

City of San José

**General Fund
Structural Budget Deficit History
&
Service Restoration Priorities
and Strategies**

January 2015

General Fund Structural Budget Deficit History and Service Restoration Priorities and Strategies

AGENDA

- General Fund Structural Budget Deficit History
- Service Restoration Priorities
- Service Restoration Funding Strategies
- Discussion
- Public Comment



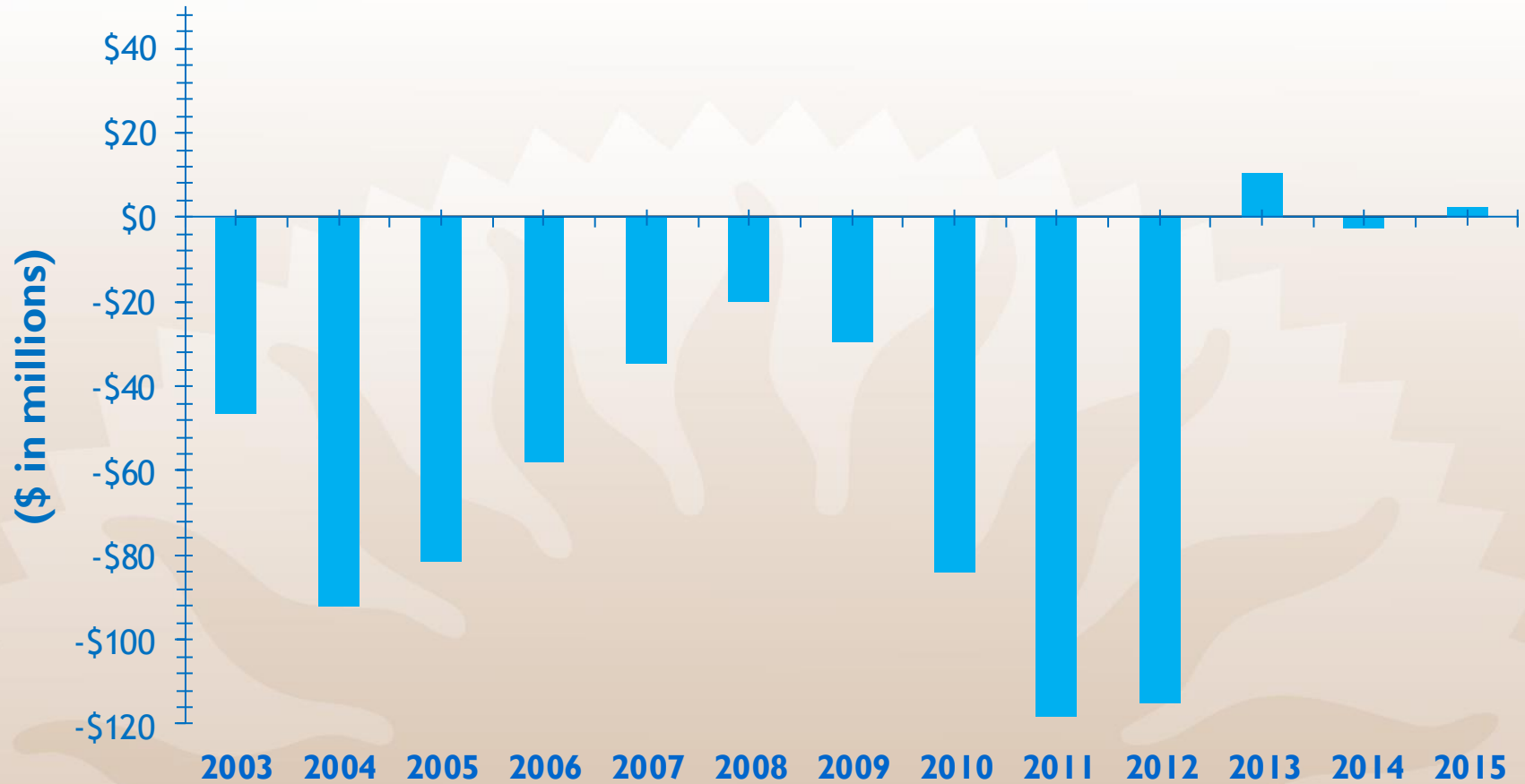
General Fund

Structural Budget Deficit History

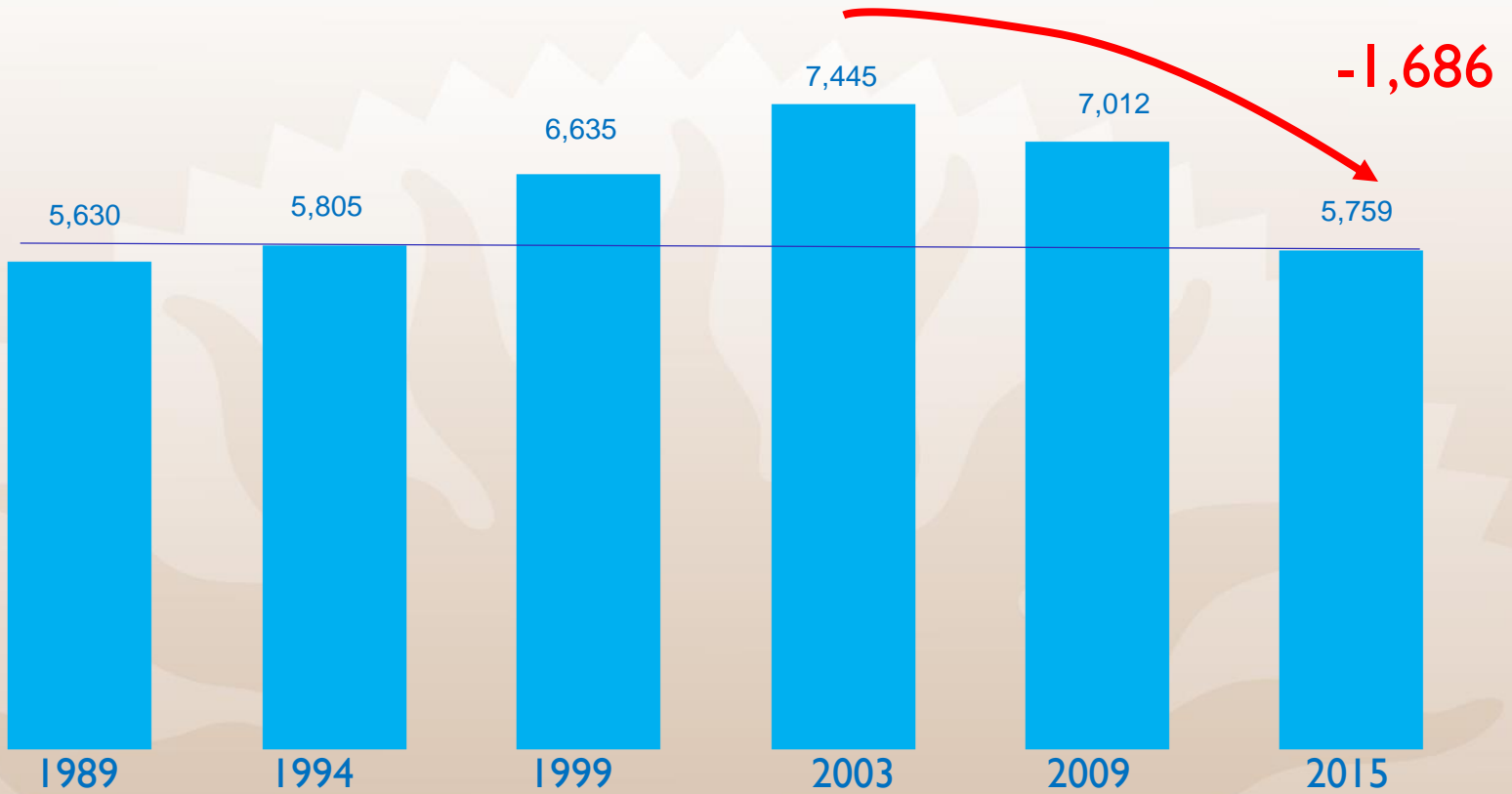
Overview

- A decade of General Fund budget shortfalls (2002-2003 through 2011-2012) driven by two deep recessions and unsustainable cost structure
- Civic engagement and combination of three major strategies used to address shortfalls
- Significant service reductions in both public safety and non-public safety areas were unavoidable

\$670M in Cumulative Shortfalls Balanced



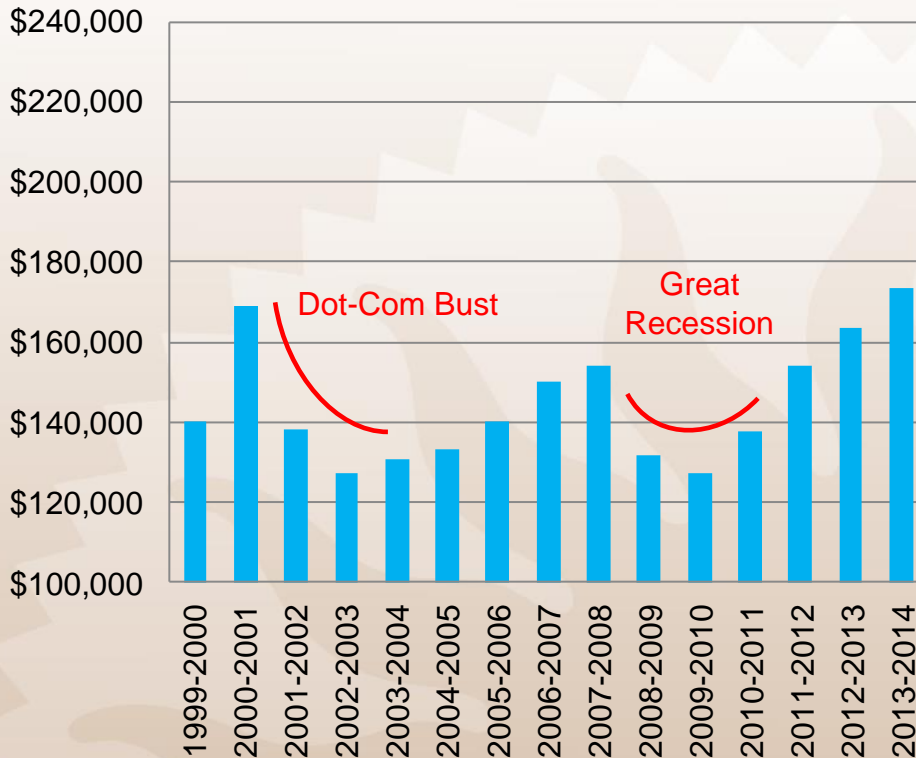
Reduced Positions by 23%



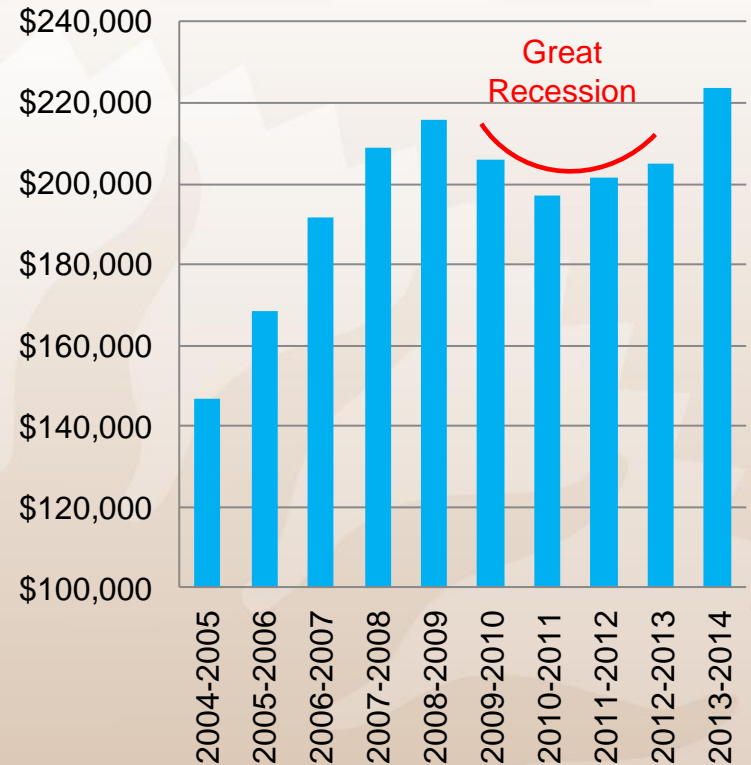
Economically Sensitive Revenues Down

\$ in thousands
(All figures not adjusted for inflation)

Sales Tax

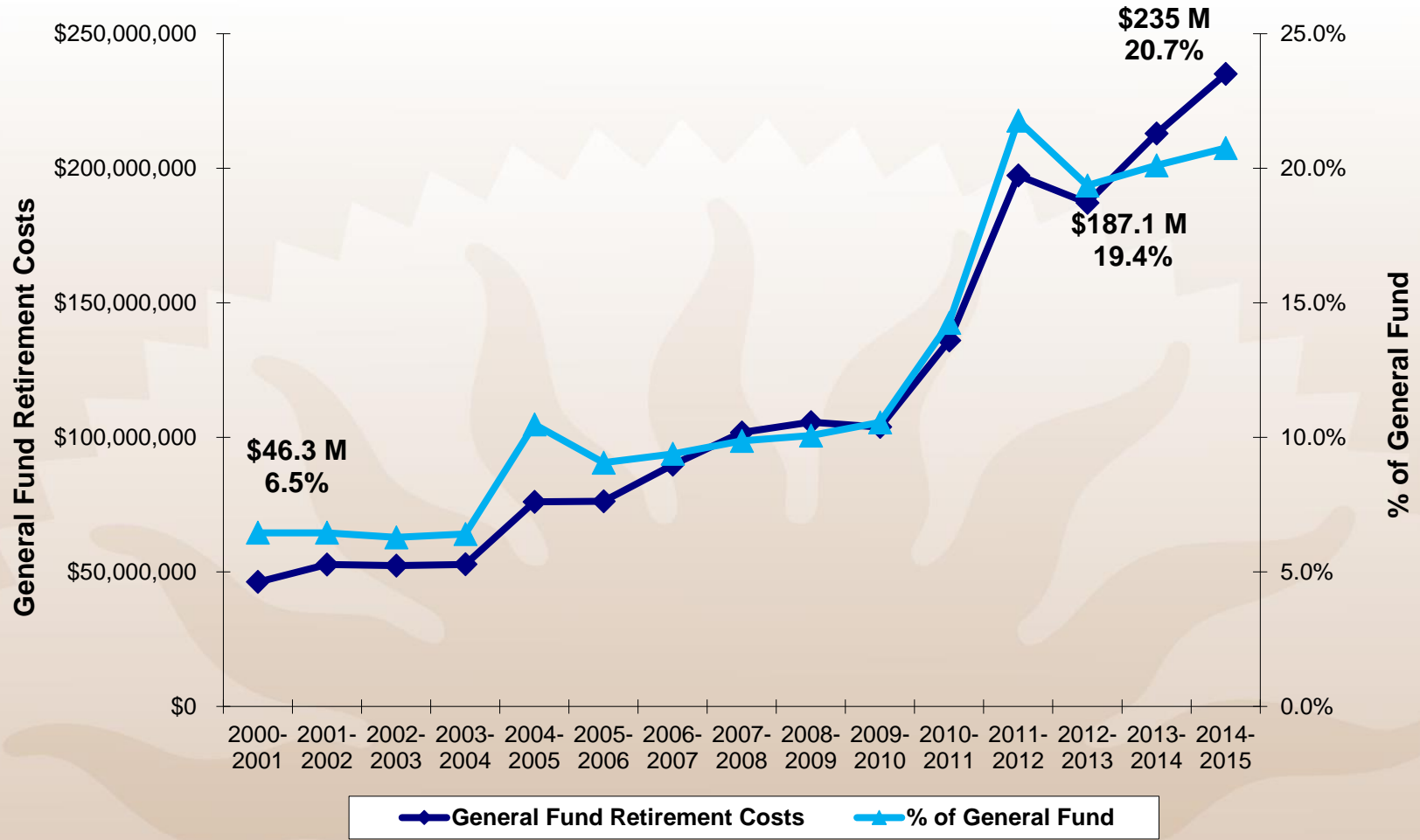


Property Tax

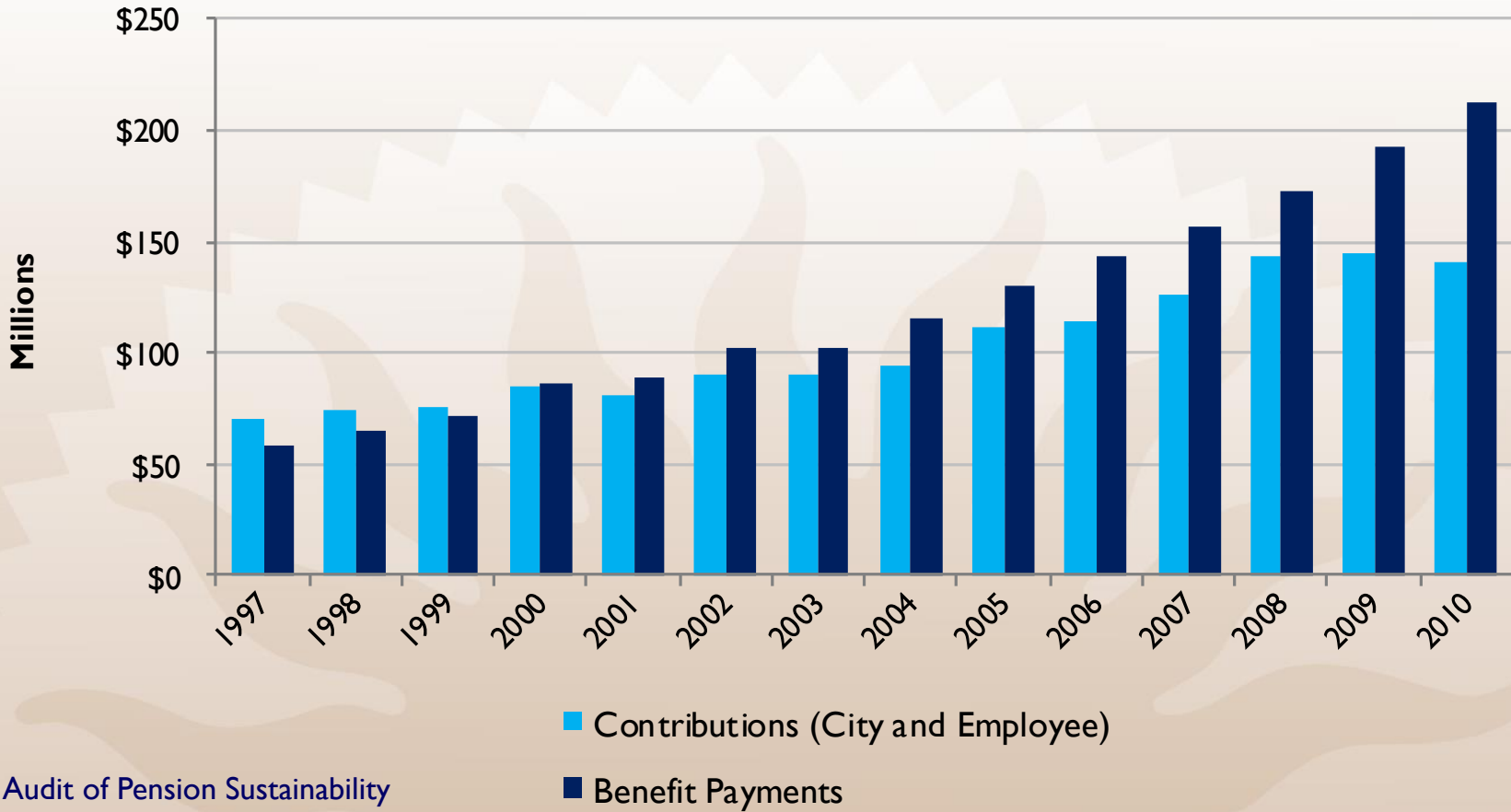


Graph begins in 2004-2005 due to a change in the calculation formula of property tax

Escalating Retirement Costs

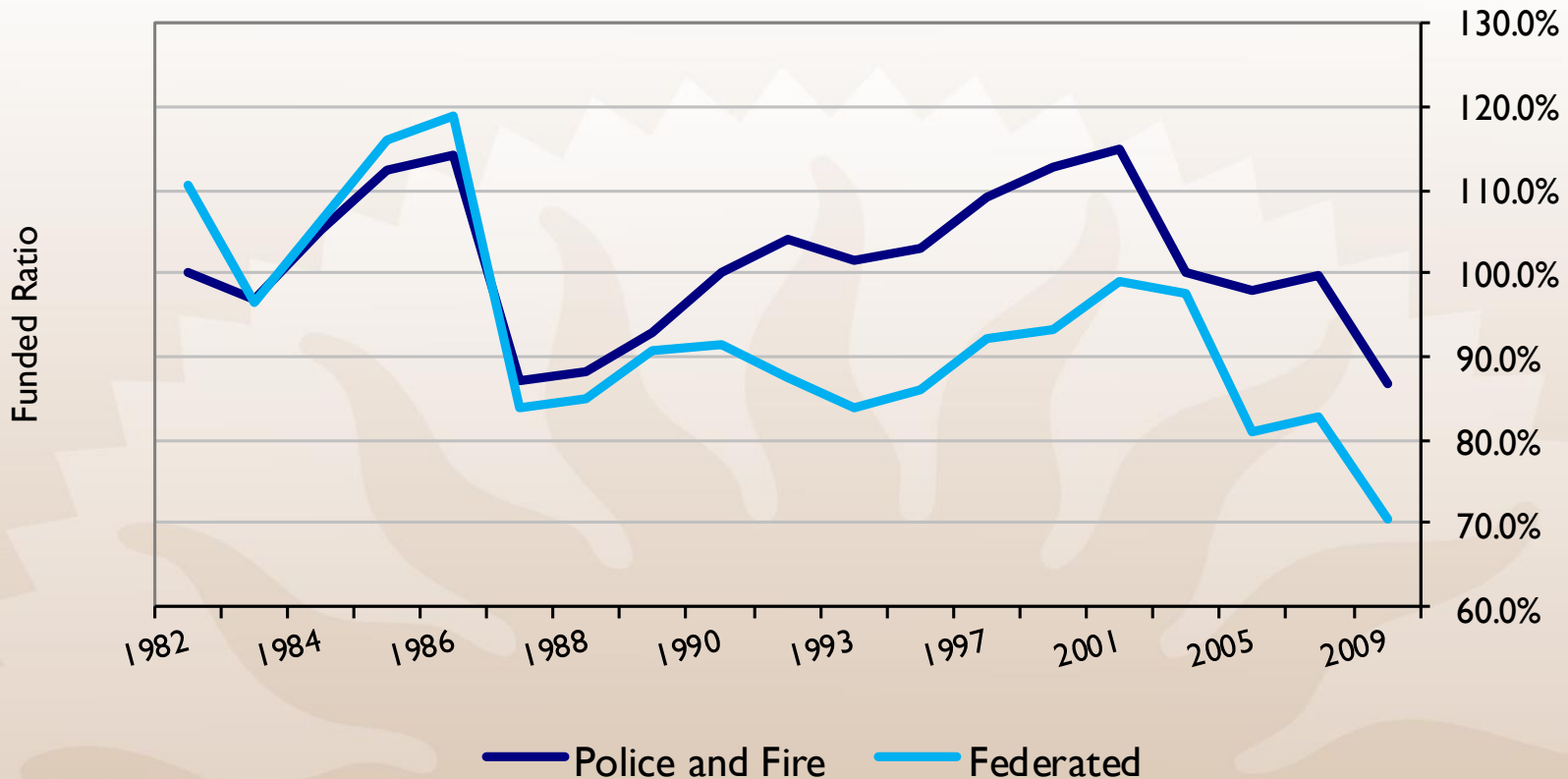


Pension Audit: Pension Benefit Payments Have Exceeded Contributions Since 2001



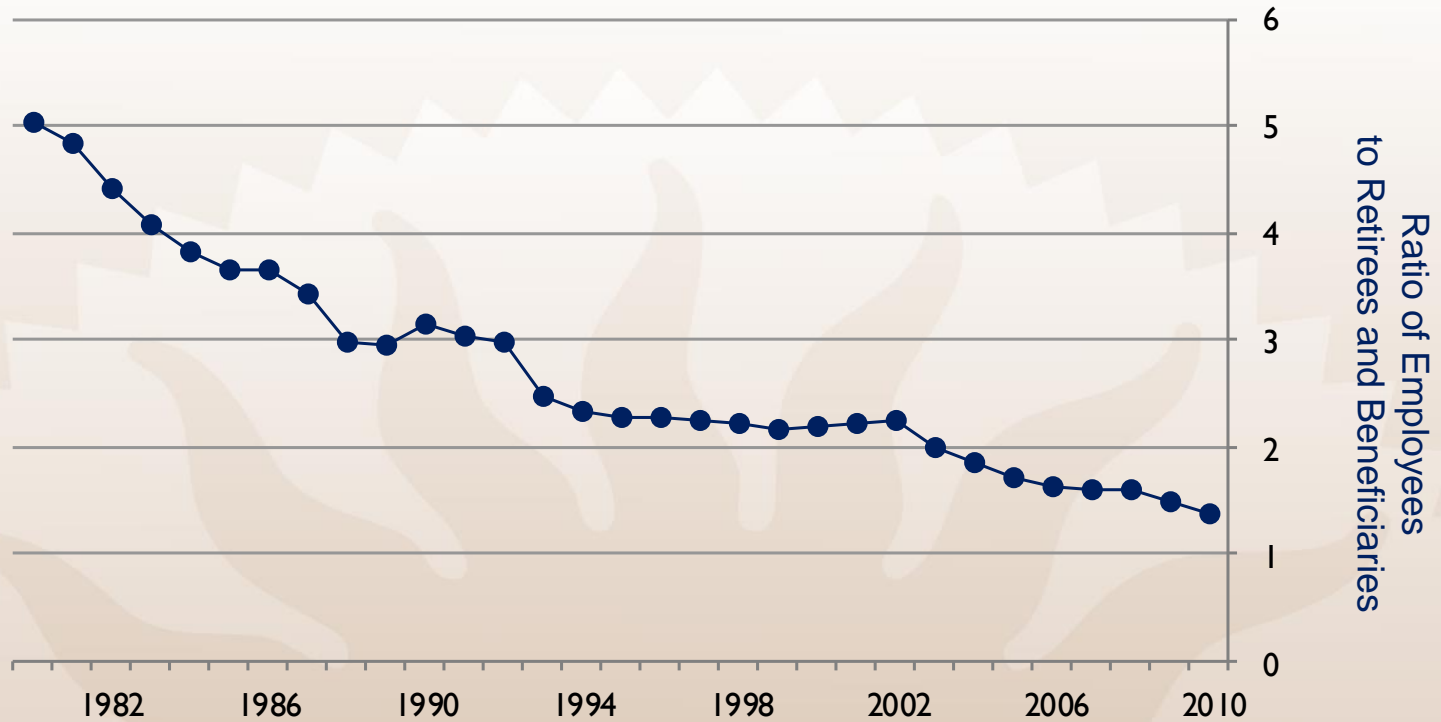
2010 Audit of Pension Sustainability

Pension Audit: Funded Ratios Have Fallen



2010 Audit of Pension Sustainability

Pension Audit: Declining Ratio of Employees to Retirees and Beneficiaries Creates a Risk of Even Higher Future Contribution Rates



2010 Audit of Pension Sustainability

Pension Audit: 2009 Estimate of the Pension Liability was \$5.4 Billion

- As of June 30, 2009
 - \$2 billion unfunded liability based on \$3.4 billion in pension assets (at market value)
 - \$1.1 billion unfunded liability based on \$4.3 billion in actuarial value of assets (smoothed)
- In addition, a \$1.4 billion unfunded retiree healthcare liability

Pension Sustainability Audit Conclusion

- Considerable risks from rising pension costs for years to come
- Rising pension costs threaten the City's ability to maintain service levels
 - Understanding how we got here
 - Identifying major cost drivers
 - Initial assessment of alternatives

2013 Unfunded Liability and Funding Ratio

| As of June 30, 2014 CAFR | Unfunded Liability | Funding Ratio |
|------------------------------------|--------------------|---------------|
| Federated Pension | \$1.231 B | 59% |
| Federated Retiree Healthcare | \$713 M | 18% |
| Police and Fire Pension | \$806 M | 77% |
| Police and Fire Retiree Healthcare | \$625 M | 11% |
| Total Unfunded Liability | \$3.375 B | |

Planning and Community Involvement

- Extensive Community Engagement (2007 and ongoing)
 - Several Stakeholder Groups (e.g., Budget Shortfall Advisory Group, General Fund Structural Deficit Elimination Plan Stakeholder Groups, Employee Groups, Program Prioritization Effort)
 - Annual Budget Surveys
 - Annual Neighborhood Association/Youth Commission Priority Setting Sessions
 - Annual Community Budget Meetings in Each Council District
- General Fund Structural Deficit Elimination Plan (2008)
- Fiscal Reform Plan (2011)

Strategies Used to Address Shortfalls

Strategy #1 **Cost Savings**

Strategy #2 **Revenues**

Strategy #3 **Service Reductions/Eliminations**

#1: Cost Savings Strategies

- Wage freezes
- 10% total compensation reductions and rollback of 2010-2011 wage increases for certain bargaining units (\$40 million)
- Pension reform, including Supplemental Retiree Benefit Reserve (SRBR) elimination, retiree healthcare changes (lowest cost plan), and new Tier 2 retirement plans (\$25 million)
- Outsourced City services at lower cost
- Consolidated City operations and services
- Implemented new technology in libraries to reduce staffing needs
- Civilianized police functions to lower costs
- Developed public-private partnerships for parks maintenance

#1: Cost Savings Strategies

Retirement Reform

| Retirement Reform Estimate | GF Savings |
|--|---------------|
| Implemented | |
| SRBR Elimination | \$13 M |
| Retiree Healthcare Changes (lowest cost plan) | \$7 M |
| New Tier 2 Retirement Plans | \$5 M |
| <i>Subtotal Implemented</i> | <i>\$25 M</i> |
| Not Yet Implemented | |
| Tier 1 Employees (additional contributions/after 4 years)* | \$46 M |
| Disability (workers' compensation offset)* | 3 M |
| <i>Subtotal Not Yet Implemented</i> | <i>\$49 M</i> |
| Total Retirement Reform Estimate | \$74 M |

* Preliminary Estimates

#2: Revenue Strategies

- **Voter-Approved Ballot Measures**

- Nov. 2008 – replaced Emergency Communication System Support Fee with Telephone Line Tax (\$20.5 million – not new revenue)
- Nov. 2008 – reduced/broadened the Telephone Utility Tax (\$30.8 million – not new revenue)
- June 2010 – \$3 million by increasing Cardroom Business Tax rate and increasing number of cardroom tables allowed
- Nov. 2010 – \$2.5 million by establishing Marijuana Business Tax; \$1.5 million from increase to tax rate to max. allowable in 2013

- **Adjusted Fees and Charges**

- Fees and Charges adjusted to maintain or achieve cost recovery

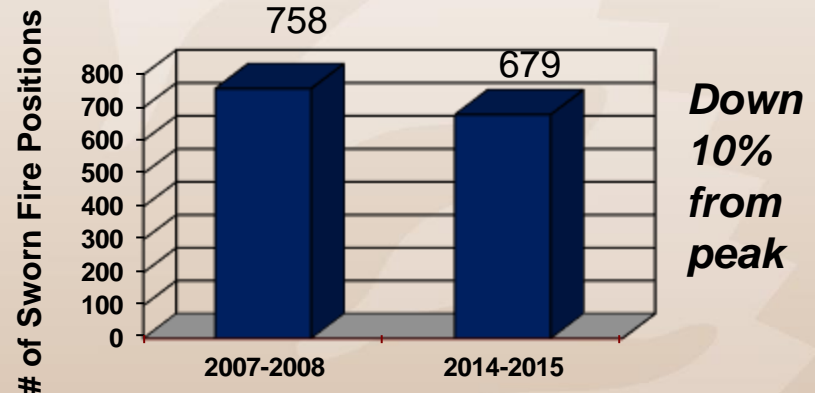
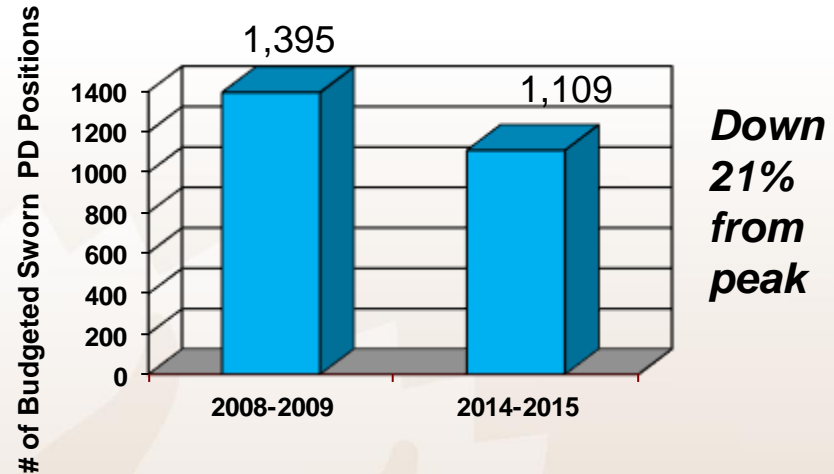
- **Used One-Time Revenue Sources**

- Exhausted City's Economic Uncertainty Reserve – \$15.8 million in 2001-2002 spent down to zero as of 2011-2012
- Made maximum allowable transfers from other funds (e.g., Construction Excise Tax Fund)
- Used revenue from legal settlements and property sales

#3: Service Reductions/Eliminations

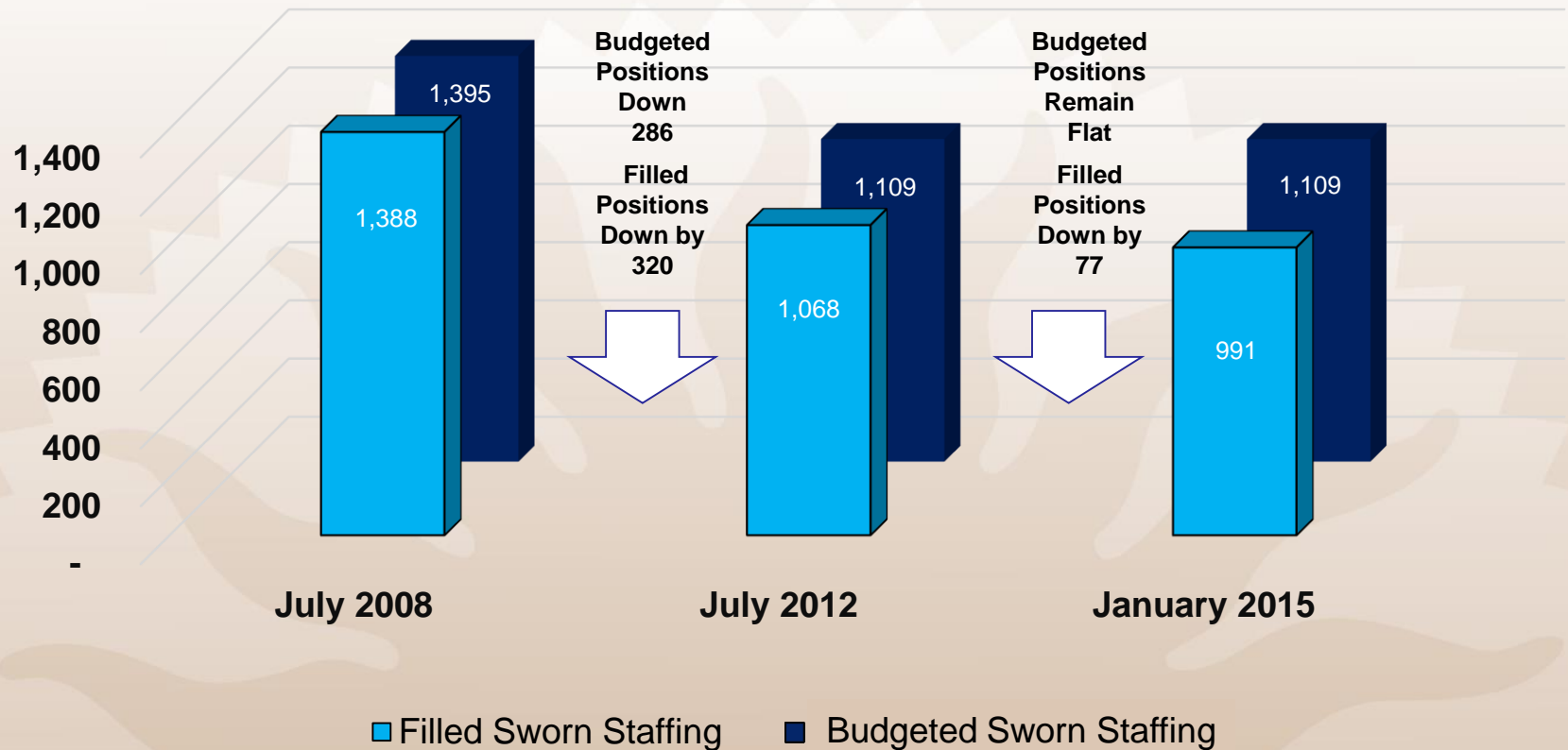
Public Safety

- Reduced police field patrol, special operations (metro, downtown, VCET, curfew, canine, horse mounted units) and investigative services in all areas
- Reduced school liaison, PAB lobby hours/staff, police pre-processing center, training, performance analysis and research
- Reduced crime prevention program
- Reduced police and fire staffing at the airport
- Eliminated fire engine companies and a truck company
- Implemented fire company brown-outs
- Reduced fire apparatus staffing



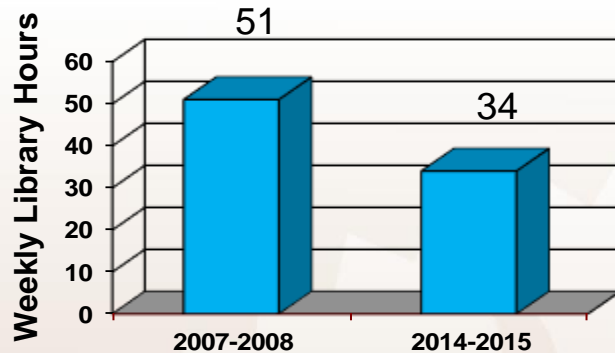
#3: Service Reductions/Eliminations

Police Sworn Staffing

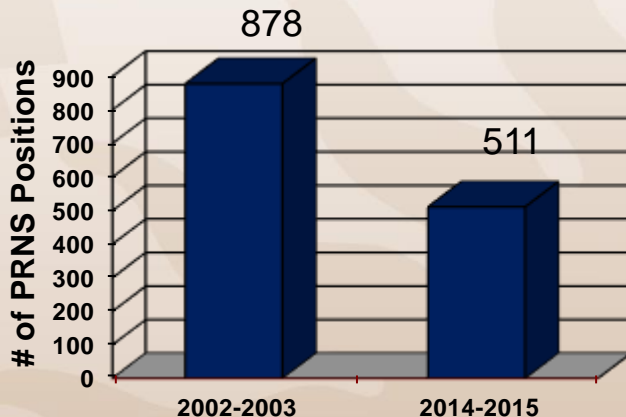


#3: Service Reductions/Eliminations

**Down
33%
from
peak**



**Down
42%
from
peak**



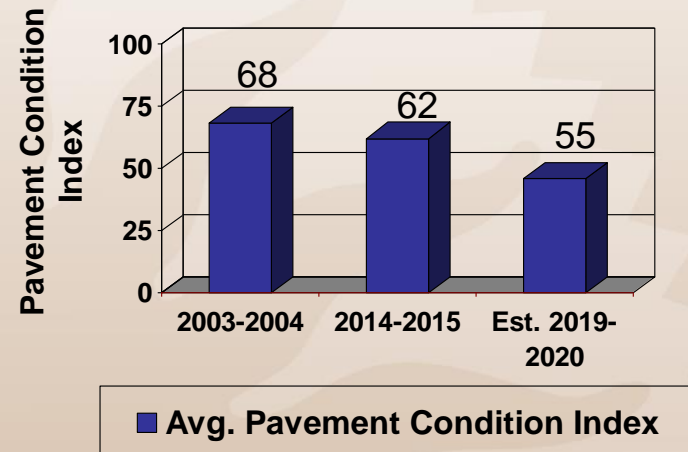
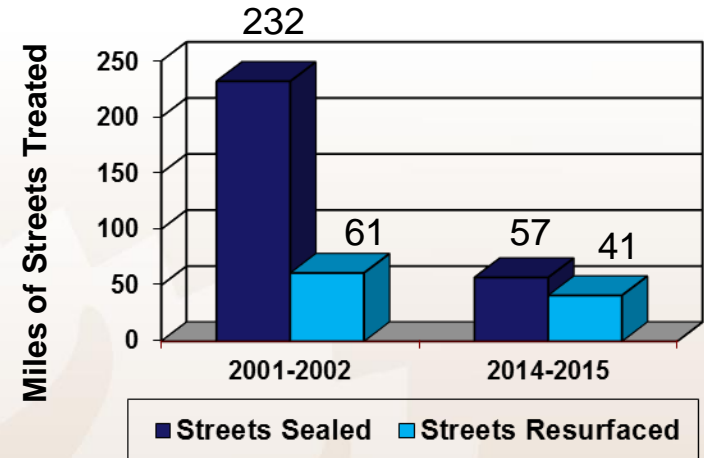
Neighborhood Services

- Reduced branch library hours/days (from 47-51 hours/6-7 days per week to 33-34 hours/4 days per week) and library services
- Reduced community centers (down from 56 at peak in 2007-2008 to 12 in 2014-2015; 42 sites in re-use program)
- Reduced neighborhood and regional parks maintenance and park ranger staffing
- Reduced/eliminated recreational services and special events support
- Reduced/eliminated services to seniors, persons with disabilities, and youth
- Reduced code enforcement staffing
- Reduced strong neighborhoods initiative
- Reduced long-range planning services

#3: Service Reductions/Eliminations

Transportation and Public Works

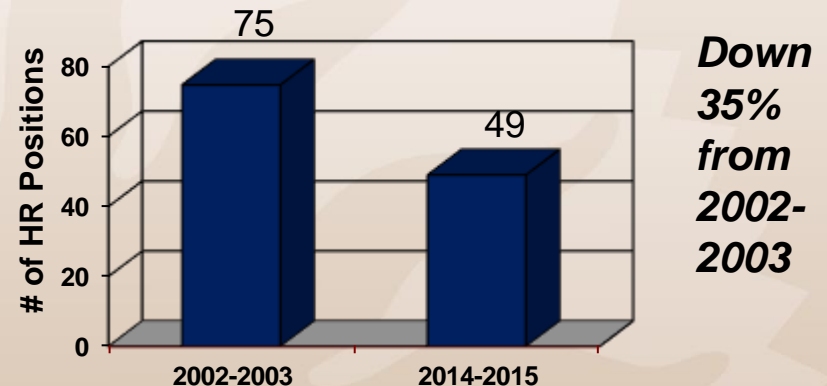
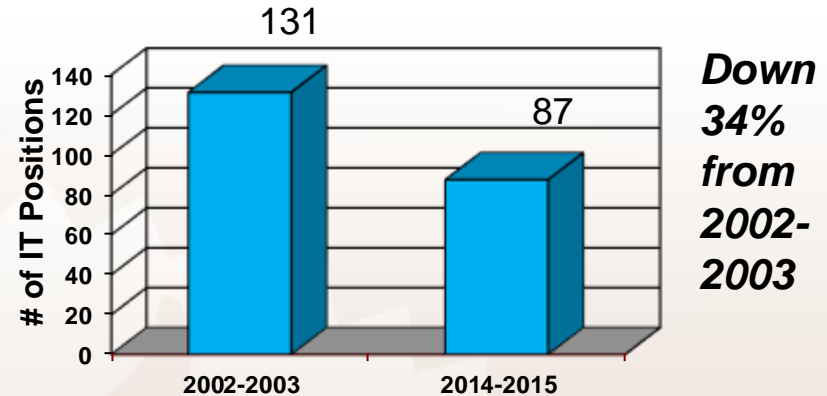
- Less resources for pavement maintenance (special funds, grants)
- Reduced traffic maintenance program (e.g., traffic signals, streetlights, street name signs, and roadway striping and markings maintenance)
- Eliminated funding for sidewalk repairs and street tree services (property owners responsible)
- Reduced street landscape services
- Reduced transportation operations services (e.g., traffic calming, neighborhood traffic studies, responses to speed compliance calls)
- Reduced City facilities maintenance and fleet maintenance



#3: Service Reductions/Eliminations

Strategic Support

- Reduced financial reporting, financial management, and finance administrative staffing
- Reduced employment services, safety program, workers' compensation claims administration, and training and development
- Reduced city-wide technology coordination, and information technology infrastructure support
- Reduced organization-wide management, support, and leadership staffing



Budget Stabilized but Fragile

- Most recent five-year forecast (February 2014) shows General Fund revenues and expenditures in close alignment

2015-2019 General Fund Forecast Incremental General Fund Surplus/(Shortfall)

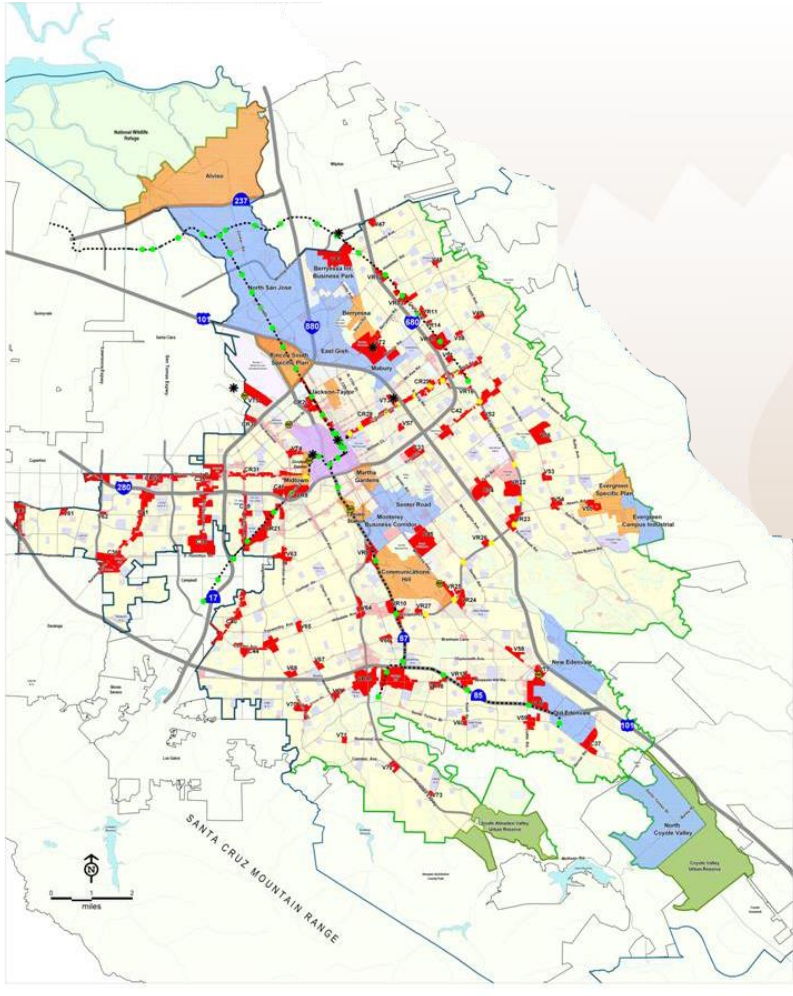
| | 2015-2016 | 2016-2017 | 2017-2018 | 2018-2019 |
|-------------------------------|------------|-----------|-----------|-----------|
| Incremental Surplus/Shortfall | (\$2.4 M)* | \$0.4 M | (\$6.5 M) | (\$1.7 M) |
| % of Annual Budget | (0.1%) | 0.02% | (0.3%) | (0.1%) |

* The 2015-2016 figure was updated from a \$4.2 million shortfall to a \$2.4 million shortfall to reflect actions in the 2014-2015 Adopted Budget.

Does not include:

- Fully funding the annual required contributions for police/fire retiree healthcare
- Elements of Fiscal Reform Plan not yet implemented
- Restoring key services to January 1, 2011 levels
- Police Staffing Restoration Strategy (increase number of sworn officers to 1,250)
- Unmet/deferred infrastructure and maintenance needs
- One-time revenue sources or expenditure needs

Factors Constraining Revenue Growth in San Jose



**UNDERLYING
PROBLEM:
CAN'T SOLVE
QUICKLY**

Other Cities

**VERY HIGH
HOME VALUES**



**LESS HOUSING
STRONG ECONOMIC BASE**



San Jose

LOTS OF LOW DENSITY HOUSING...

RELATIVELY WEAK ECONOMIC BASE

Jobs in San Jose

SAN JOSE IS UNIQUELY

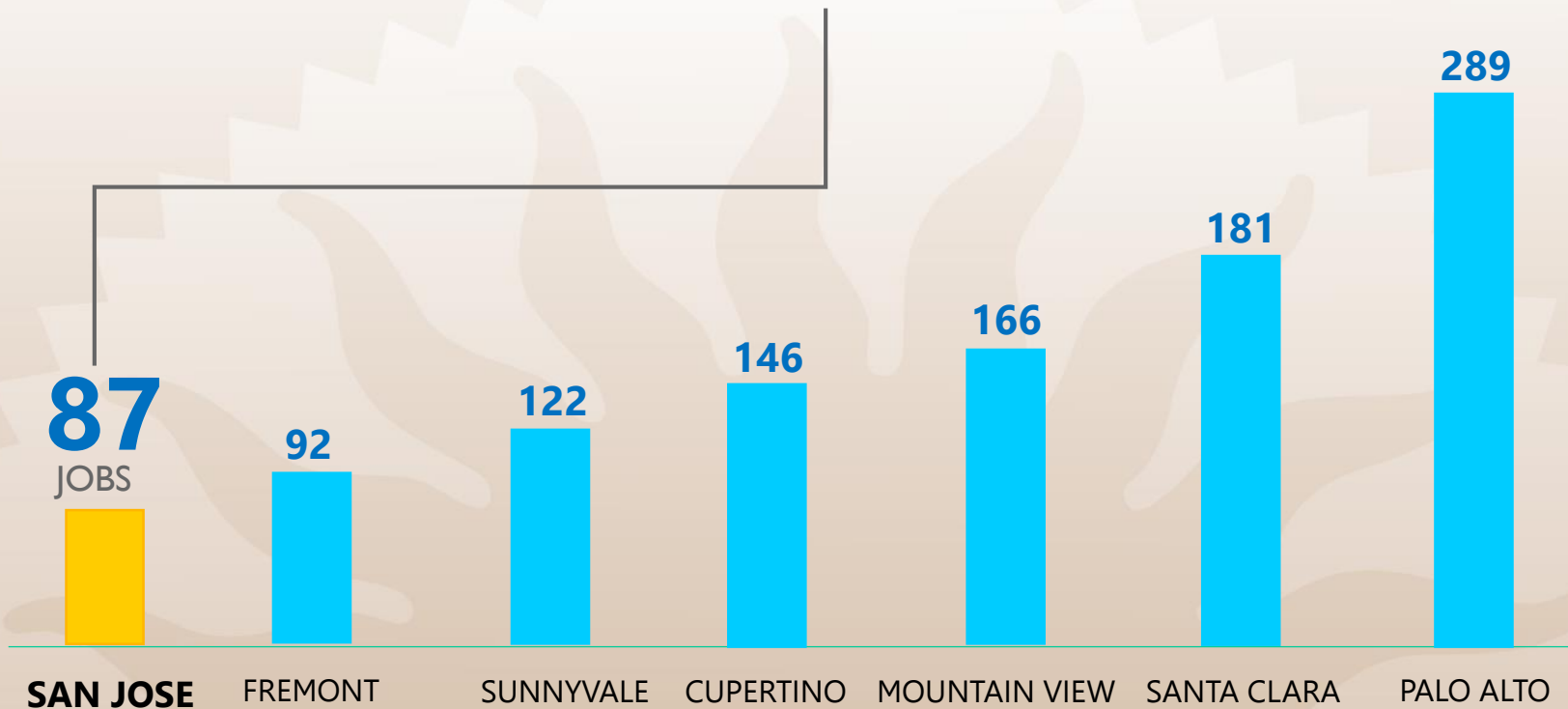
“JOBS-POOR”

RELATIVE TO OUR
RESIDENT BASE



Lower Jobs Per Resident

FOR EVERY **100** RESIDENTS,
THERE ARE ONLY



Jobs in San Jose

THE ONLY TOP 20 CITY NATIONALLY



WITH MORE NIGHTTIME RESIDENTS THAN DAYTIME WORKERS

Lower Sales Tax Per Capita

PALO ALTO

\$370

CUPERTINO

\$338

MOUNTAIN VIEW

\$186

SANTA CLARA

\$320

SUNNYVALE

\$192

FREMONT

\$172

SAN JOSE

\$142

Lower Property Tax Per Capita

PALO ALTO

\$407

CUPERTINO

\$285

SUNNYVALE

\$213

MOUNTAIN VIEW

\$260

SANTA CLARA

\$237

FREMONT

\$172

SAN JOSE

\$140

Service Restoration Priorities



Service Restoration Direction

- City Council directed Administration to use the list of baseline services as of January 1, 2011 to guide selected General Fund City service restorations
 - Police
 - Fire
 - Libraries
 - Community Centers
 - Street Maintenance
- Police Staffing Restoration Strategy (increase sworn Police staffing from 1,109 to 1,250)

Service Delivery Goals (January 1, 2011)

Police

January 1, 2011 Service Levels*:

On average, response time for Priority One police calls for service of 6.04 minutes

On average, response time for Priority Two police calls for service of 12.74 minutes

On average, clearance rate for Part 1 crimes as follows:

Homicide (65.00%)

Rape (19.37%)

Robbery (26.54%)

Aggravated Assault (39.93%)

Burglary (5.58%)

Larceny (18.90%)

Vehicle Theft (8.85%)

Opening of South San Jose Police Substation

* *Calendar year 2010 actuals*

Current Service Levels*:

On average, response time for Priority One police calls for service of 6.7 minutes

On average, response time for Priority Two police calls for service of 20.5 minutes

On average, clearance rate for Part 1 crimes as follows:

Homicide (60.6%)

Rape (15.4%)

Robbery (31.5%)

Aggravated Assault (45.0%)

Burglary (5.3%)

Larceny (16.1%)

Vehicle Theft (5.4%)

Repurposed South San Jose Police Substation

* *Fiscal year 2013-2014 actuals*

Service Delivery Goals (January 1, 2011)

Fire

January 1, 2011 Service Levels:

33 Fire Stations Open

On average, responding fire unit arrives within 8 minutes 78.7% of the time for Priority 1 calls*

On average, responding fire unit arrives within 13 minutes 92.7% of the time for Priority 2 calls*

Current Service Levels (2013-2014 actuals):

33 Fire Stations Open

On average, responding fire unit arrives within 8 minutes 68% of the time for Priority 1 calls*

On average, responding fire unit arrives within 13 minutes 84% of the time for Priority 2 calls*

* Baseline performance restated due to data collection issues in prior years; performance measures updated to include response time performance for Priority 1 and Priority 2 calls rather than first due and second due units.

Service Delivery Goals (January 1, 2011)

Libraries

January 1, 2011 Service Levels:

On average, 18 library branches open
39 hours/week

King Library Services:

Open 72 hours per week per academic
semester/58 hours per week otherwise

Children's Room – 50 hours/week

3rd floor General Collection and Reference desks –
64 hours/week

California Room – 25 hours/week

Access Services, Periodicals, 2nd Floor Reference
Desk – 72 hours/week

Current Service Levels:

On average, 22 library branches open
33-34 hours/week

King Library Services:

78 hours/week during semester, 71 hours/week
during summer, 63 hours/week during winter break

64 hours/week during semester, 58 hours/week
during summer, 52 hours/week during winter break

64 hours/week during semester, 52 hours/week
during summer & winter

25 hours/week

78 hours/week during semester, 71 hours/week
during summer, 63 hours/week during winter break

Service Delivery Goals (January 1, 2011)

Community Centers

January 1, 2011 Service Levels:

- On average, 10 Hub Community Centers open 63 hours/week*
- On average, 9 Satellite Community Centers open 40 hours/week – City operated*
- On average, 8 Neighborhood Centers open for 15 hours of programming/week – City operated*

Current Service Levels:

- On average, 10 Hub Community Centers open 59 hours/week
- On average, 0 Satellite Community Centers – City operated
- On average, 0 Neighborhood Centers – City operated

* Over 50 total centers were open in 2010-2011 but not included in the above baseline service numbers since many were operated by re-use partners. Currently 54 total centers, including 12 City operated and 42 operated by re-use partners.

Service Delivery Goals (January 1, 2011)

Street Maintenance

January 1, 2011 Service Levels:

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). Maintaining this street maintenance level is contingent upon receiving commensurate levels of regional, state, and federal funds annually.

Current Ongoing Service Levels:

Current base funding of \$20 million will seal approximately 30 miles of arterial (major) streets and resurface approximately 5 miles of arterial streets with no funding for residential streets.

Strategic Support Resources

Strategic Support resources should be considered when restoring direct services to ensure effective service delivery:

- **Finance:** purchasing/procurement; accounts payable/receivable; payroll; and payment processing
- **Human Resources:** employment services; workers' compensation; and training/workforce planning and development
- **Information Technology:** network support; application programming and support; and technical engineering
- **Public Works:** custodial services; facilities preventative maintenance and corrective repairs; fleet services; vehicle replacement; and utilities and fuel
- **City Attorney:** legal representation
- **City Auditor:** audit services
- **City Manager:** organizational leadership and management

General Fund Costs to Restore Services to January 2011

| Service | Description | FTE | Cost |
|-------------------|--|--------------|------------------|
| Police | Increase patrol, investigations, school liaison program, special investigations, sexual assaults, school safety, reserves unit, and training unit staffing | 129 | \$ 24.1 M |
| Fire | Fire company restoration; eliminate brown-outs | 14 | \$ 7.0 M |
| Libraries | Restore branch library hours from 33-34 hours/week to 40 hours/week (5 days/week under new model) | 33.5 | \$ 1.8 M |
| Community Centers | Restore Community Center hours from 59 to 63; restore satellite/neighborhood centers (old model – would need further evaluation if restored) | 53 | \$ 3.7 M |
| Total | | 229.5 | \$ 36.6 M |

Police Staffing Restoration Strategy

Mayor's June Budget Message for Fiscal Year 2014-2015

- **Goal:** Increase Police sworn staffing from 1,109 to 1,250 positions (141 positions)
- **Cost to Meet Staffing Goal:** approximately \$25 million (multi-year implementation beginning in 2018-2019)
- **Comparison to January 2011 Service Delivery Goal:** Adds 12 additional sworn positions at an additional cost of \$2 million

Pavement Maintenance Status

- **City's largest infrastructure asset**
 - 2,400 miles
- **Overall condition is declining**
 - Age, lack of investment for preventative maintenance
 - Declining revenue, escalating cost
 - Overall condition is “fair” (PCI 63)
 - \$440M backlog; 25% in “poor” condition
- **Annual need is \$100M; Base funding is \$20M**

Pavement Condition Index (PCI)



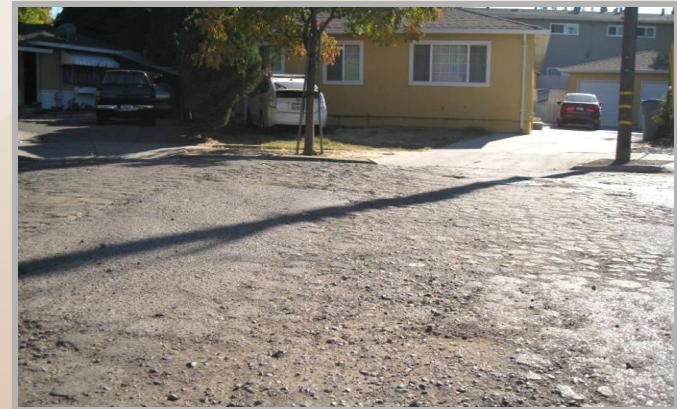
Good (70-100)



Fair (50-70)

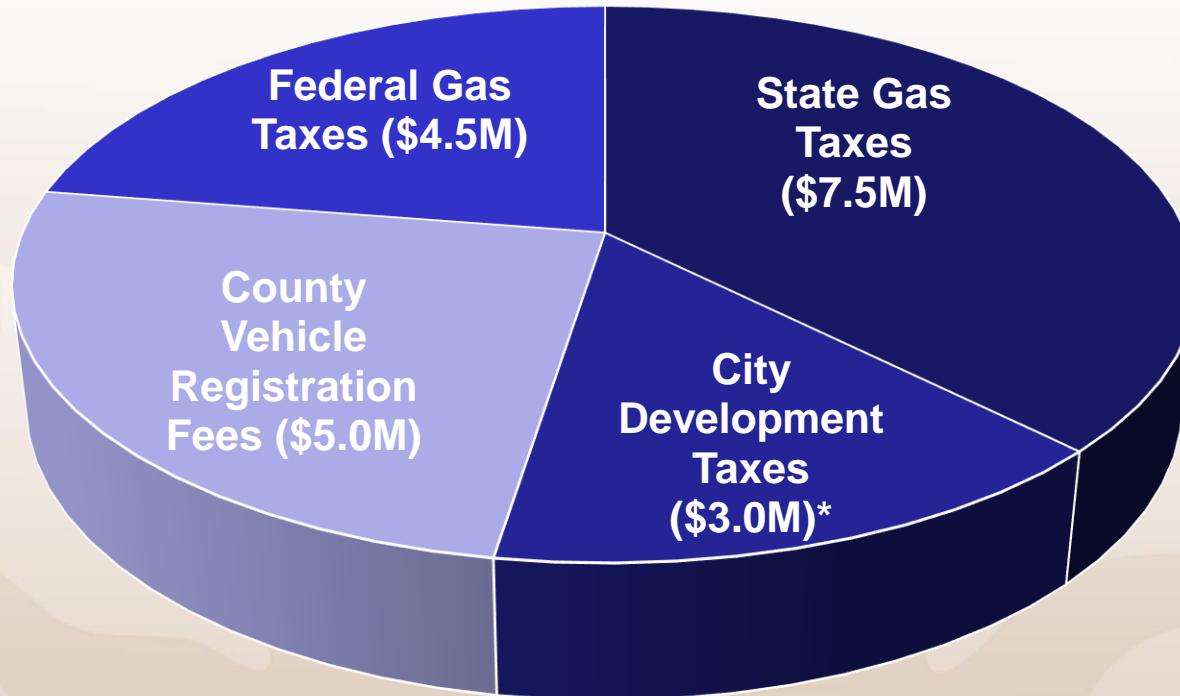


Poor (25-50)



Failed (Below 25)

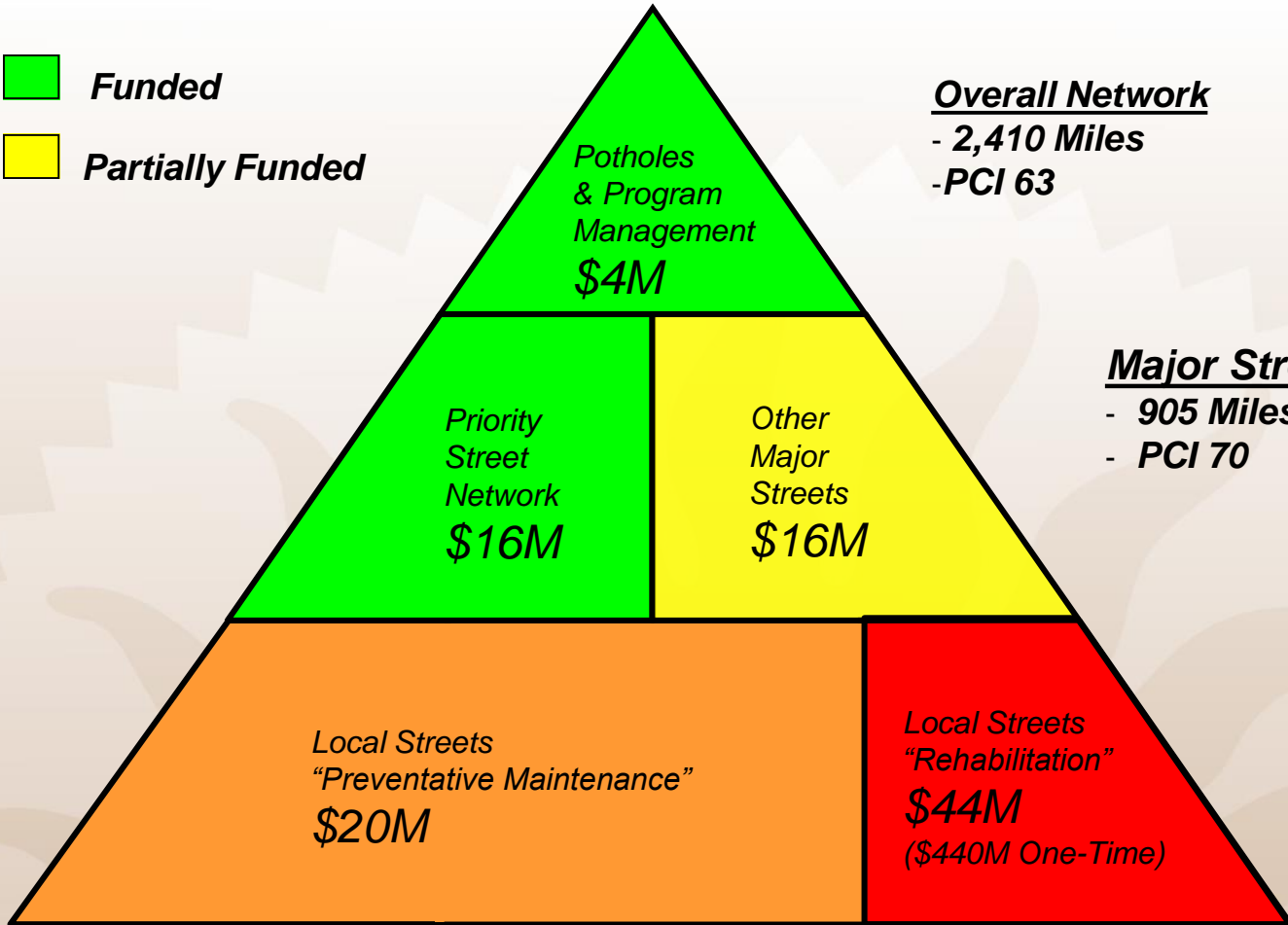
Base Funding Level Current Sources (\$20M)



* City Funding in 2014-2015 is \$24M

Pavement Maintenance “Pyramid”

-  **Funded**
-  **Partially Funded**



Overall Network

- 2,410 Miles
- PCI 63

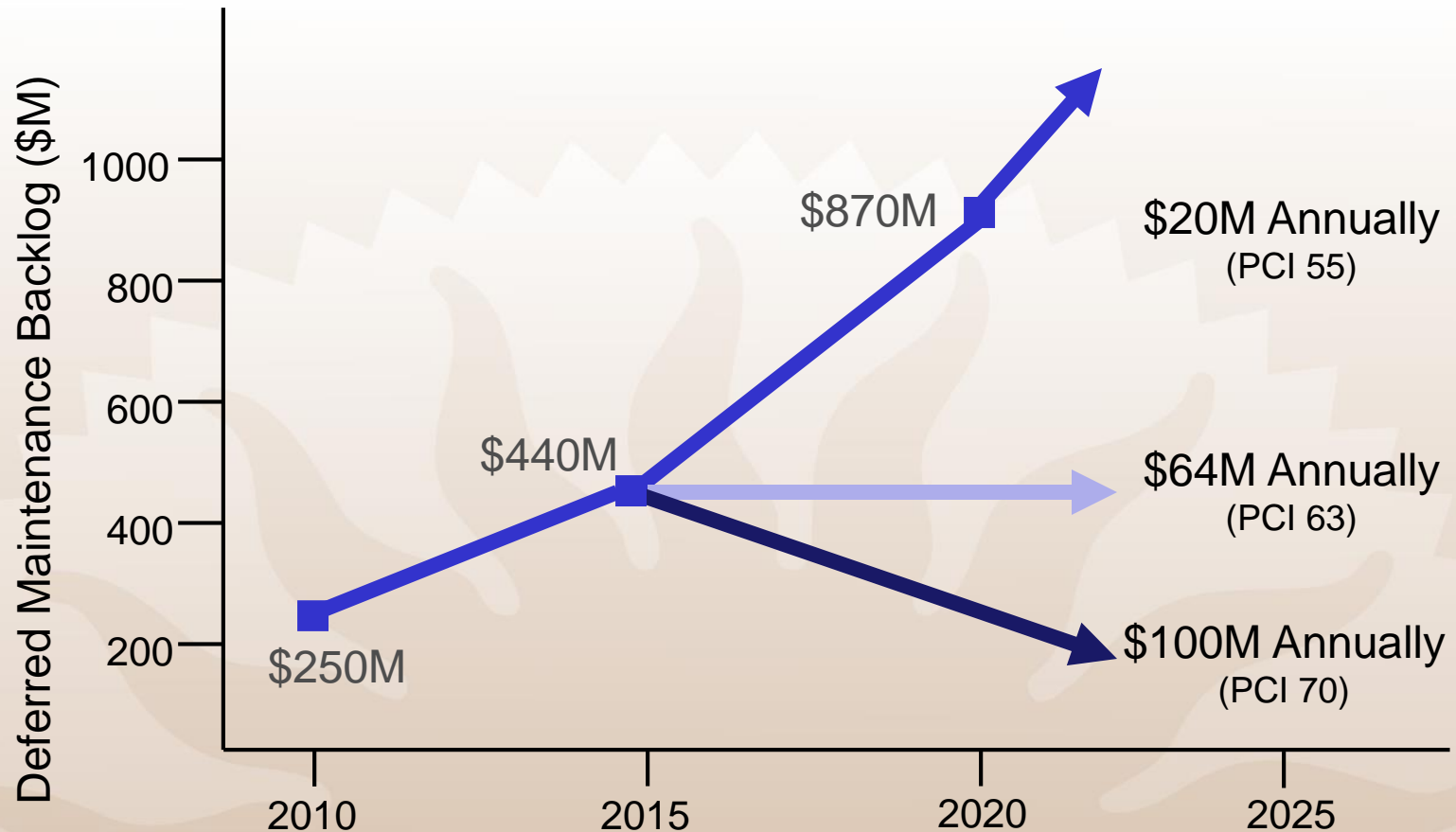
Major Streets

- 905 Miles
- PCI 70

Local Streets

- 1,505 miles
- PCI 58

Pavement Maintenance Investment Outcomes



Potential Transportation Funding

| | |
|--|-----------------------|
| City Bond Measure | Up to \$440M one-time |
| City Sales Tax Measure - Portion of ½¢ or ¼¢ increase | Up to \$20M annually |
| VTA Transportation Tax Measure | Up to \$20M annually |
| State/Federal Funding - Gas Tax - Vehicle License Tax | Up to \$20M annually |



Service Restoration Funding Strategies

Potential Revenue Measures

- **Fiscal Reform Plan**

- Sales Tax (1/4 cent = \$34 M, 1/2 cent = \$68 M)
- Business Tax Modernization (\$5 M - \$10 M)
- Disposal Facility Tax (\$5 M)
- Municipal Water System Tax (\$3 M)

- **Other Tax Measures**

Cost Savings Strategies

- **Pension Reform – Current Tier 1 Employees (Measure B)**
 - Additional contributions to current retirement system or opt in to plan with reduced benefits (VEP) (\$46 M after 4 years)
 - 4% annual increases with cap of 16% (no more than 50% of the cost of Tier 1 unfunded liabilities)
 - If VEP not in place, compensation adjustments would apply
 - Not implemented as a result of stipulation in Measure B litigation
 - VEP not yet approved by IRS

Cost Savings Strategies

- **Pension Reform – Disability Retirement**
 - Change to eligibility requirements surrounding ability to perform work
 - Eliminate duplication of benefits for same cause of disability (workers' compensation benefits and disability retirement benefits) (\$3 M)
- **Overtime Pay**
 - Eliminate overtime pay above Federal Fair Labor Standards Act (FLSA) requirement (\$1 M)

Police Staffing Restoration Strategy

Mayor's June Budget Message for Fiscal Year 2014-2015

- **Goal:** Increase Police sworn staffing from 1,109 to 1,250 positions
- **Funding Strategies:**
 - Set aside \$10 million in the 2014-2015 Adopted Budget (\$500,000 ongoing) in a Police Department Staffing Reserve
 - Ongoing cost savings from new police officers who receive Tier 2 retirement benefits
 - One-time savings within the Police Department from unfilled positions that are not rebudgeted for police overtime or other urgent needs (\$3 million added to Police Department Staffing Reserve in 2013-2014 Annual Report, bringing reserve to \$13 million)

Summary of Funding Needs and Potential Solutions

| Ongoing Funding Needs | | Ongoing Funding Sources | |
|---|----------------|---|---------------------|
| January 1, 2011 Service Levels | \$ 37 M | Potential Revenue Solutions* | |
| Police Sworn Staffing Restoration Strategy (12 additional positions to reach 1,250 sworn positions) | \$ 2 M | Sales Tax (1/4 cent or 1/2 cent) | \$ 34-68 M |
| Street Maintenance | \$44 M | Business Tax Modernization | \$ 5-10 M |
| Total | \$ 83 M | Disposal Facility Tax** | \$ 5 M |
| | | Municipal Water System Tax** | \$ 3 M |
| | | Potential Revenue Solutions Subtotal | \$ 47-86 M |
| | | Potential Expenditure Solutions | |
| | | Pension Reform – Tier 1 Additional Contributions/Opt-In (after 4 years) | \$ 46 M |
| | | Police Tier 2 Retirement | \$ 3 M |
| | | Pension Reform – Disability** (workers' compensation offset) | \$ 3 M |
| | | Overtime Pay** | \$ 1 M |
| | | Potential Expenditure Solutions Subtotal | \$ 53 M |
| | | Total | \$ 100-139 M |

* Require voter approval

** Rounded figures reported in 2011 Fiscal Reform Plan

Upcoming Key Dates

January 2015

- 2014-2015 Mid-Year Budget Review Released

February 2015

- City Council Review and Approval of 2014-2015 Mid-Year Budget Review
- 2015-2016 City Manager's Request and 2016-2020 Five-Year Forecast and Revenue Projections for the General Fund and Capital Improvement Program Released

March 2015

- City Council Final Review and Approval of Mayor's March Budget Message

April/May 2015

- 2015-2016 Proposed Capital/Operating Budgets/2016-2020 Proposed CIP/2015-2016 Fees and Charges Released
- City Council Budget Study Sessions and Initial Budget Public Hearing

June 2015

- Final Budget Public Hearing
- City Council Reviews Mayor's June Budget Message and Final Review of Budgets
- City Council Approves 2015-2016 Capital/Operating Budgets and Fees & Charges

Outstanding Lease Revenue Bonds

| | Interest Rate Range | Final Maturity | Call Date ¹ | Outstanding Principal (\$ in thousands) |
|---|---------------------|----------------|------------------------|---|
| Series 2001F (Convention Center) | 5.00% | 9/1/2022 | 9/1/2011 | \$ 110,300 |
| Series 2003A (Central Service Yard) | 4.00 - 4.70% | 10/15/2023 | 10/15/2013 | 13,400 |
| Series 2006A (Civic Center Project) | 4.10 - 5.00% | 6/1/2039 | 6/1/2016 | 56,125 |
| Series 2007A (Recreational Facilities) | 4.13 - 4.75% | 8/15/2030 | 8/15/2017 | 28,665 |
| Series 2008C (Hayes Mansion) | variable | 6/1/2027 | n/a | 10,915 |
| Series 2008D - Taxable (Hayes Mansion) | variable | 6/1/2025 | n/a | 28,920 |
| Series 2008E (Taxable) (Ice Centre) | variable | 6/1/2025 | n/a | 21,140 |
| Series 2008F (Taxable) (Land Acquisition) | variable | 6/1/2034 | n/a | 62,105 |
| Series 2011A (Convention Center) | 3.00 - 5.75% | 5/1/2042 | 5/1/2021 | 30,985 |
| Series 2013A (Civic Center Project) | 3.00 - 5.00% | 6/1/2039 | 6/1/2023 | 305,535 |
| Series 2013B (Civic Center Garage) | 3.00 - 5.00% | 6/1/2039 | 6/1/2023 | 30,445 |
| | | | TOTAL | 698,535 |

Notes: ¹ Variable rate bonds are generally callable on any interest payment date.



City Council Discussion