CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Debra Figone

SUBJECT: **RECOMMENDATIONS ON LABOR NEGOTIATIONS DIRECTION**

DATE: November 10, 2010

SUPPLEMENTAL

REASON FOR SUPPLEMENTAL

On November 9, 2010, the Annual Summary of Labor Negotiations Memorandum was issued, along with several other important budget planning documents for the November 18th Special Council Meeting. The purpose of this supplemental memo is to provide the City Council with recommendations for direction in labor negotiations, as well as to identify guiding principles for those negotiations.

There is continuing interest in transparency in labor negotiations, particularly given that personnel costs are the City's primary expenditure. The following recommendations are being provided as part of the continuing effort to provide more public information regarding labor negotiations and to provide an opportunity for the public to provide input before negotiations begin. In addition, the recommendations are being provided to ensure that the direction staff receives is clear, while still providing the space for the exchange of ideas and proposals through the negotiation process between the City's designated representatives and the designated representatives for each bargaining unit representing City employees.

For more information about the upcoming labor negotiations and the negotiation process, please refer to the recent labor negotiations memo which can be found at http://www.sanjoseca.gov/clerk/Agenda/20101118/20101118_0303a1.pdf.

RECOMMENDATION

Accept staff recommendations for direction in labor negotiations.

OUTCOME

This report will provide the City Council with recommendations for direction in labor negotiations in advance of the commencement of negotiations for Fiscal Year 2011-2012.

INTRODUCTION

As outlined in the memorandum titled "2011- 2012 Preliminary General Fund Forecast," the General Fund Preliminary Forecast shows a projected shortfall of almost $70 million next year as revenue collections not only continue to lose ground, but are insufficient to keep up with the projected growth in expenditures. While this forecast is very preliminary and will be updated over the next several months, the overall budget outlook remains dismal and significant budget balancing actions will once again be required in 2011-2012.

As part of this early engagement with the City Council to address the $70 million shortfall, the potential major strategies for solving this shortfall continue to be:

I. Reduction in employee total compensation costs
II. Transition to alternative service delivery models
III. Reduction or elimination of services to our community

It is anticipated that potential revenue strategies will contribute only minimally to addressing the shortfall.

Wages and benefits for City employees are the outcome of the labor negotiation process. There are also potential service delivery model changes that may be subject to negotiations with our bargaining units. A full discussion of recommendations which are subject to the labor negotiation process can be found in the Analysis section of this memorandum as well as in the memorandum titled "Annual Summary of Labor Negotiations." Additionally, the memorandum titled "Potential Strategies to Address the 2011-2012 General Fund Shortfall and Beyond: Organizational and Service Restructuring" identifies alternative service delivery candidates that the Administration is preliminarily evaluating in accordance with Council Policy 0-41.

Any service reductions to be included in addressing the shortfall will be in addition to the reduction of services funded only for 2010-2011 and scheduled to be eliminated effective July 1, 2011. These service reductions, which are highlighted in the memorandum titled "2011- 2012 Preliminary General Fund Forecast," will result in the elimination of 220 positions.

As you know, per the City Charter, I am required to submit a balanced 2011-2012 Proposed Budget to the City Council early May 2011. Absent any savings in total compensation costs, I will have to rely heavily on service reductions and/or eliminations to close the $70 million shortfall. In preparation for the development of the proposed budget, I plan to issue budget reduction targets for public safety and non-public safety departments soon. Currently, in order to close the preliminary General Fund shortfall, targets for non-public safety departments may range between 12% to 28% and for public safety departments between 5% and 12%. Since

public safety departments comprise the greater part of the 2011-2012 General Fund Base Budget, a lower target for public safety departments requires a significantly higher target for non-public-safety departments in order to close the budget gap. Similarly, since the average cost of a public safety employee is significantly higher than the average cost of a non-public safety employee, a lower public safety department target will result in less public safety positions being eliminated necessitating an increased reduction in non-public safety positions. Therefore, it is expected, if the budget shortfall is only addressed through service reductions and/or eliminations, the 2011-2012 Proposed Budget will include General Fund position reductions ranging between 400 and 500 positions.

Since next year's projected budget shortfall is so daunting, I am also contemplating initiating action in the current fiscal year to get a head start on solving next year's budget shortfall as part of the 2010-2011 Mid-Year Budget Review. Any savings which can be generated through budget reduction actions in February 2011 will save at least four months of costs and therefore help solve the $70 million preliminary shortfall.

The stark reality of addressing what, at this time, looks like a $70 million General Fund shortfall after closing last year's $118 million gap is truly overwhelming. Our employees are still reeling from many difficult transitions. Despite the excellent commitment and professional service from our workforce, given public sentiment, our employees wonder if they are valued.

Knowing that these feelings and emotions are in the background, it is difficult for me to make the following recommendations regarding continuing to pursue total compensation reductions as a way to avoid or limit service reductions or eliminations to the Community in 2011-2012. Given the persistence of the structural deficit, I see no choice but to do so. My recommendations are not a reflection of the value and quality of our workforce. They are a reflection of the limited choices available to get this City on stable financial ground.

ANALYSIS

Total Compensation Reduction

On March 23, 2010, the City Council directed the City Manager to achieve a 10% reduction in total compensation (5% ongoing and 5% one-time) for Fiscal Year 2010-2011. Total compensation is the total budgeted cost to the City of pay and benefits. For example, if the cost of pay and benefits for a job is $100,000, a 10% reduction in total compensation would reduce the total cost to the City of that position to $90,000.

During last year's labor negotiations, the concessions achieved reduced the amount of service reductions and layoffs that would otherwise have been necessary to solve a $118.5 million budget deficit for Fiscal Year 2010-2011. For the approximately 1,800 employees and officials who received a 10% reduction in total compensation, half of that amount is one-time. This means that if no changes are made through the labor negotiations process, the total compensation for these employees will **increase** by 5% in July 2011, in addition to any other increases in the

cost of benefits. Jobs and services that are funded by those one-time savings are not funded beyond June 2011.

For employees represented by the San Jose Police Officers' Association (SJPOA), the agreement reached achieved a 3.82% total compensation reduction that avoided the layoff of 70 police officers. Although the agreement was significant in that it avoided layoffs of police officers, the City considered it a "stop-gap" measure to give time to negotiate long term solutions with the SJPOA. Of the 3.82% reduction in total compensation made by the police officers, all but 0.67% is one-time.

For employees represented by the San Jose Fire Fighters, their contract has been expired since June 30, 2009. No agreement has been reached on any concessions for San Jose Fire Fighters. Eligible firefighters continue to receive automatic 5% "step" wage increases.

The following is a chart of the progress in achieving the City Council's direction of a 10% reduction in total compensation.

Progress of Achieving 10% Total Compensation Reduction				
Employee Unit	**Fiscal Year 2010-2011 Total Compensation Changes**			
	Ongoing	**One-Time**	**Total**	**Step/Performance Increases[1]**
Unit 99/Unit 82	**-5%**	**-5%**	**-10%**	No
AEA	**-5%**	**-5%**	**-10%**	No
ALP	**-5%**	**-5%**	**-10%**	No
AMSP	**-5%**	**-5%**	**-10%**	No
CAMP	**-5%**	**-5%**	**-10%**	No
IBEW	**-5%**	**-5%**	**-10%**	Yes
OE#3	**-5%**	**-5%**	**-10%**	Yes
ABMEI[2]	**-5%**	**0%**	**-5%**	No
POA	**-0.67%**	**-3.15%**	**-3.82%**	Yes
IAFF, Local 230[3]	**TBD**	**TBD**	**TBD**	Yes
MEF[4]	**+2%**	**0%**	**+2%**	Yes
CEO[5]	**+2%**	**0%**	**+2%**	Yes

Given the magnitude of the projected budget shortfall for the next fiscal year, it is recommended that the City Council continue this direction from last year with the modification that the entire 10% be an ongoing reduction in total compensation. This should include the healthcare changes recommended by the City Auditor and approved by the City Council in August 2009.

[1] Information reflects eligibility for step/performance increases for FY 10-11 only.
[2] Council approved terms of 5% ongoing total compensation reduction in April 2010.
[3] No agreement has been reached with the San Jose Firefighters.
[4] MEF has received a 2% general wage increase per their current contract, which extends through FY 10-11.
[5] CEO has received a 2% general wage increase per their current contract, which extends through FY 10-11.

This means that staff would be directed to achieve the following for Fiscal Year 2011-2012 resulting in projected savings totaling over $52 million for all employees in the General Fund[6]:

AEA, ALP, AMSP, CAMP, IBEW & OE#3: An additional 5% ongoing total compensation reduction upon expiration of the 5% one-time total compensation reduction for Fiscal Year 2010-2011

ABMEI: An additional 5% in an ongoing total compensation reduction

POA: Achieve an additional 9.33% in an ongoing total compensation reduction, upon expiration of the 3.15% one-time total compensation reduction for Fiscal Year 2010-2011

MEF & CEO: Achieve a 10% ongoing total compensation reduction in addition to rolling back the 2% general wage increase received this year

IAFF, Local 230: Achieve a 10% ongoing total compensation reduction

Additional Recommended Reforms

In addition to the 10% ongoing total compensation reduction, it is recommended that the City Council also direct the City Manager to achieve reforms in the following areas:

Retirement Reform

True and meaningful retirement reform is critical to ensure the sustainability and availability of retirement benefits and City services. Retirement reform should include, but not be limited to:

- 2nd Tier pension and retiree healthcare benefits for new hires
- Options for current employees
- Supplemental Retiree Benefit Reserve (SRBR) or "13th Check"
- Workers' Compensation Offset in the Police and Fire Retirement Plan

Retirement reform discussions should also include cost/risk sharing between the City and employees.

Sick Leave Payout Reform

Sick leave benefits are generally provided by employers as a benefit for employees when they cannot work due to illness or injury. For many years, the City has had a "sick leave payout" benefit in which the City pays cash to an eligible employee for a certain amount of unused sick leave hours when they leave City service.

The City's cost for sick leave payouts have more than doubled in the last four years to an estimated **$14.6 million** for the current fiscal year. The most expensive payouts are for Police

[6] These savings are not adjusted for potential loss in overhead and other reimbursements to the General Fund.

and Fire employees who can receive payment for 100% of unused accrued sick leave hours with no limit. Savings from changes to this benefit are dependent upon the extent of the changes. For example, if changes are made only to new employees, the City would experience no savings from the change for many years. Changes for current employees could result in significant savings depending on the specific changes made.

Consideration of changes to this benefit cause very strong reactions among employees, as it did during last year's negotiations. However, this benefit is more generous than other public or private employers, and the current cost of the sick leave payout benefit is much more expensive to the City than when it was originally put into place. Some employees consider this benefit to be "vested" and not subject to change. The City has asserted that this program can be modified through the negotiations process.

Despite the reaction among City employees to the possible change in this benefit, the current $14.6 million cost to the City cannot be ignored, particularly in light of the service level reductions to our community that could be avoided by reducing or eliminating this expense.

Compensation Structure Reform

At present, the City utilizes a traditional public sector salary schedule with five, 5% salary steps for most non-management job classifications that occur automatically unless action is taken to withhold the 5% increase. The typical time it takes an employee to reach the top step of the salary range is three and a half years. Police Officer and Firefighter classifications have seven, 5% salary steps that occur automatically. It generally takes a public safety employee five and a half years to reach the top step.

This traditional Civil Service compensation structure provides pay increases based upon time in the job rather than performance, and also makes it difficult to proactively control wage growth. Elimination of "automatic" step increases and the reconfiguring of salary ranges is a strategy to assist the City in controlling costs as well as providing valuable tools for building the City's workforce of the future.

Another aspect of the City's compensation structure is the eligibility for overtime. Many City employees receive overtime compensation over and above what is required under the Federal Fair Labor Standards Act (FLSA). For example, paid time off is included in the calculation of overtime and results in sizeable overtime costs even when an employee has not actually worked more than forty hours in a week. In addition, there are positions that qualify for exemption from overtime under the FLSA (i.e. salaried) but are currently receiving overtime.

These practices, while common in Civil Service, increase the overall costs of providing services. Changes to these practices would provide additional means of controlling future costs.

Guiding Principles for the Upcoming Labor Negotiations

Based upon last year's negotiations as well as feedback received regarding that process, the following guiding principles are recommended to be included in Council's direction to the City Manager for the upcoming labor negotiations.

Commence Negotiations in January 2011

It is very important that the negotiations between the City and the bargaining groups commence early so that there is sufficient time to carefully evaluate proposals that are exchanged between the City and each union. Last year, concerns were raised that there was not sufficient time for the negotiations. For Fiscal Year 2010-2011, the City achieved contractual agreements with the majority of the unions to commence negotiations in January.

Continue Using a Total Compensation Approach

The cost of an employee is not limited to cash compensation. It includes the total cost to the City, including pay and benefits. For example, the City's cost of retirement benefits comprise a significant portion of total compensation.

Last year, the City Council provided direction to achieve a 10% total compensation reduction. There were some misunderstandings regarding "total compensation." There is value in continuing efforts to provide information to employees as to the total cost to the City of pay and benefits.

The City will continue using a total compensation approach in the upcoming labor negotiations.

Savings Must be Achievable & Verifiable in Fiscal Year 2011-2012

In order for a proposed change to help save jobs and services for the coming fiscal year and contribute towards solving the budget shortfall, the savings generated in concessions must be achievable and verifiable for Fiscal Year 2011-2012.

For example, savings generated in previous years were allocated to maintaining funding of services and the jobs that provide those services. A proposal to provide "credit" for savings achieved in previous years does not achieve any funds that can be used to save services in Fiscal Year 2011-2012 and balance the City's budget. In other words, the allocated funds cannot be utilized twice.

Another example would be a proposal to "trade in" vacation or personal leave provided to employees towards the 10% total compensation reduction. While reductions in paid time off of work would result in an increase in work hours and productivity, there is no savings that can in turn be used to preserve services and jobs. In other words, there is no reduction in the City's annual cost for an employee if they take 80 hours of vacation or 0 hours of vacation. The "cost" or "savings" is in productive time. It should be noted that savings may be achieved in some cases by a reduction in time off of work through savings in overtime costs. In certain job

functions, an employee absence must be covered with another employee receiving overtime. However, not in all cases is an employee absence filled by another employee on overtime.

Reductions in City Jobs and Services Do Not Reduce Per Employee Costs

An unfortunate alternative to reducing the average costs per employee, the City Council can reduce the size of the workforce by eliminating positions and the associated services. If the City Council eliminates positions and the services that those positions perform, a bargaining unit cannot be given "credit" in lieu of wage and benefit concessions. For example, during last year's negotiations, some bargaining units proposed "credit' on the concessions for reductions in positions.

Avoid Adverse Impact to Retirement Systems

Ensuring that the City has sustainable retirement benefits available to current and future employees is of the utmost importance to the City. Taking steps to ensure that both the City's and employees' retirement contributions are made and the retirement system is kept whole is one component of achieving sustainability.

Similar to agreements reached in previous years, all proposals should include provisions to ensure that the retirement system is kept whole. For example, unpaid furloughs, if not structured correctly, could result in a shortage of payment from the City and the employees to the retirement system.

Consider Inter-Relationship of Variations by Bargaining Unit

It is important that we are mindful of the impact that differences in the way concessions are achieved across bargaining units may have. Issues such as compaction, in which a supervisor may have the same or lower rate of pay than the employees they supervise. This is not only seen as unfair by supervisors, it is not accepted management practice. If this continues, it may create a disincentive for employees to pursue promotional opportunities. Other issues, like variation in healthcare plan design by bargaining unit may decrease buying power and increase cost for the City as well as employees. Because of the variations in the concessions achieved last year, as well as some groups not participating in the concessions, compaction is currently a problem.

Transparency in Negotiations

In 2008, the City Council adopted the attached Council Labor Negotiation Guidelines that were incorporated into the Council Policy Manual. As stated in those guidelines, the City has the right to insist that labor negotiations take place at the bargaining table. However, there is an interest in transparency in the labor negotiations process.

Given the significant portion of the City's General Fund that is allocated to employee costs and the direct impact that labor negotiations has to those costs, the City has made significant efforts to provide an unprecedented amount of labor relations information to the public. This includes information prior to the initiation of negotiations, negotiations in progress, and total

information prior to the initiation of negotiations, negotiations in progress, and total compensation costs for City employees. The link to this website is: http://www.sanjoseca.gov/employeeRelations/labor.asp.

Those efforts will continue for 2011. All proposals made by the City and each bargaining unit will be posted on the City's website after they are exchanged.

Availability of Information Requests and Responses to be Public

During last year's negotiations, the City received an unprecedented number of information requests from the bargaining units. The City provided responses to requests for information that was relevant and available. As the City enters negotiations with the bargaining groups in January, the City will continue to respond to any information requests that are made and provide information that is relevant and available. These requests and responses will be posted on the City's website.

Inclusion of Operational and Other Contractual Issues

There are unique issues for specific union contracts that are related to operations or other contractual issues. There may be issues that need to be addressed by specific bargaining unit to the extent that they are mandatory subjects of bargaining.

CONCLUSION

Although these are difficult recommendations, they are provided for the City Council's consideration and discussion at the November 18th Special City Council Meeting in order to address the preliminary $70 million General Fund shortfall.

By being clear and aligned in the direction, the City Council can assist staff to achieve timely, successful resolutions though the negotiation process.

COORDINATION

This memo has been coordinated with the City Manager's Budget Office. Legal issues that arise during labor negotiations will be coordinated with the City Attorney.

Debra Figone
City Manager

For questions please contact Alex Gurza, Director of Employee Relations, at 535-8155.

Attachment A: Council Policy on Labor Negotiation Guidelines (approved March 4, 2008)

ATTACHMENT A

COUNCIL POLICY

TITLE COUNCIL LABOR NEGOTIATION GUIDELINES	PAGE 1 of 2	POLICY NUMBER 0-39
EFFECTIVE DATE March 4, 2008	REVISED DATE	
APPROVED BY COUNCIL ACTION	3/4/2008, Item 3.6, Res. No. 74265	

BACKGROUND

Collective bargaining is governed by the Meyers-Milias-Brown Act (MMBA), the City of San José Employer-Employee Relations Resolution (#39367) and the City Charter. The City Charter designates the City Manager as the chief administrative officer of the City. Accordingly, Resolution #39367 delegates the authority to negotiate labor contracts on behalf of the City to the City Manager or the City Manager's designee.

Pursuant to the Meyers-Milias-Brown Act, the City has a right to insist that contract negotiations take place at the bargaining table between the designated representatives of the City and the designated representatives of the various bargaining unit employees. Members of the City Council should refrain from negotiating directly with employee representatives. Both the City and the bargaining units have an obligation under applicable laws to negotiate in good faith.

As used in this policy, "negotiate" means to meet and confer with another to endeavor to reach agreement on matters within the scope of representation.

PURPOSE

This policy applies only to the Mayor, members of the City Council and Mayor and Council staff.

References in this policy to members of the City Council or Council staff include the Mayor and Mayor's staff.

The purpose of this policy is to set guidelines for the City Council and Council staff to ensure labor negotiations are conducted in good faith and to avoid actions that would circumvent the City's designated bargaining team.

POLICY

It is the policy of the City Council that all of its members and staff shall abide by the following guidelines when the City Manager or the City Manager's designee is in negotiations with any bargaining unit:

1. Pursuant to San José Resolution #39367, negotiations are conducted by the City Manager through his/her designee. Accordingly, negotiations regarding potential proposals and possible settlement shall occur between the City's designated negotiator(s) and the union's designated negotiator(s).
2. Pursuant to Section 411 of the City Charter, while the Council may express its views to the City Manager, the Council shall not interfere with the execution by the City Manager of his or her authority and duty to negotiate on behalf of the City.
3. Members of the City Council or Council staff shall not negotiate with the bargaining unit representatives or persons acting on their behalf.
4. Nothing in this policy shall prohibit members of the City Council or Council staff from listening to bargaining unit representatives or persons acting on their behalf. Members of the City Council shall not knowingly respond to or discuss any proposals not presented to the negotiating team or any confidential closed session discussion.

5. Members of the City Council and City Council staff shall disclose to the City Manager and to the entire City Council material communications regarding issues related to ongoing negotiations. (See Council Policy 0-32 regarding disclosure of material facts).
6. Authorization and direction to the City's negotiating team is provided in closed session. In order to maintain the integrity of the negotiation process, such authorization must remain confidential.