Special Meeting
April 30, 2012

The City Council of the City of Palo Alto met on this date in the Council Chambers at 5:09 P.M.

Present: Burt, Espinosa, Holman, Price, Scharff, Schmid, Shepherd, Yeh

Absent: Klein

ORAL COMMUNICATIONS

Todd Burke discussed the California Avenue project. He said he lived on California Avenue, and was President of the Homeowners' Association at Palo Alto Central. The Board voted to support the streetscape project. He appreciated Staff working with the community, and saw a number of benefits including a lane change. He wanted to find a middle ground with the businesses, and a way to work with those in extreme disagreement with the project. Staff had run a good campaign to include all residents and businesses.

Howard Hoffman called on the City Council to place on the ballot a measure to institute a 5 cents per gallon tax on gasoline and diesel fuel. Palo Alto had an opportunity to set an example for the County of Santa Clara, for all of California, and all of the United States. Any increase in the fuel tax would encourage Palo Alto residents to further reduce their consumption of gas and diesel. Most economists and environmentalists would rally to support such a ballot measure.

ACTION ITEMS

1. Presentation and Transmittal of FY2013 Proposed Budget – Referral to Finance Committee.

James Keene, City Manager reported no action was necessary on the Budget document. In accordance with his responsibility as City Manager, he was pleased to submit the City of Palo Alto's Proposed Fiscal Year (FY) 2013 Operating Budget. Since the fall of 2008, the City's General Fund had faced significant challenges. Recent economic data indicated reasonable growth for the world economy, a slow mend to the U.S. economy, and perhaps a faster rebound for Silicon Valley. Other positive data showed that retail sales in 2011 rose nearly 8 percent over 2010, manufacturers had increased production and hiring, agricultural exports had increased, new auto sales had increased, and the rate of housing foreclosures had declined. A recent consensus of economists predicted the economy would grow by 2.4 percent in 2012, a modest but welcomed rate. California had witnessed 21 straight months of GDP growth driven by exports from the technology and agricultural sectors. Unfortunately, these improvements for the State had been uneven geographically. Companies such as Apple, Google, and Facebook had been heavily recruiting workers. Unemployment rates remained stubbornly high, homeowners were concerned about the value of their homes, consumers were thrifty and paying down debt and the stock market was volatile. He said he was discussing issues outside the immediate budget conversation because the structural problems the City faced were part of a bigger picture, some of which the Council could control and others it could not. As with the nation, the Council could not completely "revenue a way out" of legacy benefits or looming infrastructure bills. The Council needed to continue efforts long underway to reduce salary and benefit cost structure, prioritize services, reallocate resources, and find new revenue sources, most of which would require voter approval. The FY 2013 Budget presented some difficult decisions and there would be more in the years ahead. The chief structural issue that the City faced was expenditures growing faster than revenues. The vast majority of operating expenses in the General Fund were salaries and benefits, which accounted for 63 percent of General Fund expenditures. As with all governments serving the public, it was people who delivered services. Unfortunately, like cities across California, the benefits paid to employees had risen over the past decade, dramatically in the past several years, and would continue to grow in the years ahead. To illustrate the trajectory of these increases, the ratio of benefits to salary had risen from 50 percent of salary in 2010, to 63 percent in 2012. In 2002, citywide pension costs were $3 million a year, and had risen to approximately $24 million a year in 2012. In large part, this increase was due to the California Public Employees' Retirement System (CalPERS) retirement portfolio dramatically dropping as a consequence of the recession. City contribution rates rose and fell based on the portfolio's performance as well as a variety of other factors, such as the number and demographics of active and retired City employees. The City's pension costs had skyrocketed and would continue to grow, because of the large retroactive benefit increases granted in 2001 to Public Safety employees (a 50 percent retroactive lifetime benefit increase) and in 2007 to non-safety employees (a 35 percent retroactive lifetime benefit increase). In granting such unsustainable benefit increases, Palo Alto was following cities across California that had done the same. Citywide healthcare costs had also risen considerably, from $6.6 million in 2002 to $14.9 million in 2012. The City's current liability for retiree health benefits had risen from $105 million in

January 2009 to $134 million three years later. The effect had been to raise the annual funding requirement Citywide towards the retiree healthcare liability from $9.8 million a year to $12.5 million. The City, like other jurisdictions and the nation, was confronting a dramatic compensation structure imbalance as well as a looming infrastructure bill. The City had made significant strides with its employees over the past three years to recalibrate its compensation structure. The City was in the latter stage of negotiations with the Police Officers' Association and the Police Management groups. With the exception of these two groups, the following important labor concessions had occurred: cost of living freezes since FY 2010 (over three years) for Management, Professional, and Service Employees International Union (SEIU) employees; Fire personnel wage freeze from FY 2011 through FY 2014; implementation of a 90/10 medical cost sharing plan for Management, SEIU, and Fire; eliminating the variable management compensation plan for the Management and Professional group; eliminating tuition reimbursement for SEIU and Fire personnel; increasing the employee pay contribution to pension plans for SEIU and Fire; and instituting new two-tier retirement systems for new employees in Management, Professional, SEIU, and Fire personnel. In terms of actual General Fund expense reductions, the City had realized nearly $3.6 million annually in concession savings from SEIU, Management, and Fire employees. Moreover, in changing pension plans, pursuing employee payment of employee share of pension costs, and requiring contributions to medical costs, the City would reduce future employee costs as employees retired or left the City. As a result of these benefit changes, the trend line for rising benefit costs causing structural dislocations had been driven downward. Benefits continued to rise and, since pension benefit changes only applied to new employees, it would take a long time for the City to recover from this predicament. The Council had been committed to approaching the City's wage and benefit issues with the principle of fairness and consistency to all employees. The Council had pursued a guiding principle that all bargaining groups should share equally in terms of the percent of total compensation in contributing to a solution to the City's immediate and long-term fiscal demands. Similar concessions to those mentioned had been proposed to Police personnel, and the City hoped these negotiations could be concluded to help reduce anticipated deficits. The Council estimated that those negotiations could result in an additional $1.5 million in savings to the General Fund. The Proposed Budget anticipated Police savings beginning at the start of the fiscal year on July 1, 2012. In addition, negotiations with SEIU had begun, and those with the Managers and Professional group would soon follow. Based on the financial forecast, the City would need additional compensation savings from these groups as well as Public Safety units when their contracts expired. No cost savings from Management and SEIU groups were included in the Proposed FY 2013 Budget, because that process was not concluded. It was important to note that in addition to those compensation adjustments, Staff had reviewed operations and realized cost savings and efficiencies in recent years. On an annual basis, Public Works reorganized operations to save $356,000 a year. The Council had contracted a portion of parks maintenance for Mitchell Park, Rinconada Park, and the Lucie Stern Community Center, saving $314,000 a year; contracted golf course maintenance, reducing costs by $338,000; contracted custodial maintenance; initiated a Computer Aided Dispatch (CAD) Records Management System (RMS) agreement with the cities of Mountain View and Los Altos; and initiated a new Procurement Card that would result in some cost savings and efficiencies. These reductions, together with prior year changes, reduced the General Fund's structural spending deficit by $14 million and eliminated over 60 positions, approximately 10 percent of the City's General Fund workforce. Overall, General Fund sources of funds were budgeted at $151 million, a $4.5 million or 3.1 percent increase over the Adopted FY 2012 Budget and a $0.7 million or 0.5 percent increase over the Adjusted FY 2012 Budget adopted by the Council in the past month. Staff projected solid increases in sales tax, property tax, Transient Occupancy Tax (TOT), and documentary transfer taxes for FY 2013, but these had been offset by drops in rental income and other revenues. In the past year, the City had witnessed a rebound in economically sensitive revenue sources. Sales taxes, originally budgeted at $20.2 million for FY 2012, were expected to end the year at $21.6 million. Based on recent performance, the projected target for FY 2013 was $22.5 million. Specifically, department store and electronic sales had spearheaded the rise. Because of increased business activity, TOT had risen nicely as well. TOT revenues from July through February of this fiscal year were running nearly 23 percent above those of the same period in the prior year. Accordingly, Staff had raised the FY 2012 target from $8.2 million to $8.7 million, and had set an ambitious goal of $9.6 million for FY 2013. In contrast to other jurisdictions, property taxes remained stable in FY 2012, and were expected to increase by approximately $1 million in FY 2013. Documentary Transfer Taxes had fallen in the current fiscal year compared to FY 2011's stellar performance of $5.2 million. Staff was optimistically forecasting this revenue source to slightly exceed $5.0 million in FY 2013. While some revenues were recovering, other key revenue sources were still below Great Recession levels. Sales and Documentary Transfer Taxes projected for FY 2013 were slightly below actual revenues realized in FY 2008. Other tax revenues, such as property and TOT, had increased since 2008, but TOT together with other revenues were not sufficient to cover projected FY 2013 expenses or projected future expenses forecasted in the City's Long Range Financial Forecast. The concerted effort to reduce expenditures thus far had not been sufficient to erase General Fund funding gaps. The FY 2013 General Fund Proposed Budget was actually $152 million on the expense side, an increase of $5.6 million or nearly 4 percent over the FY 2012 Adopted Budget. The main drivers of this increase were rising benefit costs; the lack of compensation concessions in FY 2012 from the Palo Alto Police Officers Association and the Police Management Association; and, a recommendation by the Finance Committee to include an additional $2.2 million in the annual Budget for the maintenance and upkeep of City infrastructure to prevent future backlogs (the keep-up recommendation from the Infrastructure Blue Ribbon Commission (IBRC)). This Budget proposed reductions in Public Safety spending. As the largest portion of the City's General Fund Budget and an area that had been largely insulated from cuts over the prior three years, this Budget included short-term and long-term proposals for cuts in Public Safety spending with generally minimal impacts on service levels. Successful City negotiations resulted in the elimination of the citywide minimum staffing requirements in the Fire contract. A more flexible operational structure was proposed this year to enhance paramedic services, a service that was in high demand by the community. The Medical Services Utilization Study, completed this year, recommended an increase in the City's paramedic services. To address this recommendation, the proposal was to shift Staff from one fire response vehicle to the City's paramedic operations. Removal of a fire response vehicle from service resulted in $1.1 million of savings, which was offset by a $500,000 increase for paramedic services. The total General Fund expense savings from this shift in Fire staff was $600,000 a year. Based on U.S. Department of Energy cutbacks, the Stanford National Accelerator Laboratory (SLAC) fire station was scheduled for closure in May 2012. This action would result in the elimination of nine fire positions and an expense reduction of $1.4 million, of which 30.3 percent or $422,000 was reimbursed by Stanford. The City was in the process of renegotiating the Stanford fire services contract and, as a result, the final savings to the City from SLAC's closing had not been reconciled. Other important expense reductions in the General Fund included first, redeployment of six police officers, now in traffic operations, to field patrol and holding one police captain position vacant. These redeployed positions would be kept vacant in FY 2013 for a savings of $1.3 million. This freeze was proposed for FY 2013 only at this time, with exploration of alternate shift and programming approaches in the Police Department as part of this recommendation. Secondly, this Budget included a proposal to contract animal services to an outside agency. This would eliminate 13 City positions and potentially result in approximately $500,000 in service operating costs. The loss of Mountain View to another contract resulted in nearly $1 million in net operating costs to the City's General Fund. By contracting this service, the City not only saved money, but also avoided significant capital costs that would be needed to improve the animal services center facility and explore site reuse that could have positive revenue implications for the City. In the Planning Department, the Budget included a proposal to eliminate two positions and freeze another, saving $394,000. In the Library Department, the 2013 Budget included freezing five library positions while the renovation of the Main Library was undertaken, for a savings of $336,000 in FY 2013. Those would ultimately be reestablished. After the budget cycle concluded, Staff would deliver to the Council the findings of a Cost of Service Study that had been performed over the past year. Staff anticipated the Study would demonstrate which services were heavily subsidized by the General Fund. Informed decisions could then be made, for example, about raising fees, eliminating a service, privatizing it, or maintaining the subsidy. This Study would also help the Council, Staff, and the community to prioritize services and establish clear and transparent cost-benefit rationales for services and funding levels. There were new ongoing and one-time costs proposed in this Budget. The former included positions in City Communications and Information Technologies. These positions represented an investment in greater government transparency and innovations that would lead to greater efficiencies. The one-time recommendations included: $800,000 for technology investments in the Development Center Blue Print process to continue improvements in the building and permitting processes; and, a $300,000 loan to the Airport Fund to match the operational expenditures needed to continue the transition plan from the County. He proposed these expenditures be covered by transfers from the Budget Stabilization Reserve, since they were one-time in nature. If the Council agreed with these recommendations the net effect would be a $200,000 positive balance in the General Fund for FY 2013. Before addressing highlights of the Enterprise Fund budgets, he wanted to address the City's major efforts of the past year. As a consequence of the IBRC's work there was clarity in the need to improve, rehabilitate, and replace aging roads, facilities, parks, and the general financial scale of investments the City would need to make. In his 2012 State of the City Address, Mayor Yeh stated that maintaining infrastructure was essential for Palo Alto's continued vibrancy. Quality infrastructure allowed the City to provide a high quality of life for its residents, businesses, and nonprofits and contributed to Palo Alto's attractiveness as a global center of technology and innovation. As stated, the IBRC's keep-up recommendation of an annual funding amount of $2.2 million had been included in this Budget. The Council was engaged in a series of strategic retreats to address the City's catch-up or backlog needs of $41.5 million. There was also a need to replace or build new, necessary facilities such as a Public Safety Building and a Municipal Services Center. Beyond the IBRC recommendations, other important capital decisions could also be on the horizon, including the Regional Water Quality Treatment Plant, how to address the City's compost and organics recycling future, and outcomes from the Cubberley planning process. The Palo Alto Utilities and Public Works Departments were proposing rate changes for water, refuse, wastewater collection, storm drainage, and fiber optics. No increase was planned for electric rates. The cumulative impact of the proposed rate changes would increase the average household residential utility bill by $8.94 or 3.8 percent per month. This included increases resulting from the utility user tax. The Gas Fund rate decrease of 10 percent was prompted by a change in gas procurement strategy. The City of Palo Alto would implement market price-based retail supply rates instead of the prior laddered gas purchasing strategy that spread out gas purchases in increments over time. The new supply rate would be adjusted every month and would be based on the monthly market price. Given the historically low gas prices currently in effect, the gas rate for the average customer would decrease approximately $5.52 per month. The recommended Water Fund rate increase of 15 percent was driven by increases in the wholesale price for water from San Francisco Public Utilities Commission (SFPUC) coupled with lower water usage forecasts. Because most of the Water Utility costs were fixed costs, the water rate for the average residential customer would increase approximately $8.52 per month. The Refuse Fund rate increase for residential customers consisted of changing the current Fixed Residential Monthly Charge to a charge for street sweeping service, as well as adding charges for Annual Cleanup Day and household hazardous waste services. These changes implemented findings from the refuse Cost of Service Study. The total increase would vary slightly depending on the customer's garbage cart size. For the majority of customers who had 32-gallon garbage cart service, the increase would be $4.06 per month. Commercial refuse rates would remain unchanged. The Wastewater Collection Fund rate increase of 5 percent was caused by a need to maintain the financial viability of the Fund. Expected rate increases were forecast for FY 2014 through FY 2017 as well. The Wastewater Collection rate for the average residential customer would increase approximately $1.40 per month. Both the Storm Drainage and Fiber Optics rates were adjusted annually based on the Consumer Price Index (CPI). The Storm Drainage and Fiber Optic fees would increase by 2.9 percent to reflect the annual CPI change. The Storm Drainage rate for the average residential customer would increase approximately $0.33 per month. The Fiber Optic rate increase would impact only customers with fiber optic licenses beginning prior to September 18, 2006. The City was in the process of conducting a Utilities Organizational Study. Best practices in the industry would be used to evaluate current operational and organizational structures within the Utilities Department. The Study would not be completed prior to Council's adoption of the FY 2013 Budget, but potential changes and recommendations would be shared with the Council during FY 2013 and would inform future Budget decisions. The City's largest General Fund tax revenue was property tax, and Proposition 13, passed in 1978 by voters, had created over time an absurdly unfair and unequal tax system. As a result, despite high real estate values, property tax rates were uneven. The City also received less than 10 percent of the property tax paid by the property owner. The City's next largest revenue source, sales tax, was also diverging from the upward direction of the Silicon Valley economy. The movement towards a service economy (no sales tax); internet shopping (less sales tax); and companies' off-shoring of points of sale (no sales tax) put the City at risk and pushed the need for new revenues, rate changes, and governmental fiscal reform for cities at the State level. It had taken a long time to reach this point, and working out of this mess would also take time. The Council's efforts to curb employee compensation and benefit increases had been ongoing and would have to continue. The Cost of Service Study, the Utility Organizational Assessment, and other initiatives were underway. The Council would engage in community and Staff discussions in the years ahead about restructuring services, costs, outsourcing, and determining who paid. Because of the scale and different strategies that must be employed and the different constituencies that must be engaged, the Council's plan for responding to the IBRC's recommendations must unfold gradually and thoughtfully. The Council must also grow new revenues, which mostly would require voter approval and thus, planning, outreach, education, effective communication, right sizing, and right timing. The Council Priorities appendix listed some examples of strategic decisions. The Council was focused on the future and invested in the long-term best interests of the community and its citizens. The Council worked hard, was engaged with its citizens, expected the same of City Staff, and had been willing to make difficult choices. These three factors gave Palo Alto a great advantage. The Council would again move through this budget year thoughtfully, respectfully, and effectively with the right balance of decisions, for the benefit of Palo Alto residents and with an eye on the future.

Lalo Perez, Chief Financial Officer, said on page 11 of the Operating Budget was a discussion of the document layout. The second document was the Capital Budget, which provided any capital work planned for the next five years. Some of the changes to the Budget document were made at the request of the Council. Staff had included a breakdown of the benefit cost allocation by department. On page 125 was the allocation of benefits, the retiree health excess management benefits, and disability. Staff was attempting to provide additional information. A breakdown of positions and changes over time was conveniently located on the previous page. Staff had highlighted a summary of the major changes in each department. Staff would begin the discussion with the Finance Committee on May 8, 2012, and accept feedback on the format and substance. Discussions would begin at the Finance Committee on May 8, 2012, with an overview, Council Appointed Officers, the Library, and Community Services Department; May 10, Planning, Information Technology, Human Resources, Administrative Services Department, and related internal services; May 15, Police and Fire budgets; May 17, Utilities and General Fund Capital Improvement Programs (CIP); May 22, Public Works General Fund and Enterprise Funds; and, May 29, Wrap-up. Staff had included a back-up night on May 24 to have additional discussion on the Budget if needed. After hearings with the Finance Committee concluded, the Budget would return to the City Council on Monday, June 11, 2012 for opening discussions, with adoption scheduled for June 18, 2012. That calendar was provided on page 10 in the Budget document.

Mr. Keene reported a gap of approximately $1 million, because Staff had not included his recommendation to draw the technology CIP and the loan to the

Airport from the Budget Stabilization Reserve. This would result in a net $200,000 on the positive side.

Andrew Boone urged the Council to give a higher priority to pedestrian and bicycle infrastructure projects than in past years. The draft plan indicated approximately $10 million of matching funds along with grants would need to be invested over five to ten years to implement an excellent bicycle and pedestrian network. Approximately 15 percent of Palo Alto residents biked and walked to work; 40-50 percent of public school children walked or biked to school. People wanted safe infrastructure. He urged the Council to consider the possibility of identifying funding sources for local matching funds.

2. Council Retreat No. 3 for Further Discussion of Infrastructure Investment and Renewal. Direction to Staff Regarding Implementation Issues, Funding, and Other Items.

James Keene, City Manager, reported this discussion would provide an opportunity to touch on the topic the public speaker addressed. This was a retreat setting, designed for discussion and free-form conversation. The title of the session had been broadly worded so the Council could have a wide range of discussion related to infrastructure issues and investment. Discussions would allow the Council to determine infrastructure challenges and then strategically arrange them. He hoped the transmittal letter set a context for connecting infrastructure challenges to choices, trade-offs, and revenue streams. It was important to have the Council clearly define catch-up and keep-up; discuss implementation of the Infrastructure Blue Ribbon Commission (IBRC) recommendations; identify, prioritize and fund new projects; and consider both a near-term schedule and a larger strategic schedule that revolved around the election cycle. The IBRC focused on three areas: 1) new projects at a total cost of $210 million, including a Public Safety Building, fire station, the Municipal Services Center (MSC), and Animal Services; 2) catch-up or the backlog of maintenance and investment projects that had accumulated over time; and, 3) the keep-up gap in addition to the existing Operating Budget and Capital Improvements Program (CIP). Beyond the IBRC recommendations, funding would be needed for the Regional Water Quality Control Plant (RWQCP), the Airport, and waste energy capital investments under Measure E. The Council asked Staff to review the potential acquisition of the Post Office. The Cubberley issue, beyond maintenance, could include future infrastructure needs. The Bike and Pedestrian Plan had approximately $35 million in identified costs, if it was fully implemented. The IBRC report attempted to focus the Council in a particular area and to provide a beginning roadmap to solving infrastructure problems. Staff wanted to acknowledge, as the IBRC did, the dynamic nature of these other capital needs of the City. The IBRC report identified $41 million in catch-up needs, and recommended investing over a ten-year period to get on the right track for maintaining facilities and assets. Keep-up annual costs were the amounts spent in both the Operating and Capital Budgets for maintenance. The IBRC report identified a $600,000 gap in the CIP portion and a $1.6 million gap in the operating portion on an annual basis for planning purposes. He had included in the Proposed Budget for Fiscal Year (FY) 2013 the addition of $2.2 million to meet that recommendation. If the Council could retain that $2.2 million in the Budget for the first year, it would set itself on a path to keeping up with the projects that needed to be done. The City had a backlog of $41.5 million to fund over a ten-year period. As far as a backlog of existing assets that needed to be brought up to standard, the City was in better shape and closing that gap seemed to be within reach. The next piece was the new projects, and that was the big cost area. New projects included in the IBRC recommendations were: a new Public Safety Building at a potential cost of $65 million, a Municipal Services Center replacement project with significant cost sharing by the Enterprise Funds, a bike bridge, and other issues. In addition, the Council needed to consider new projects and additional needs, such as the bike plan, Cubberley, and a Regional Water Quality Control Plant. If the Council could add $2.2 million yearly to the Operating Budget on an ongoing basis for keep-up, the City would not perpetuate the decline in existing assets. The problem was funding catch-up of $41 million over ten years to close the gap. The City had a host of needs; some immediate and some of unknown cost. The questions were how to prioritize and fund these projects. He asked the Council to think about the interrelationship between achieving the keep-up recommendation of $2.2 million and fixing the catch-up piece of $41 million.

Joe Saccio, Assistant Director Administrative Services, stated the handout was a primer on revenues, taxes, and commonly used debt instruments. The Transient Occupancy Tax (TOT) was last increased in 2007, and the current rate was 12 percent. Staff projected an $8.7 million revenue stream for the current fiscal year. A one percent increase in the tax could raise revenue by $723,000, not considering economic influences or competition. San Francisco had a rate of 14 percent, and most communities were in the 10 percent range. Taxes were one way to fund catch-up, and could also be used for some of the debt instruments. The last increase in the Utility Users Tax was in 1987, when it was increased to 5 percent. A general election was required to increase the rate. Staff projected $10.7 million in revenue in the current year. San Francisco had a very high Utility Users Tax Utility Users Tax, but only on commercial entities; San Jose and Redwood City were at 5 percent. Some surrounding jurisdictions were at 3 percent or below. The Documentary Transfer Tax rate was $3.30 per $1,000 of assessed value for the City and $1.10 for the County, for a total of $4.40 per $1,000 of assessed value. The tax was generally shared 50/50 between the purchaser and seller in Palo Alto. A $1 increase in the rate would increase revenue by $1.4 million, and a $2 increase would generate approximately $3 million.

Berkeley and Oakland had rates of $16; San Francisco's rate was even higher with a tiered structure. All local jurisdictions throughout the State received 1 percent sales tax, and each jurisdiction within a county could increase the sales tax rate to a maximum of 2 percent. Barring increases from the Valley Transportation Authority (VTA) and the County, the City could increase the sales tax rate to 2 percent. A 1/8 percent increase would result in a revenue increase of $2.7 million; a 1/4 percent increase would provide $5.4 million. San Francisco was the exception to having 1 percent, at 1 1/4 percent. Palo Alto did not have a parcel tax, but the Palo Alto Unified School District (PAUSD) did. Typically, a parcel tax was increased for a particular purpose. An increase had to be approved by a two-thirds vote, and could be placed on the ballot during any election. With approximately 20,000 parcels in Palo Alto, a $25 parcel tax would generate $500,000 in revenue; a $50 increase would generate $1 million. Palo Alto was one of the few cities that did not have a Business License Tax. A general election and majority vote would be required to pass a Business License Tax. Staff projected the City could raise between $3 million and $5 million with a Business License Tax. Usually, the tax was tailored for a certain revenue level. The Council had used Certificates of Participation (COP) many times for improvements. COPs did not require a vote, but did rely on either new revenue streams or a reallocation of resources to pay the debt service. As a rule of thumb, $1 million in debt service could generate $10-$12 million in project funds over a 30-year term. COPs tended to have slightly higher interest rates than General Obligation (GO) bonds, and thus provided a lower yield. The City would need a $50 parcel tax, for example, to raise $1 million to pay a COP of around $10-$12 million. A sales tax increase could generate much more than that, if needed. GO bonds required a two-thirds voter approval. The City had implemented a parcel tax of $15.51 per $100,000 in assessed value to pay the debt service on the $55.3 million bond for the Library, Mitchell Park Community Center and Library, and Downtown. For a $500,000 home in assessed value, the cost to the homeowner was approximately $78. Funding for utility revenue bonds came from utility rates, whether gas, water, or electric. These were dependent on the interest rates at the time.

Mr. Keene noted the handout had a summary of election requirements. Other than a GO bond election, all the other voter approval decision points were at a general election, either November 2012 or November 2014. In the timing of the 2012 election schedule, the Council had only May and June to perform any background work. July 16 was the deadline for an ordinance calling an election, which was a short period of time for community outreach, education and campaign. For a general election in 2014, the Council would need to prioritize infrastructure projects during the second half of 2012, determine the feasibility of financing measures and a communication plan in 2013, and develop formal recommendations and a campaign in 2014. Staff wanted to place IBRC recommendations in the context of additional, larger infrastructure drivers; to link them to revenue issues and options; and to tie them to a schedule. Staff hoped the outcome would be definitions, funding, new projects, and scheduling.

Mayor Yeh suggested the Council work through the definitions of catch-up and keep-up, determine new projects, and find methods to move forward in these areas.

Council Member Holman noted the IBRC did not look at the dollars associated with estimated projects. She asked if the estimates were accurate or not.

Mr. Keene stated the IBRC did not attempt an engineering analysis.

Council Member Holman inquired if there was a broad evaluation of project costs.

Steve Emslie, Deputy City Manager, answered yes. The IBRC recognized it did not have the expertise to detail costs. For the most part, the numbers were generated by Staff and engineers who prepared infrastructure and CIP programs. If the Council moved forward with these projects, it would have the opportunity to review the projects critically.

Mr. Keene indicated some projects would be higher than the estimates, others lower. The Council's decisions would be tempered by the reality of what the City could afford. The IBRC provided a starting point for the Council's conversations.

Council Member Holman asked whether Staff had performed a practical analysis of how many projects the City could manage in a set period of time.

Mr. Keene stated that was another factor to implementation issues. The IBRC recommendation was a $4.2 million investment over a ten-year period for catch-up. If the Council wanted to shorten that ten-year period, then Staff would have to test that against its ability to deliver.

Council Member Holman believed the question was not only dollars, but also manpower. The Documentary Transfer Tax was based on a $1.2 million home valuation. She asked whether the median home sale price was $1.2 million.

Mr. Saccio reported the average assessed value in Palo Alto was $574,000, which was very different from the sale price of a home. Staff chose the $1.2 million figure serendipitously.

Mr. Keene felt $1.2 million was on the low end of the median home sale price. Staff had not factored in commercial real estate sales, which could be significantly more. When a property was sold, it was reassessed at the market value and the Documentary Transfer Tax was paid on that value.

Council Member Holman suggested the average and mean sale prices in Palo Alto were critical to informed decisions, because that would indicate the amount of revenue generated by a tax increase. She asked if the City had issued COPs twice in the past.

Mr. Saccio answered yes.

Council Member Holman inquired what the experience had been with COPs in 1992 and 1998 in terms of having increased revenues to cover the load.

Mr. Saccio reported the 1998 COP was for the golf course, and revenue streams from the golf course were meant to pay the debt service. If the economy faltered and golf course revenues decreased, the General Fund would have to supplement the revenue stream. Revenues from the golf course had covered debt service. The COP in 2002 was for Civic Center improvements. He did not recall a new revenue stream to pay for that. If the Council chose to issue COPs, it would need to either reallocate resources to pay the debt service or determine a new revenue stream.

Council Member Holman did not consider increasing sales tax as a solution. She asked for an update on the challenge to the Utility Users Tax, and whether that would influence the amount of revenue.

Molly Stump, City Attorney, reported Staff had advised the Council about those types of legal risks. There was active litigation related to the Utility Users Tax. She could update the Council confidentially in the next few days.

Council Member Holman noted the potential Post Office acquisition was outside of new projects. She asked if Staff had evaluated a potential cost savings in moving Staff from rented office space to the Post Office.

Mr. Emslie reported Staff had not identified an end user and was concentrating on obtaining essential information to make a credible offer. Moving Staff from rented facilities would greatly offset some expenses and could eventually pay for the building. Otherwise, it was premature to analyze savings.

Council Member Price asked if the numbers for catch-up assumed inflation costs over ten years.

Mr. Perez stated there was no inflation factor in the numbers. They were kept constant for the purpose of calculations. Inflation would have to be considered if the Council moved forward on projects. Before the Great Recession, there were significant construction cost increases. The IBRC discussed including an inflation factor, but preferred to keep the calculations simple by not including it.

Council Member Price asked if that also applied to keep-up.

Mr. Perez replied yes.

Council Member Price commented the Council did not have a lot of choices with regard to keep-up and catch-up. At a certain point, the City would not be able to keep the various entities functioning.

Mr. Perez agreed with Council Member Price in general. The Council needed to catch-up and keep-up infrastructure in order to have it right-sized and to maintain that level. The Council would need to prioritize projects and decide if the City had the capacity for these projects with existing Staff.

Council Member Price inquired whether the new project estimates were capital costs.

Mike Sartor, Public Works Director, reported those were capital costs including design and construction.

Council Member Price asked if those estimates were in 2011-2012 dollars.

Mr. Sartor answered yes.

Council Member Price inquired if the concept of tiered rates could be applied to other categories of taxes.

Mr. Saccio indicated the Business License Tax could have tiers depending on how it was structured.

Mr. Perez stated Utility Users Tax had a threshold where the tax decreased depending on consumption. Staff could review that aspect.

Council Member Price asked if the concept of indexing was also a possibility in some cases.

Mr. Saccio indicated an index could be applied to some areas.

Council Member Price said she supported facilities related to Public Safety and health and safety of the community. The others were also important, but the two Fire Stations and the Public Safety Building were extremely important in terms of providing important services to the community.

Vice Mayor Scharff remarked that providing $2.2 million yearly for keep-up would be the foundation for asking the voters to approve new revenues or bond issues for other issues. He felt Cubberley was in a different category from fixing sidewalks and parks and updating buildings.

Mr. Emslie agreed Cubberley could be reclassified as a new project.

Vice Mayor Scharff felt Charleston/Arastradero was also a new project for which there was not funding yet.

Mr. Emslie reported the Charleston/Arastradero project was landscaping and median improvements. It could be viewed independent of the traffic calming effects, and could be reclassified as a new project.

Vice Mayor Scharff suggested those two projects and Bixby Park should be placed in the category of new projects. He asked if there was funding for completion of Bixby Park.

Mr. Emslie stated there was not funding for Bixby Park, but it was included in new projects.

Vice Mayor Scharff stated moving Cubberley and Charleston/Arastradero to new projects left $28 million in catch-up projects. That amount was not too daunting. The Council needed analysis and thought to determine the priority of new projects, and had to consider a ballot measure in 2014 for new projects. The only proposal he would consider for a 2012 ballot measure was catch-up. He suggested the Council focus on increasing the TOT.

Council Member Shepherd asked if the $2.2 million for keep-up in the FY 2013 Budget had been offset by one-time hiring freezes in both Police and Library.

Mr. Keene indicated that was an appropriate way to look at it.

Council Member Shepherd preferred having a plan for incremental changes. She asked what other changes would be proposed.

Mr. Keene noted the Council's focus had been to make structural adjustments when possible. It would be a question of pacing spending and income. Because of the trajectory of expenses, the next three years would be challenging years.

Council Member Shepherd indicated the $2.2 million would come back to the Council in FY 2014 unless the Council made structural changes in the existing Budget. The City was in a vulnerable situation of supporting legacy pieces. She wanted to discuss the difficult questions in order to make incremental changes.

Mr. Perez stated the Cost of Service Study would begin the conversation. The Council would have to engage the community to make some of these choices. For the most part, changing the methodology of service delivery had been a good experience. The Council needed to review every service the City provided, how it was provided, and then make choices about outsourcing services.

Council Member Shepherd felt keep-up was vulnerable, unless it was secured with a plan. The Council would know more about Cubberley when that process moved forward as to whether or not the $6.9 million for capital improvements would be a City or PAUSD expense. The City needed an infrastructure budget for catch-up of $5 million for ten years. She asked if Staff was suggesting a new revenue source for this.

Mr. Keene reported a larger capital need would require a new revenue source. A $2-$3 million a year need could be funded through a new revenue source or found within the City Budget. The viable option was to consider a new revenue source.

Council Member Shepherd suggested putting the $2.8 million into the Budget, so that the Council could consider that challenge. Impact fees for building a home from the ground up totaled approximately $27,000. She asked for an explanation of those fees.

Mr. Emslie indicated the permit issuance cost was required by law for cost recovery, while impact fees were set by the Council. The City had a housing fee, a library fee, a community center fee, and a parks and recreation fee. All those fees applied to rebuilding a home. All impact fees were a fraction of the total cost, but could be significant. Also the Utilities Department charged a hook-up fee which was an impact fee.

Council Member Shepherd inquired if there was a method to analyze that and determine recovery of document transfer fees. She asked if the document transfer fee was paid by the purchaser or the seller.

Mr. Perez stated it was typically split 50/50 but negotiable.

Council Member Shepherd wanted to clearly define catch-up needs, so that the Council could determine which tax to increase. She inquired if Staff had the time to invest in polling and a campaign.

Mr. Emslie reported there was not enough time to perform the proper groundwork for a November 2012 ballot measure.

Council Member Shepherd asked if the City could have a Utility Users Tax for either businesses or residences.

Mr. Perez stated Staff would have to review that, because he was unsure of the implications.

Council Member Shepherd inquired if Staff had communicated with stakeholders at the Chamber of Commerce level and the business level regarding possibilities for increasing revenue. She felt a tax elevated the way the government worked and the way services were delivered. The IBRC report indicated the services in which the City was deficient.

Council Member Burt asked if the surface category excluded the increase for street maintenance and replacement begun two years ago.

Mr. Sartor reported the surface category did not include the annual maintenance program. The surface category for catch-up included about $3.7 million in sidewalk repairs, medians and other surface amenities.

Council Member Burt inquired whether the ten-year program eliminated the deficit in funding for keep-up and catch-up of streets.

Mr. Sartor answered yes.

Council Member Burt reported libraries would fall under catch-up, keep-up, and new projects, but they would come off those lists as the libraries came online. Streets would fall under catch-up and keep-up, but that had been funded over a ten-year period and would be accomplished. The presentation should include that. Those two projects did not belong in the same category as going forward problems, but Staff should acknowledge them. If the PAUSD took back a major portion of Cubberley lands, then the City probably would not spend these dollars under catch-up for Cubberley. Instead, the City would have to spend more dollars for major or new projects that were either at the Cubberley site or for functions being provided at the Cubberley site. The presentation should note that. The category "new projects" implied to the community that these were new things that the Council wanted to add. Most of them were not new. If the MSC were repaired piecemeal, it would be keep-up and catch-up. Instead, Staff had chosen to designate it as one project and placed it under "new projects." That term was misleading, and these projects should be categorized in ways the public understood. He asked what triggered an impact fee.

Mr. Emslie stated they primarily applied to a new structure. If more square footage were added, the school fee would apply.

Council Member Burt noted the RWQCP was used by four cities. He inquired if it was also an Enterprise Fund.

Mr. Keene answered yes.

Council Member Burt stated other than the Utility portion of the MSC; the list did not contain Enterprise Funds. Projects were primarily General Fund obligations.

Mr. Keene indicated the MSC was a blend.

Council Member Burt suggested it should be identified that way, so everyone understood it was split among a number of cities and it was an Enterprise Fund. He assumed the dollars would come from sewer fees. He noted the bike bridge was listed for $10 million, and asked if the City would pay the full $10 million or apply for grants.

Mr. Keene stated that was the figure the IBRC used to identify the scope of the project.

Council Member Burt stated the number should be the anticipated amount of the City's share of costs. If the City had to pay $10 million, he would not support the project because the City had higher priorities.

Mr. Keene reported that was the known funding potential for this particular project. Other projects could have creative solutions where the Council could earmark funding.

Council Member Burt suggested that should be noted and discounted accordingly. The amount listed should be the discounted amount and not the full amount. He noted the Charleston/Arastradero project was a catch-up project which did belong here. There was a convergence between what the Council could successfully ask from the voters and the highest priorities. He leaned toward identifying the Public Safety Building as a high priority, and suggested having the revenue measure on the ballot along with the advisory measure. The City Attorney had clarified that was commonly done, and it set a policy obligation that the Council would use the funds for that purpose. He asked if that was a fair and permissible characterization.

Ms. Stump stated it was a fair characterization for the discussion.

Council Member Burt asked the Chief of Public Safety to present his adjusted needs assessment at the next Study Session, because he wanted to focus on that. Infrastructure needs had been building over 30 years, and the Council was reviewing an aggressive plan to solve it all in ten years. If the Council looked at what was doable, then it would continue to make progress. It probably was not feasible to consider one large revenue stream to fund all projects at one time. The electorate would not be willing to do that. He asked Staff for an estimate of the difference in liabilities and expenses if the City had not reformed employee compensation, pension and benefits over the past three years.

Mr. Perez reported the number would range between $3 million and $6 million for the General Fund alone, not including changes for the second tier. Those were instrumental for the restructuring of finances.

Council Member Burt stated that was the near-term impact, and the long-term impacts of pension and retiree medical costs were millions of dollars.

Mr. Keene reported the difference was $5-$6 million in direct costs on an annual basis.

Council Member Burt noted the City was negotiating with different employee groups to implement this plan. The Council was in the process of demonstrating to the electorate aggressive near-term and long-term reforms on pensions, benefits and efficiency. The Council would have to couple that story with any discussion of revenue.

Mr. Perez noted compensation changes did not include the 60 positions that were eliminated.

Council Member Burt suggested Staff provide the impacts of pension and benefit reforms 10 or 20 years in the future. The Council needed to share that clearly with voters when asking for revenue streams.

Council Member Schmid indicated the IBRC provided pathways to deal with these long-term, outstanding issues. It was good to show in the FY 2013 Budget that the Council was trying to deal with keep-up and hopefully catch-up. He was concerned that the Council was under pressure by the Association of Bay Area Governments to plan for a substantially increased population in Palo Alto. At the same time, there was potential rail corridor development of north/south routes through the City. The Gateway Project, which was the ideal situation to grapple with housing issues, finished with no houses. That implied that housing would end up in places where infrastructure would be needed to deal with issues. It was important for the infrastructure blueprint to identify the potential needs of a proliferation of housing in different parts of the City. He agreed with the comments on Cubberley. New projects were larger in scale, and asked for a longer-term investment in infrastructure. The only two exceptions might be the Fire

Station and the Post Office. He understood both of them had the potential to generate some operational savings that could help fund those two projects. The other new projects would be a long-term capital investment. PAUSD had done well with bundling their capital needs, and going to the public at one time. One vote would provide a resolution of the major pieces of infrastructure issues. That would be a good discussion for the Council, and the ideal time would be the week after the Council had their first session in the new Mitchell Park Community Center. The FY 2012 Budget needed some reconciliation to determine if the City would need to draw on Reserve Funds. The FY 2013 Budget would freeze positions in Public Safety and Library, reduce services in Community Services, and use Budget Stabilization Reserve funds. It was essential to have a clear articulation of how the Council would deal with long-term structural issues if the Council considered a ballot measure in 2012.

Council Member Espinosa asked Staff why they considered a ballot measure in 2012 to be unfeasible.

Mr. Emslie reported there would not be adequate time to perform the research to understand voter sensitivity and to engage stakeholders, and a lack of preparation could set back future efforts.

Council Member Espinosa asked what the research process was to determine which of these projects resonated with voters and an acceptable dollar amount.

Mr. Emslie recalled the research on the Library bond measureswhere various scenarios were tested at different levels, and Staff received direct input through professional polling data that indicated which scenarios were most likely to succeed. There was always uncertainty in any research, but the information pointed Staff in the right direction. Staff needed to know where there was lack of understanding. Election experts stated results would be influenced by a well-managed information campaign. It would be important to ensure maximum effect for a project that was not readily identifiable as a community asset.

Council Member Espinosa inquired about a timeline to obtain that information.

Mr. Keene reported 2014 was the right schedule for a majority, if not all, of the measures that the Council would have. The prelude piece would be prioritizing projects, and that would have to be interactive with the public. Often focus groups were needed as well as polling. In the next six months, the Council could determine the scope of projects, and in 2013 test that with the public. The Council's actions over the last three years needed to be better known and understood by the public as a whole. Continually articulating that was not part of a ballot campaign, but an information campaign. That left 2014 for the Council to refine and test the measures. One topic not discussed was other measures from the State and other jurisdictions. The larger the measure, the greater the risk and the more time the Council needed.

Council Member Espinosa noted the majority of feedback on Palo Alto Online was not a penny until the Council reformed compensation and benefits. He felt that would be part of a dialog during any campaign. He suggested the category new projects be named longer-term projects.

Mayor Yeh liked the timeframe for catch-up and new projects. Catch-up implied a certain level of prioritization. He could not imagine not addressing a Public Safety Building within the next ten years. From that perspective, the terminology needed to be clear about prioritization. Catch-up would incorporate some of the projects currently listed under new projects. He was interested in the MSC and some of the vehicles and operations there as being necessary for an emergency preparedness response. He hoped the June presentation would include the consultant's comments regarding the MSC and emergency response. That would give the Council time to make strategic decisions for the long-term. If the primary definition of catch-up was the timing for infrastructure, then the Council had to make a decision on Cubberley in some fashion within the next ten years. Cubberley would remain within catch-up, while recognizing there was a separate process. There was not a similar ten-year pressure for the Charleston/Arastradero corridor in terms of finalizing the medians and striping. The biggest impact was the adjustment of traffic flow. New projects should be renamed as longer term infrastructure needs. The Council added $2.2 million for keep-up, but did not necessarily identify a new revenue source. The City did not have an ongoing means of addressing the $2.2 million amount. He wanted to know what other cities had done in terms of issuance of GO Bond debt. Palo Alto had a long history of preserving its bonding capacity. The Council would ask the public for a GO bond only when it was truly needed. This would provide voters with the context of the Council's discipline in the past. He felt the Airport Fund and compost facility were appropriate for the Enterprise Funds. For potential revenue sources, he felt it would be difficult to do anything on this November's ballot.

Herb Borock stated in terms of developing the remainder of Bixby Park in accordance with the Baylands Master Plan and in current dollars, the $3.6 million amount seemed to be low. In regard to the Utility Users Tax, the larger users did not pay their fair share of the tax. Those that used 30 percent of electricity paid approximately 20 percent of electric revenue. He did not believe people paying 5 percent now would want to increase their rate, when others were paying less than 5 percent. In regard to convincing the voters and telling the story of reforms, he asked if residents should vote in favor of a police building when the City now had less police officers. In terms of whether the Council should be talking about near term or long term, he asked the Council to remember the term limits and how many years they would serve. They would be discussing the near term.

Council Member Holman concurred with comments regarding identification of projects as new projects. For the Council to make informed decisions regarding prioritization, other pieces of information were needed. The current election cycle was too short to educate voters. The Council needed an updated Public Safety Building proposal. The Council needed to know the possible scenarios regarding Cubberley. She agreed with comments about projects funded by City and grant dollars, partner projects, and Enterprise Fund projects. Projections for TOT revenue did not include two new hotels. She asked for an analysis of Post Office costs versus savings. The Council wanted an MSC budget, because the $93 million amount seemed exceedingly high. She requested a new report of the incremental change in the Documentary Transfer Tax using either average or median sales price. To the extent it was reasonable and feasible, she asked Staff to provide in context the possibilities for labor reform costs versus savings moving forward. Near-term and long-term terminology could be a good way to view the three-year, five-year, and ten-year scenarios.

Mayor Yeh asked how the Council's input would be incorporated for the final Retreat.

Mr. Keene stated many angles and perspectives had surfaced on this framework for Staff to incorporate. As it related to the next Retreat, Staff had directives from the prior and current Retreats. If the Council wanted a ballot measure in 2012, the sooner Staff knew that the better. Even though the Council had one more infrastructure retreat that would not be the last meeting on the issue. The Council's leadership role and vision would be checked and modified by polling. Aligning near-term and long-term projects would provide a better sense of perspective, and allow the Council to give more specific assignments.

Mayor Yeh said the Council should reflect on categorization of projects to ensure it could reach a consensus at the end of the next and last Retreat and make a decision about a ballot in 2012.

Mr. Keene indicated Staff would perform a small amount of follow-up research. To the extent the Council pushed projects into the possible or probable but not necessary areas, and then the scope of discussion would come into clearer focus. At that point, Staff could perform meaningful research. If Council could reach that sort of conversation, then Staff could perform the research efficiently to meet the Council's schedule.

Council Member Shepherd noted a period of time before the June meeting where the Finance Committee could be helpful in identifying cuts. She asked if that could be part of the process or if she needed to supply a Motion.

Mr. Keene suggested a Motion was not necessary, because the Finance Committee discussion should unfold naturally.

Council Member Shepherd noted the proposal to freeze certain Staff positions.

Mr. Keene did not see the Public Safety freeze as a one-year issue. On the other hand, if the Council viewed it as a permanent freeze, it would have a different reaction. Any departure from the status quo made it almost impossible to see alternatives. The Council was not finished with finding cost savings.

Council Member Shepherd stated super majority votes were difficult to obtain. A major infrastructure build should go out for a bond measure, because that was the appropriate method for funding it.

Council Member Price inquired if Staff would provide a clarification of comments made, further refinement of definitions, and recommendations regarding phasing of the one-time options on the list. She needed context and understanding of the Charleston/Arastradero project. A GO bond made sense for a project as significant as the Public Safety Building. She had a bias towards TOT and Documentary Transfer Tax, because most of that burden fell on people moving into the community. She asked if the Berkeley Documentary Transfer Tax increase occurred during the City Manager's administration there.

Mr. Keene indicated that occurred before his administration.

Council Member Price asked how much the Council could achieve at the June Retreat.

Mr. Keene indicated the Council would have to determine if it wanted to pursue any measure in November 2012. The Council would then need to plan the future relating to 2014, even if there was a special election for a bond issue prior to November 2014. Hopefully Staff could present information on the Public Safety Building and refine the next steps. It was fairly easy to consider keep-up, and prevent it from falling back into the backlog. While it was a challenge, catch-up totaled approximately $40 million, and there were ways to fund that. The Council needed a sense of which projects were necessary and how large a package could be handled. Ultimately, the question was strategy for the next few years. Not every problem had to be solved simultaneously.

Council Member Price asked when the Council would receive the Cost of Service Study.

Mr. Perez expected Staff would receive the first draft in two weeks. Staff would need to review that, create an understandable format, and determine how to present it.

Council Member Price inquired if the Cost of Service Study was on a parallel path and not related to the Proposed Budget.

Mr. Perez understood the urgency to move it forward, and it was a high priority.

Council Member Burt recalled the City had extensive polling around the Public Safety Building and the Library three or four years ago. Unfortunately, the Public Safety Building proved to be a difficult sale for a super majority vote. He suggested Staff provide that data to the Council.

Council Member Price assumed the current discussions would include a note that past Public Safety Building scenarios included three-part funding.

Council Member Holman felt the information requested would help the Council prioritize projects.

ADJOURNMENT: The meeting was adjourned at 8:45 P.M.