHome funds. Because of the requirements of the use of CalHome funds, there have not been a large amount of applicants that qualify for the loans and the Department has been only able to provide for three loans within the past year. (Special Funds)

- Homeownership Down Payment Program As a result of reduced federal and State grant funding, eliminates 2.0 positions in the Homeownership Downpayment Program that provides downpayment assistance to low-income first time homebuyers. The demand for this program has significantly decreased as the housing market recovers. (Special Funds)
- Available Fund Balance Additional Fund Balance of \$51.0 million in the General Fund would primarily be generated from various reserves as well as excess revenues and expenditure savings in 2012-2013. The liquidation of various reserves is projected to generate \$36.6 million for use in 2013-2014, the largest of which include: Future Deficit Reserve of \$29.4 million (established in the 2012-2013 Adopted Budget at \$22.5 million and increased by \$6.9 million as part of the 2012-2013 Mid-Year Budget Review actions); Police Department Overtime Reserve of \$4.0 million (this reserve was established in 2012-2013 to address overtime needs in 2013-2014 due primarily to the large number of vacancies); and Development Fee Reserves of \$2.6 million (\$2.2 million ongoing). Projected cash flow of SARA between 2012-2013 and 2013-2014 will change the allocation of funds (\$6.4 million) between these two fiscal years and an additional \$3.5 million from higher than anticipated Tobacco Settlement funds that included a one-time settlement payment in 2012-2013 are also included. Additional excess revenues and expenditures savings from 2012-2013, including the close-out of two funds, are expected to generate an additional \$5.2 million from levels assumed in the 2014-2018 Forecast.
- Medical Marijuana Tax Increase Recognizes additional revenue of \$1.5 million generated from an increase in the Marijuana Business Tax rate from 7% to 10% of gross receipts (increasing the revenue estimate from \$3.9 million to \$5.4 million). A public meeting regarding this increase is scheduled for May 21, 2013, and the public hearing is scheduled for June 4, 2013, where City Council will consider an ordinance to increase the tax rate.
- Vendor Automation/Revenue Sharing Changes the vendor payment process to allow vendors to pay a small fee to receive electronic payments in lieu of manual checks, and recognizes revenue of \$250,000 (\$500,000 ongoing) from a revenue-sharing agreement with the City's banking services provider. With this streamlined process, the Finance Department will be able to return to issuing vendor checks weekly rather than bi-weekly.
- Transfer from the Park Trust Fund Recognizes a transfer from the Park Trust Fund of \$594,000 to reimburse the General Fund for prior year expenditures related to Watson Park that were eligible to be paid from Park Trust Fund.
- Transfers from the Integrated Waste Management Fund and the Water Utility Fund Increases the transfer from the Integrated Waste Management Fund by \$350,000 (from \$250,000 to \$600,000) in 2013-2014 and \$50,000 ongoing to reflect unclaimed Construction Demolition Diversion Deposit (CDDD) Program revenues that can be transferred to the General Fund. Also, increases the transfer from the Water Utility Fund by \$50,000 (from \$225,000 to \$275,000) on an ongoing basis to reflect actual late fees that can be transferred to the General Fund.

- Transfer to the Community Facilities Revenue Fund Reduces the General Fund subsidy to the Community Facility Revenue Fund (Hayes Mansion) by \$300,000 to reflect lower anticipated debt service payments. The anticipated refunding of outstanding fixed rate and variable rate bonds issued to finance the construction of City Hall and associated parking garage is projected to generate savings between \$3.5 million to \$7.2 million in the General Fund. These savings will be recommended to be used reduce the City's outstanding variable rate debt, specifically the 2008D Lease Revenue Bonds issued for the Hayes Mansion improvements. The savings will be recommended to be used to pay down a portion of the \$53.7 million in outstanding principal, which will reduce annual debt service payments by approximately \$300,000 to \$600,000, reducing the annual ongoing General Fund subsidy to the Community Facilities Revenue Fund. The Proposed Budget currently reflects a \$300,000 reduction to the General Fund subsidy to the Community Facilities Revenue Fund as the minimum amount of savings that are expected to be realized. Additional budget adjustments will be brought forward to recognize the savings in the Civic Center Fund and pay down of a portion of the Lease Revenue Bonds for the Hayes Mansion improvements once the City Hall refunding is complete.
- SAFER Grant Revenue/Airport Reimbursement for Fire Services Recognizes SAFER 2010 grant revenues of \$2.3 million anticipated to be received in 2013-2014 as a result of the approved extension of the period to expend the grant funds. This additional revenue is recommended to be used to reduce the transfer from the Airport Maintenance and Operation Fund to reimburse the General Fund for aircraft rescue and firefighting services provided by the Fire Department in 2013-2014 and 2014-2015. With the acceptance of the SAFER 2011 grant, the potential outsourcing of aircraft rescue and firefighting services will have to be postponed to October 2014 to remain in compliance with the SAFER grant requirements. By lowering the transfer to the General Fund from the Airport Maintenance Operation Fund by \$1.8 million in 2013-2014, the cost to Airport for fire services will be in-line with an outsourcing proposal received by the Airport. The remaining \$0.5 million in SAFER grant revenues will be used to establish an Aircraft Fire Services Reserve to offset the higher aircraft rescue and firefighting services costs for a portion of 2014-2015. This action will maintain sworn firefighter staffing levels and avoid layoffs.

Limited Fee Impacts

There are a limited number of fee increases in the 2013-2014 Proposed Budget. No rate increases will be recommended for the Sewer Service and Use Charge, Storm Sewer Service Fee, and Recycle Plus rates in 2013-2014. The Municipal Water System rates are recommended to increase by approximately 8% (but no more than 9%), due primarily to the higher cost of wholesale water purchases.

In the four Development Fee Programs (Building, Fire, Planning, and Public Works), no general fee increases are needed to maintain cost recovery. The existing revenue streams in those programs along with the use of portions of the Development Fee Program Reserves are sufficient to support additional staffing to meet service demands and improve customer service in these areas without fee increases. However, a new Technology Fee, which will apply a 2% fee on development permits, is recommended and will be used to fund technology initiatives for the Development Fee Program. There are adjustments to various departmental fees and some new fees proposed to maintain or improve cost-recovery levels.

LOOKING FORWARD

While it is good news that our overall financial position continues to stabilize and allows us to continue to make modest investments to address our most critical needs, services also continue to remain well below desired levels. One of the principal goals of the Fiscal Reform Plan issued in May 2011 was to restore key services to January 2011 levels, including police, fire, community centers, libraries, and street maintenance. It remains important to note that even when we achieve this goal for service restoration, we will not be at the full levels of service that we were able to provide to our community in the past.

The Fiscal Reform Plan identified specific cost reduction and revenue strategies to provide the capacity to meet this goal. While some of the components of this plan have been implemented and have started to generate savings to help us restore stability, other elements remain outstanding. One major component of the Fiscal Reform Plan that has not yet been implemented is the increase in employee retirement contributions required under Measure B that was approved by the voters in June 2012. This is currently a matter under litigation, and therefore its effect on long-term cost control has not been realized. Another major component of Fiscal Reform Plan is a revenue strategy, specifically a potential increase in the local Sales Tax of up to ½%. The City Council decided not to pursue this step for the current year, but it could revisit bringing such a measure to San Jose voters for their approval in the coming year. These two elements together would generate additional resources of approximately \$85 million to \$122 million annually, depending on the Sales Tax rate increase, and could enable significant improvements in the City's capacity to restore and enhance delivery of critical services.

CONCLUSION

It is a great relief to present a balanced budget without the need to resort to the painful decisions we have had to make in recent years. We still have a long way to go, however, to achieve the budget stability that will allow us to restore service levels and meet major community and organizational needs. We are now seeing the benefits of those difficult decisions, which combined with economic recovery, have allowed us to address some of our most urgent needs. Our current level of stability, however, is not where we want to stay, and we also must be mindful that economic or financial conditions could quickly become adverse again as a result of factors beyond our control. Our financial progress could be reversed by a number of events, such as swings in the rate of economic recovery, policies made by the Governor and Legislature of California, negative Court decisions, or potential increases in the required contributions to the City's retirement funds.

For these reasons we must continue the remarkable discipline and leadership exhibited by elected officials, City management, and our outstanding employees in order to keep steadfast with our commitment to our community. The goals of the Fiscal Reform Plan remain valid, and we must continue to seek ways to reduce costs through innovations, partnerships, efficiencies, and community support. Economic development must continue to be a priority for our community so that we can strengthen our economic foundation that generates the revenues we need to provide vital public services. I am confident that we are on a good path back to sustainable financial stability.

2013-2014 PROPOSED OPERATING BUDGET MESSAGE

CONCLUSION

Finally, I must again thank our remarkably dedicated and talented City staff – great people from the front lines of each department to the City Manager's Budget Office – who have worked so hard and spent long hours to prepare this Proposed Budget. They represent the best in public service, and I continue to be inspired by their commitment to ensure that San José remains a wonderful city for our residents, businesses, and employees.

Debra Figone City Manager

\$20 Million General Fund Contingency Plan

The 2014-2018 General Fund Forecast included approximately \$20 million in ongoing savings from the Supplemental Retiree Benefit Reserve (SRBR) elimination and the lowest cost healthcare plan changes. These changes have been challenged and the SRBR is part of a trial related to Measure B in the Superior Court in July 2013. In the Mayor's March Budget Message approved by the City Council, the Administration was directed to develop a list of \$20 million in proposed ongoing and/or one-time expenditures that will not be implemented until at least 60 days after a favorable verdict is received. Below is the list of budget proposals that meet this City Council direction with \$20 million in 2013-2014 budget reductions, of which \$15.7 million is ongoing. Additional detail regarding these proposals is included in the City Departments and City-Wide Sections of this document. If the City does not prevail, the one-time proposals will need to be replaced with ongoing solutions in order to not carry over an additional shortfall to 2014-2015.

\$20 Million General Fund Contingency Plan

Proposal	2013-2014	Ongoing
Budget Stabilization Reserve	(4,000,000)	
Employee Compensation Planning Reserve ¹	(11,100,000)	(11,100,000)
Employment Services Staffing ²	(77,000)	(94,000)
Microsoft Office Upgrade	(812,000)	(262,000)
Police Field Patrol Community Service Officers ³	(1,107,000)	(1,836,000)
Police Crime Analysis Staffing ²	(64,000)	(78,000)
Police Crime Prevention Staffing ²	(224,000)	(244,000)
Preventative Maintenance Program	(370,000)	
Senior Nutrition Program Meal Enhancements	(100,000)	(100,000)
South San José Police Substation Opening ⁴	(2,146,000)	(2,006,000)
Total	(20,000,000)	(15,720,000)

- If all or part of the savings associated with the SRBR and lowest cost healthcare plan changes contained in the 2013-2014 budget are not realized, the City will no longer have identified ongoing funding to pay for compensation increases. In the event all or part of these savings are not realized, the City's proposal on the table with most of its bargaining units would be to roll back any negotiated compensation increases prospectively, effective the pay period upon notice that the savings will not be realized. However, since the pay adjustment would not be retroactive, the costs associated with salary increases provided up until the notice date would have to be backfilled with the 2014-2015 Future Deficit Reserve.
- Start date of September 2013
- Start date of January 2014
- Opening planned for January 2014; staff start date of November 2013, includes closure costs

In addition to this plan, the Administration has developed a contingency plan to address the uncertainty related to the final outcome of the litigation with the County of Santa Clara related to the withholding of Successor Agency to the Redevelopment Agency tax increment associated with the PERS and Water District levies (see Exhibit 2). Depending on the final outcome of litigation, proposals may be shifted between the contingency plans, particularly if only the contingency plan related to the SRBR and lowest cost healthcare plan changes litigation is needed.

Successor Agency to the Redevelopment Agency PERS Levy/Water District Levy General Fund Contingency Plan

In the 2013-2014 Proposed Budget, it is assumed that the County of Santa Clara will not be allowed to withhold Successor Agency to the Redevelopment Agency (SARA) property tax increment to fund the County employees' retirement plan (the PERS Levy) and Water District levy. As a result of a tentative ruling in the Superior Court, Sacramento County, this budget presumes that Santa Clara County will be ordered to remit funds withheld for the PERS and Water District Ievies to SARA beginning in 2012-2013 (\$7.65 million) and ongoing (approximately \$7.5 million annually). With additional tax increment available to fund SARA legal obligations, the required \$15.0 million estimated 2013-2014 SARA General Fund subsidy is reduced by \$13.5 million in 2013-2014 and \$2.7 million ongoing. However, if it is determined that the County can withhold this tax increment, the SARA General Fund subsidy will remain at the \$15.0 million level.

Following is a contingency plan that lists the General Fund budget proposals of \$13.5 million in 2013-2014 and \$2.7 million ongoing that would not be funded if the Successor Agency does not prevail. In a number of cases, the proposals would be funded in 2013-2014 but would not receive ongoing funding, such as the City Attorney's Office Legal Support Staffing and the Medical Marijuana Program. Additional detail regarding these proposals is included in the City Departments and City-Wide Sections of this document. The 2013-2014 expenditures of \$13.5 million for the items listed below would be placed on hold pending the outcome of the litigation.

Successor Agency to the Redevelopment Agency PERS Levy/Water District Levy General Fund Contingency Plan

Proposal	2013-2014	Ongoing
2014-2015 Community Action and Pride Grants Reserve	(100,000)	•
2014-2015 Homeless Response Team Reserve	(1,500,000)	
Anti-Graffiti Program	(75,000)	(75,000)
City Attorney's Office Legal Support Staffing		(350,000)
Office of the City Clerk Staffing		(250,000)
City Hall Bamboo Courtyard Renovation	(250,000)	
Computer Server Replacements/Network Upgrades	(250,000)	
Economic Development/Incentive Fund	(750,000)	
Evergreen Community Aquatics Program		(25,000)
Medical Marijuana Program		(1,257,000)
Neighborhood Business Districts		(45,000)
Office of Employee Relations Fiscal Reform Staffing		(208,000)
Operating/Capital Budget System Replacement Reserve	(2,850,000)	
Police Administration Building Unmet/Deferred Infrastructure and Maintenance (chiller, HVAC, waterproofing, firing range lighting)	(1,350,000)	
Police Communication Building Unmet/Deferred Infrastructure and Maintenance (electrical, chiller, waterproofing)	(3,600,000)	
Preventative Maintenance Program	(300,000)	
Radar Speed Display Signs	(100,000)	
Real Estate Services Document Imaging and Records Retention System	(200,000)	
San Jose BEST and Safe Summer Initiative Programs	500,000	(500,000)
Successor Agency Legal Obligations	(2,500,000)	
Street Tree Maintenance	(160,000)	
Total	(13,485,000)	(2,710,000)

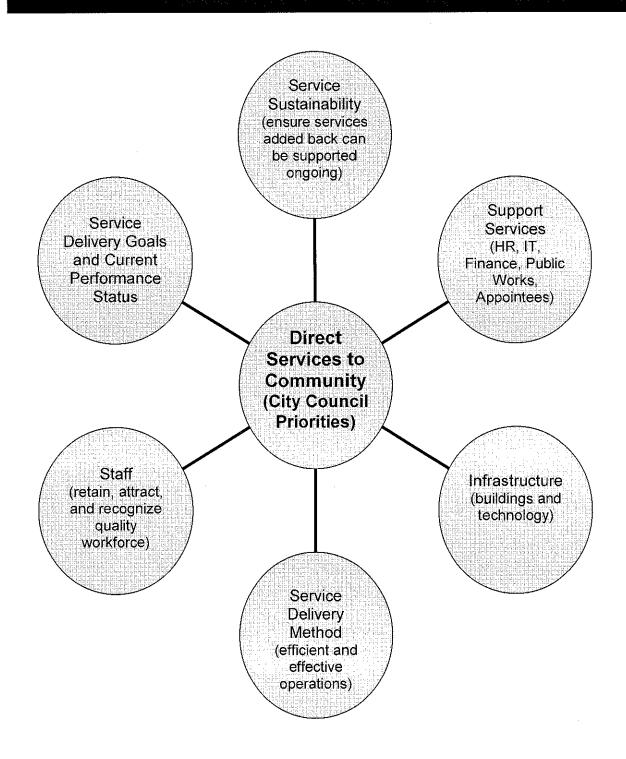
Successor Agency to the Redevelopment Agency PERS Levy/Water District Levy General Fund Contingency Plan

In addition to this plan, the Administration has developed a contingency plan to address the uncertainty related to the final outcome of the litigation regarding the Supplemental Retiree Benefit Reserve (SRBR) elimination and the lowest cost healthcare plan changes (see Exhibit 1). Depending on the final outcome of litigation, proposals may be shifted between the contingency plans, particularly if only the contingency plan related to the SRBR and lowest cost healthcare plan changes litigation is needed.

2013-2014 Budget Balancing Strategy Guidelines

- 1. Develop a budget that balances the City's delivery of the most essential services to the community with the resources available.
- 2. Balance ongoing expenditure needs with ongoing revenues to ensure no negative impact on future budgets and to maintain the City's high standards of fiscal integrity and financial management.
- 3. Focus on business process redesign in light of the severe staff reductions experienced during the last several years in order to improve employee productivity and the quality, flexibility, and cost-effectiveness of service delivery (e.g., streamlining, simplifying, reorganizing functions, and reallocating resources).
- 4. Explore alternative service delivery models (e.g., partnerships with the non-profit, public, or private sector for out- or in-sourcing services) to ensure no service overlap, reduce and/or share costs, and use our resources more efficiently and effectively. The City Council Policy on Service Delivery Evaluation provides a decision-making framework for evaluating a variety of alternative service delivery models.
- 5. Analyze non-personal/equipment/other costs, including contractual services, for cost savings opportunities. Contracts should be evaluated for their necessity to support City operations and to identify negotiation options to lower costs.
- 6. Explore redirecting and/or expanding existing revenue sources and/or adding new revenue sources.
- 7. Establish a fee structure to assure that operating costs are fully covered by fee revenue and explore opportunities to establish new fees for services, where appropriate.
- 8. Identify City policy changes that would enable/facilitate service delivery changes or other budget balancing strategies.
- As additional resources become available, focus service restorations to meet the baseline January 1, 2011 service levels previously identified by the City Council in the areas of fire, police, library, community centers, street maintenance, and facility openings.
- 10. In addition to considering the service restorations to meet the baseline January 1, 2011 service levels, take a holistic approach regarding the restoration of services. As outlined in the Guiding Principles for Restoring City Service Levels, allocate additional resources with the following goals in mind: ensure the fiscal soundness of the City; choose investments that achieve significant outcomes; and improve efficiency and effectiveness of service delivery. Using a multi-pronged approach to restoring direct services, take into consideration the following factors: adequate strategic support resources; adequate infrastructure; service delivery method to ensure efficient and effective operations; service delivery goals and current performance status; service sustainability; and staffing resources.
- 11. Incorporate compensation adjustments in a fiscally responsible manner that does not result in a reduction or elimination of services in the General Fund. Compensation increases included in the budget will be quantified and identified in separate categories: automatic step increases required by existing contracts, management pay for performance, and Employee Compensation Planning Reserve.
- 12. Engage employees in department budget proposal idea development.
- 13. Use the General Plan as a primary long-term fiscal planning tool and link ability to provide City services to development policy decisions.
- 14. Continue a community-based budget process where the City's residents and businesses are educated and engaged, as well as have the opportunity to provide feedback regarding the City's annual budget.

Service Restoration Decision Making Framework



Guiding Principles for Restoring City Service Levels

Ensure the Fiscal Soundness of the City

- 1. Develop the General Fund budget to support the City's mission and use the City Council-approved Budget Principles to ensure the long term fiscal health of the City (City of San José Budget Principles)
- 2. Ensure services that are restored can be sustained over the long-run to avoid future service disruption (Use Five-Year General Fund Forecast as one tool)
- 3. If possible, defer adding new permanent positions until new retirement system is in place

Choose Investments that Achieve Significant Outcomes

- 4. Ensure restored services represent City Council priorities and the highest current need in the community
- 5. Balance investments among three categories:
 - Restoration of services (public safety and non-public safety services, including critical strategic support services)
 - · Opening of new facilities
 - Maintenance of City infrastructure and assets
- 6. Prioritize baseline service level restorations using performance goals (Exhibit 1 Service Restorations Previously Identified by City Council January 1, 2011 Levels)
- 7. Focus funding on areas where there is a high probability of success and/or high cost of failure
 - Focus funding on infrastructure needs where there is a significant increase in cost if maintenance is delayed (such as street maintenance)
 - Focus investments in technology that have the greater return on investment in terms of services to the public and employee productivity

Improve the Efficiency and Effectiveness of Service Delivery

- 8. Before restoring prior service methods, evaluate options to determine if alternative service delivery models would be more cost effective.
- 9. Ensure strategic support and technology resources are capable of supporting direct service delivery and effective management of the organization.
- 10. Prioritize organizational investments that maximize workforce productivity, efficiency, and effectiveness.
- 11. Pursue opportunities and methods, including performance, to retain, attract, and recognize employees within resource constraints.

Service Restorations Previously Identified by City Council (January 1, 2011 Levels)		
Fire	 33 Fire Stations open; On average, Citywide, 82.6% of time, the initial responding fire unit arrives within 8 minutes after an emergency 9-1-1 call is received*; and On average, Citywide, 85.2% of time, the second response fire unit arrives within 10 minutes after an emergency 9-1-1 call is received*. * Response time data under review 	
Police	 On average, Citywide, average response time for Priority One police calls for service (present or imminent danger to life or major damage/loss of property) is 6.04 minutes; On average, Citywide, average response time for Priority Two police calls for service (injury or property damage or potential for either to occur) is 12.74 minutes; and On average, overall, the clearance rate (number cleared / total cases) for Part 1 crimes is as follows: Homicide (65.00%), Rape (19.37%), Robbery (26.54%), Aggravated Assault (39.93%), Burglary (5.58%), Larceny (18.90%), and Vehicle Theft (8.85%). 	
Library	 On average, 18 library branches open 39 hours per week; and On average, King Library (subject to future contractual arrangements with San José State University): Hours open: 72 hours per week per academic semester; 58 hours per week otherwise; Children's Room: 50 hours per week; Third Floor General Collection and Reference Desks: 64 hours per week; California Room: 20 hours per week; Access Services: 72 hours per week; Periodicals: 72 hours per week; and Second Floor Reference Desk: 72 hours per week. 	
Community Centers	 On average, 10 Hub Community Centers open 63 hours per week; On average, 9 Satellite Community Centers open 40 hours per week; and On average, 8 Neighborhood Centers open for 15 hours of programming per week. 	
Street Maintenance	72 miles of residential and arterial streets resealed and 6 miles of residential and arterial streets resurfaced with various Capital and Grant funds (no General Fund allocation). Maintaining this street maintenance level will be contingent upon receiving commensurate levels of regional, State, and federal funds annually.	
Facilities Built or Under Construction/ Opening Deferred	South San José Police Substation.	