

# Memorandum

**TO:** CITY COUNCIL

**FROM:** Mayor Chuck Reed

**SUBJECT: DECLARATION OF FISCAL  
EMERGENCY AND BALLOT  
MEASURES**

**DATE:** June 20, 2011

Approved

*Chuck Reed*

Date

*6/20/11*

## RECOMMENDATION

Defer Items 3.1(a) and 3.1(b) regarding fiscal emergency and ballot measures regarding fiscal reforms and disability retirement to August 2, 2011.

Include the following in the Report on Council direction on fiscal reforms (Item 3.1(c)):

- a. Report on analysis of costs of possible new "opt in" tier and other proposed changes in retirement benefits for existing employees, as directed on May 24, 2011.
- b. Update the Council on negotiations with unions regarding a process to combine meeting and conferring on a fiscal reform ballot measure with meeting and conferring on contract terms for retirement reform.
- c. Direct staff on scope and timing of polling to be done to test voter support for revenue measures if fiscal reforms are implemented.

## BACKGROUND

We urgently need to take action to on fiscal reforms to help reduce our costs prior to Fiscal Year 2012-2013 when we will face another major budget shortfall. Action must be taken quickly to ensure that we reach a resolution before the budget process begins for 2012-2013 so we can avoid additional service cuts and layoffs.

The City Council has directed staff to work with the bargaining units on potentially giving more time to the process for consideration of a fiscal reforms ballot measure so that contract negotiations over broader retirement reform issues perhaps could be done at the same time.

Some of our unions (AEA, CAMP, AMSP, POA, IAFF) have agreed on a framework do so, and some additional time should be allowed before the Council sets the date for ballot measures. The October 31, 2011 deadline to complete the negotiations agreed to in the framework provides substantial time to negotiate the complex issues of pension reform, reach a resolution in time to achieve savings for the 2012-13 fiscal year, and go to the voters in March 2012.



# Memorandum

**TO:** Mayor and City Council

**FROM:** Councilmember  
Donald Rocha

**SUBJECT:** Fiscal Reform Plan

**DATE:** June 20, 2011

Approved

Date

6/20/11

## INTRODUCTION

Council direction on May 24, 2011 concerning the City Managers Fiscal Reform Plan provided that the City Manager would perform analysis of several different alternatives, including the memo issued by the Mayor on May 13<sup>th</sup>, the bullet points Councilmember Constant distributed, and the memo that I issued on May 20<sup>th</sup>. It was my understanding that Staff would return to Council with the aforementioned information and cost analysis in order to facilitate a fully informed decision in respect to negotiation points with our bargaining units, pension reform direction, a proposed ballot measure, and potential declaration of a fiscal and public safety emergency. As of the distribution of this memorandum, it is my understanding that staff intends to communicate its Council directed analysis through a power point presentation, and may possibly release a staff report before the meeting. Given the lack of certainty that information will be provided in advance of the meeting, I have decided to focus on laying out a process and approach to negotiation that I believe will give us the best chance of coming to agreement. If staff does release the requested information in advance of the meeting, I am open to incorporating any valuable policy work into the direction I have suggested.

## RECOMMENDATION

- A. Approve the Mayor's memo dated June 20, 2011, and respectfully request that the deferral dates be amended as follows:
  1. Council consideration of Item 3.1(a), declaration of fiscal and public safety emergency, will be deferred to the meeting at which the Council approves the Mayor's March Budget Message for Fiscal Year 2012-13, in order to give staff time to pursue all cost saving alternatives before resorting to an emergency declaration.
  2. Council consideration of item 3.1(b), discussion of draft ballot language for possible charter amendments, will be deferred to October 31, 2011, to allow staff time to engage with the bargaining units, as outlined in item B below.
  
- B. I have heard repeated concern from staff that they be given clear negotiating direction on retirement reform so that they can begin working with our bargaining units to find solutions. In order that negotiations may begin as soon as possible, I recommend that the Council adopt the following negotiating direction to be used only as a starting point for the retirement reform discussion:

**1. Negotiate Under a Pledge of Cooperation and Agreement**

Direct staff to use the framework for retirement reform negotiations agreed to by AEA IFPTE Local 21, CAMP IFPTE Local 21, and AMSP (included as Attachment A), including the deadline for negotiations of October 31<sup>st</sup> established as part of that framework, as a model for agreements with the remaining bargaining units.

**2. Changes to the Existing Retirement System**

Instead of beginning negotiations on 1<sup>st</sup> tier changes with a specific proposal and ballot measure language, staff is directed to begin by attempting to determine what level of 1<sup>st</sup> tier changes, if any, the bargaining units would support in categories listed below. The below categories are items i through o on page 2 of the Mayor's Adopted March Budget Message; I believe they are a better starting point for negotiation than the very specific proposals outlined in the Mayor's May 13 memo. As part of these initial discussions, staff shall not present the Mayor's May 13 memo as the sole City proposal. With that said, if agreement cannot be reached on this item through negotiation, the Council would preserve its ability to consider the Mayor's memo or other proposal as outlined in item B5 below.

- The retirement age should be raised.
- Guaranteed annual increases in pension benefits should be eliminated.
- The rate of accrual for pension benefits should be lowered.
- Spiking of pension benefits should be prohibited, including lengthening the period used to calculate final average salary.
- Bonus payments for retirees should be eliminated, except for long term service retirees who fall below the poverty level.
- The maximum percentage of salary that retirement benefits are based on should be reduced.
- Unfunded retirement liabilities need to be addressed, including risk analysis and sharing of risk with employees.

**3. 2<sup>nd</sup> Tier for New Employees**

For purposes of beginning a discussion on 2<sup>nd</sup> tier, staff is directed to put forward the plan design in Attachment B, which I originally put forward at the May 24, 2011 Council meeting. We should treat this plan design as a basis for discussion, not as a formal proposal or final decision as to what benefit levels we want to implement. If this proposed plan design does not meet the target Council has established (a minimum normal cost of 12.4% with benefits greater than those provided by Social Security) benefit levels can be modified to bring the plan within council direction. This direction should not impede, disrupt, or preempt the discussion in Item #1 but should be on the table during, and/or after its conclusion. It is important to work collaboratively on this issue prior to the negotiation of new contracts and next fiscal year's budget adoption in order to continue the collaborative spirit that our Manager and bargaining units have developed.

**4. If the Bargaining Units and Council Agree on 1<sup>st</sup> and/or 2<sup>nd</sup> Tier Changes**

If bargaining units are willing to support 1<sup>st</sup> and/or 2<sup>nd</sup> tier changes at a level that is acceptable to the Council, staff will meet and confer with bargaining units on necessary municipal code changes or ballot measure language for charter amendments (if necessary, based on existing charter minimums) to effect such changes. The timeline

for such meet and confer process should preserve the Council's ability to place a measure in front of the voters at a March 2012 election.

5. **If the Bargaining Units and Council Do Not Agree on 1<sup>st</sup> and 2<sup>nd</sup> Tier Changes**

If the Council decides that the 1<sup>st</sup> and/or 2<sup>nd</sup> tier changes the bargaining units are willing to pursue are insufficient, staff will agendize a Council decision on which specific 1<sup>st</sup> tier changes it wishes to pursue. Discussion regarding this decision should initially take place in closed session to allow for full discussion of legal issues and risk. Should the Council decide on a set of specific 1<sup>st</sup> tier changes and process to effect such changes, the City Manager will meet and confer with the bargaining units on potential municipal code modifications and/or ballot language for charter amendments (if necessary, based on existing charter minimums) necessary to effect such changes. The timing of the Council's decision on whether to pursue a ballot measure without the agreement of the bargaining units should preserve the Council's ability to put a measure on the ballot for a March 2012 election and provide the City adequate time to fulfill its meet and confer obligations.

- C. As part of the Council's deliberation on 1<sup>st</sup> tier changes, the Manager is directed to analyze the possibility of either exempting retirees who have been separated from the City for a long period of time from benefit changes, or changing their benefits to a lesser degree. The policy consideration here is that employees who retired long ago under lower benefit levels may be affected differently by 1<sup>st</sup> tier changes than more recent retirees. It is necessary to know prior to any implementation of any retirement reforms whether employees who retired 10, 15, or 20 years ago have significantly different pension levels, and how proposed 1<sup>st</sup> tier changes may affect them.

## **ANALYSIS**

### **Fiscal and Public Safety Emergency**

Declaring a fiscal and public safety emergency before we've conducted negotiations and meaningfully pursued all of our options is premature and might compromise efforts to solve the problem. The Public Law Journal article referenced in the Mayor's memo dated May 24<sup>th</sup>, entitled "Declarations of Fiscal Emergency: A Resurging Option for Public Entities Attempting to Deal With the Current Economic Climate" states on page 12 that the courts have found that before a public agency can impair its own contracts, it must be able to show that it did not "impose a drastic impairment when an evident and more moderate course would serve its purpose equally well." In my opinion, we have not sufficiently explored all possible alternatives in order to demonstrate that there is not a more moderate course. Before taking a step that has already raised questions from rating agencies about the City's fiscal future, we should make every effort to resolve our problems prior to the declaration of an emergency.

### **Negotiation Direction**

Now that we have concluded employee contract negotiations regarding compensation and are no longer operating under a tight budget timeline, we have a chance to really engage with our employee unions on pension reform in a more productive and less tense context. It is my hope that our City staff and bargaining units can sit down and work together to identify which reform measures we agree on and which we don't. Within these negotiations the City should fully evaluate on its merits *any* pension reform proposal, which could include an opt-in proposal, that realizes significant cost savings. The City's primary goal should be to work with its bargaining units to develop a package of reforms that protects city services in the interest of our residents.

By starting with a common goal, not a hard position, this approach is akin to interest based bargaining, and I think will give us the best chance of working meaningfully with the bargaining units. This approach is a departure from our past practice of exchanging proposals, but I think it has the potential to promote a more successful collaboration than our past efforts. If it does not succeed, we reserve the ability to move proposals through the negotiation process as has been our previous practice, as outlined in my recommendation B5.

## **CONCLUSION**

There are two paths that we can choose to follow towards our goal: one is to identify our cost savings target on our own and implement them through contract negotiations and ballot measures, and the other is to identify those bargaining units willing to work with us and determine which issues we can address together. I prefer the later as a starting point. If the two sides are not able to find common ground, I am willing to discuss the former approach with my colleagues once we have exhausted negotiations. If this process does not provide reforms that are acceptable to the Council, then the Council can choose a different approach.

I believe that an atmosphere which is collaborative and engages employees as part of the solution should be our first choice. As we embark upon a reform effort fraught with legal questions, a collaborative solution may offer the best means of limiting our legal risk and implementing reforms on a quick timeline. Making an attempt to work with our unions is not only a fair approach, it is also pragmatic, and offers the best chance of avoiding a lengthy legal dispute.

Without the benefit of having the costs of the varying proposals in advance of our meeting, the best recommendation that I can make, and that I will feel comfortable suggesting, is direction on how to proceed in terms of process and a framework with proposed issues for consideration.

# Attachment A

**PLEDGE OF COOPERATION & AGREEMENT UPON  
A FRAMEWORK FOR RETIREMENT REFORM AND RELATED BALLOT MEASURE  
NEGOTIATIONS  
JUNE 17, 2011**

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CITY OF SAN JOSE

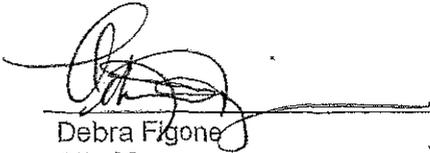
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**ASSOCIATION OF ENGINEERS AND ARCHITECTS, IFPTE LOCAL 21 (UNITS 41/42 AND 43)  
CITY ASSOCIATION OF MANAGEMENT PERSONNEL, IFPTE LOCAL 21  
ASSOCIATION OF MAINTENANCE SUPERVISORY PERSONNEL**

1. The parties are fully committed to negotiating in good faith to reduce the costs of the Federated City Employees' Retirement System and to preserve critical City services and the employees who deliver those services.
2. The parties agree to negotiate concurrently on the issues of retirement reform and related ballot measure(s). Negotiation of retirement reform shall include pension and retiree healthcare benefits for current and future employees, including but not limited to healthcare benefits; the Supplemental Retiree Benefit Reserve (SRBR); an opt-in program in which current employees could voluntarily choose to opt-out of the current level of pension benefits into a lower level of benefits; and other items as identified through the negotiations.
3. Although the negotiation sessions on retirement reform and related ballot measure(s) will not be public, all written proposals and correspondence exchanged will be made available to the public on the City's website.
4. Any party's relevant subject matter experts may attend negotiation sessions. By mutual agreement of the City and the Unions, other individuals may attend negotiation sessions.
5. It is understood that the parties shall each engage an actuary and work together to develop cost estimates. It is understood that the Annual Required Contribution (ARC) shall be determined by the Federated City Employees' Retirement System Board's actuary.
6. Estimated cost savings for any proposals during the negotiations shall be supported by analysis and data.
7. The parties agree to meet and confer in good faith and agree to complete the negotiation process by October 31, 2011. If the parties are unable to reach an agreement on retirement reform and/or related ballot measure(s) by October 31, 2011, the parties shall proceed to impasse, pursuant to the procedures outlined in the Employer-Employee Relations Resolution (EERR) #39367. In the event of impasse, AEA, AMSP and CAMP will participate in the impasse procedures collectively. As set forth in the Side Letters on Retirement Benefits for current and future employees dated March 23, 2011, the City will have the right to unilaterally implement in the event that no agreement is reached at the conclusion of negotiations and mandatory impasse procedures on the issues of retirement reform (including pension, retiree healthcare and the Supplemental Retiree Benefit Reserve). The City Council expressly reserves the right to propose charter amendments in the form of ballot measure(s) at the conclusion of negotiations and any impasse procedures, subject to the above obligations.

8. It is understood that, by participating in these negotiations, neither party waives any legal rights, including the Unions' or employee's rights to assert that certain benefits are vested.

FOR THE CITY



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Debra Figone  
City Manager



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Alex Gurza  
Director of Employee Relations



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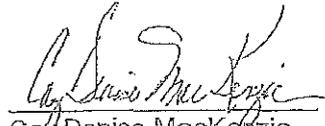
Gina Donnelly  
Deputy Director of Employee Relations

FOR THE UNIONS



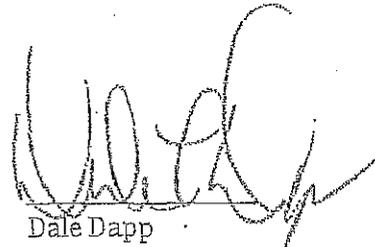
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John Mukhar  
AEA IFPTE Local 21



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Denise MacKenzie  
CAMP IFPTE Local 21



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Dale Dapp  
AMSP

## Attachment B: Benefit Levels for 2<sup>nd</sup> Tier

Benefit	Recommendation
Retirement Age	<p>Federated: 62 Public Safety: 57</p>
Early Retirement Reductions	Allow early retirement provided that the benefit does not exceed the actuarial value of full retirement.
Formula	<p>Federated: 2% per year of service for 30 years, to a maximum of 60% of final salary Public Safety: 2½% per year of service for 30 years, to a maximum of 70% of final salary</p>
COLA	Tied to Bay Area CPI and capped at 1.5%
City/Employee Share of Costs	50/50 split for 2 <sup>nd</sup> tier normal costs and unfunded liability
Final Salary	Final 3 year average
Health Care	Employees receive a fixed dollar amount for retiree healthcare costs based on how many years of service they have when they retire (as recommended by staff in the last paragraph of page 41 of MBA #1).
Service Credit	Change the definition of one year of service from 1739 pensionable hours to the number of hours typical Federated and typical Public Safety full time employees work per year.
Opt-in	Allow for an opt-in program for 1 <sup>st</sup> tier employees.



# Memorandum

TO: City Council

FROM: Mayor Chuck Reed  
Vice Mayor Madison Nguyen  
Councilmember Rose Herrera  
Councilmember Pete Constant  
Councilmember Sam Liccardo

SUBJECT: DECLARATION OF FISCAL  
EMERGENCY AND BALLOT  
MEASURES

DATE: June 22, 2011

APPROVED:

*Chuck Reed* *Pete Constant* *6-22-11*  
*Sam Liccardo* *Madison Nguyen* *Rose Herrera*  
*RH* *N.V.*

## RECOMMENDATION

Negotiations with the bargaining units shall include the following direction that continues with the current Council direction, with the additional flexibility to:

### 1. Opt-In Program for Current Employees:

- a. Negotiate an "opt-in" plan, and draft related ballot language implementing such a plan, such that when combined with the current Council direction, the City's share of retirement costs for FY12-13 would not exceed the aggregate cost of pension and retiree health costs for FY10-11 (approx. \$186.0 million for all funds).<sup>1</sup>
- b. Make explicit to all parties that the incentive for employees to choose to "opt-in" to this lower tier of benefits by:
  - 1) Enabling these employees to avoid the additional contribution to pay for unfunded liabilities, as described in Paragraph 2, below, and
  - 2) Reducing the costs of benefits for these employees.

### 2. All Other Current Employees Who Decline to Opt In:

- a. Calculate the savings in the City's Annual Required Contribution (ARC) for each plan (Federated, Police and Fire) from the opt-in program described above, again assuming that every employee would choose to "opt-in."
- b. Negotiate additional employee contributions in an amount equivalent to the ARC savings from the opt-in program, to pay for benefits and unfunded liabilities.

<sup>1</sup> For purposes of making the cost calculations described in that paragraphs 1 and 2, the City Manager should assume that every employee would choose to "opt-in" to the new tier of benefits.

According to the City Manager's May 2, 2011 Fiscal Reform Plan, the \$186.0 million figure includes the City's pre-payment discount. It also reflects what the City would have paid for retirement benefits had several bargaining units not paid for a portion of their contributions as part of that year's concessions.

- c. Provide all employees the ability to avoid paying these additional contributions by choosing to “opt in” to the set of retirement benefits outlined above.
3. **Other Alternatives:** Bargaining units are encouraged to offer other alternatives that achieve equivalent savings under the same assumptions.

### **BACKGROUND**

This recommendation re-affirms Council’s basic direction from its approval of the Mayor’s Budget Message on March 22, 2011: to propose a set of retirement benefits for current and new employees that would provide sufficient savings to restore the City’s services to their levels on January 1, 2011. We recognize that January 2011 levels of service remain inadequate by anyone’s standards, particularly as we consider the deep reductions in such basic services as police patrol, library hours, and other basic services. We must also recognize, however, that the task of reducing retirement costs sufficiently to reach even those paltry levels of service will prove challenging to the most committed of negotiators on both sides of the table. Our current direction, for instance, would require that by July 2012, we close a \$125 million gap between next year’s (FY12-13) and last year’s (FY10-11) retirement costs.

Recognizing the work that has already been completed to achieve savings through modifications to the SRBR, retiree COLA, workers compensation and reductions in retiree benefit premium costs, the direction for savings in this memorandum shall be combined with savings achieved by earlier council direction. The \$125 million in savings sought by this recommendation approximates the \$127 million in 1<sup>st</sup> Tier retirement savings identified in the City Manager’s Fiscal Reform Plan.

Fortunately, the leaders of several of our employee groups -- namely, the Association of Engineers and Architects, City Association of Management Personnel, Association of Maintenance Supervisory Personnel, the Police Officer’s Association, and the International Association of Fire Fighters-- recognize the severity of the challenges in front of us, and have stepped forward earnestly to begin negotiating to find a solution. We hope that with the additional direction provided in this memorandum, we will help to open the door for fruitful discussion.



# Memorandum

**TO:** HONORABLE MAYOR AND  
CITY COUNCIL

**FROM:** Councilmember Ash Kalra

**SUBJECT: DECLARATION OF A FISCAL AND PUBLIC SAFETY EMERGENCY**     **DATE:** June 23, 2011

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Approved		Date	6/23/11
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## RECOMMENDATION

1. Approve the Mayor's memorandum dated June 20, 2011 seeking to defer the fiscal emergency and ballot measures with the following amendment: instead of attempting to prepare ballot measures in time for a March 2012 election, we should aim to go to the voters in June 2012.
2. Use the approximately \$2 million in savings from moving potential ballot measures to June 2012 to immediately restore police officer positions.

## ANALYSIS

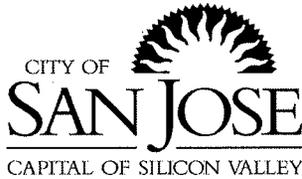
Last week I submitted a proposal to restore additional police officer positions. One aspect of the proposal recommended using the funds allocated for the potential November election to restore police officer positions if it turned out that there would be no November election. This proposal was rejected under the reasoning that an election could still possibly occur in November, and even if the election was postponed, funds would still be needed for an election in 2012.

The Clerk's office estimates that the cost of an election in June 2012 will be approximately \$1.4 million, \$2 million less than the estimated cost of \$3.4 million for an election in November 2011 or March 2012. We still have the opportunity to address the serious public safety issue currently facing San José.

States, counties, and cities all across the nation, including California, have moved or are considering moving their elections to coincide with statewide primaries in recognition of the significant cost savings that can be realized. Given our current fiscal dilemma, we should do the same.

Doing so would allow us to use this \$2 million to immediately restore police positions. As numerous police officers are scheduled to be laid off within days, there can be no dispute that this matter is urgent. Using these funds to restore police officer positions will allow us to address a clear public safety crisis while retaining funds for a potential June 2012 election and without touching a single penny currently earmarked for next year's budget shortfall.

While I appreciate the desire to move quickly on retirement reform, it is extremely uncertain whether the many complex legal questions that surround this issue can be resolved in time for a March 2012 election. Furthermore, under the City Manager's Fiscal Reform Plan, there are zero savings associated with first tier retirement for fiscal year 2012-2013, and all of the listed FY 2012-2013 savings are associated with issues that do not necessarily require ballot measures to implement. What is absolutely certain, however, is that San José is facing a potential crime epidemic, and we are running out of time to take steps to address it.



# Memorandum

**TO:** CITY COUNCIL

**FROM:** Councilmember Sam Liccardo

**SUBJECT:** FISCAL REFORM PLAN

**DATE:** June 24, 2011

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Approved Sam Liccardo Date 6/24/11  
by FB

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**Recommendations:**

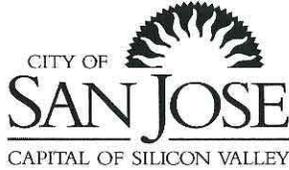
1. **Public Airing of Numbers and Actuarial Assumptions:** In a manner that does not obstruct, delay, or distract from the bargaining process, and at a time of her selection, the City Manager shall convene an informational meeting(s), inviting all of the bargaining unit leaders and their actuaries, in a public setting.
  - a. The meeting will serve to vet the City's assumptions, cost estimates, and the impacts of variations in plan design on costs. Actuaries and professionals hired by the bargaining units will also to demonstrate and explain their calculations and assumptions. The duration of the meeting(s) shall not exceed two days.
  - b. The meeting will be conducted in a manner that will best facilitate questioning and the exchange of information, with a goal to clearly understand differences in cost figures and assumptions, as well as to identify points of agreement.
  - c. This meeting will not be hosted by a policymaking body, nor governed by the Brown Act, but will be publicly noticed and made open to the public.
  - d. This direction does not have any bearing on the manner in which the City Manager shall conduct actual negotiations with our bargaining units on this or an.
  
2. **Information Requests:** During these negotiations, City negotiators shall continue their current practice of posting information requests from the bargaining units, and shall inform the Council and the public of the status of those requests, with an estimate of any forthcoming response. In those instances in which the City deems a response inappropriate, the City shall explain the rationale for that determination, such as whether the request is too voluminous, too burdensome, irrelevant, duplicative, tardy, etc.
  
3. **Polling:** the City Manager shall include questions in its summer polling that seek to assess the level of voter support for:
  - a. a revenue-generating measure where it is:
    - i. included on the same ballot with retirement benefits reform,

- ii. Included within the same measure with retirement benefits reform,
- iii. Placed on separate ballot from a retirement benefits reform referendum.
- b. a specific tax (to support public safety) or a general tax.
  - i. Questions shall ascertain whether a measure will be most successful if it is targeted solely on funding police, fire, or more broadly focused on “public safety,” (to include crossing guards, gang prevention programs, and the like) are most likely to engender public support.
- c. Ballot language should be vetted with organizations experienced in proposing and supporting ballot measures, such as the Silicon Valley Leadership Group, South Bay Labor Council, and the San Jose-Silicon Valley Chamber of Commerce.

**Analysis:**

Separate from the issue of Council direction to negotiators regarding the outcome of negotiations, it appears worthwhile to consider the “how” of negotiations in this very unique and uncharted territory. We should recognize the expertise and experience of our negotiating team, but also that to some extent, achieving agreement under these circumstances requires consideration of unorthodox and novel approaches. We offer those listed above.

There appears little question that we cannot continue to cut our way to service level solvency; the City needs new revenues. Accordingly, we direct additional examination of the polling options described above.



# Memorandum

**TO:** City Council

**FROM:** Mayor Chuck Reed  
Vice Mayor Madison Nguyen  
Councilmember Rose Herrera  
Councilmember Sam Liccardo

**SUBJECT:** Fiscal Reforms

**DATE:** May 13, 2011

**APPROVED:**

*Chuck Reed*  
*Madison Nguyen*

**DATE:**

*5/13/11* *Sam Liccardo*

## INTRODUCTION

The dramatic impacts of the budget shortfall on our community demonstrate why we have to gain control over skyrocketing retirement costs. If we act now, we can preserve the retirement benefit levels our employees and retirees have earned and accrued, and we can restore jobs and vital services.

If we fail to act, jobs and services will be decimated in a fiscal disaster and retirement benefits will be cut.

This proposal is not the only solution. It is one combination of ideas that we believe will solve the problem. We are open to other solutions, and our proposal directs staff to engage with employee groups – many of whom have said they are eager to work in partnership to solve this crisis – and to discuss alternatives that also solve the problem.

## RECOMMENDATION

### A. DECLARE A FISCAL AND PUBLIC SAFETY EMERGENCY

Declare a fiscal and public safety emergency and direct staff to return to the Council on June 21 with a formal declaration that describes the necessity of making fiscal reforms to avert a fiscal disaster, prevent substantial degradation of public safety and other vital city services, and maintain the integrity of our retirement system so that earned and accrued benefits can be paid to current and future retirees.

### B. AMEND THE CHARTER IN ORDER TO LIMIT RETIREMENT BENEFITS AND TO REQUIRE VOTER APPROVAL OF INCREASES IN RETIREMENT BENEFITS

Approve the City Manager's Fiscal Reform Plan and direct staff to return to the Council on June 21 with proposed changes to the Charter to implement the Manager's recommendations, subject to the following additions and limitations, all to be placed into the Charter in order to set maximum limits on benefits and other compensation that may not be exceeded without voter approval:

### 1. **Place Limits on Retirement Benefits for New Employees**

Without voter approval of enhancements or increases, new employee retirement benefits shall be limited to a hybrid plan that may consist of a combination of social security, defined benefits or defined contributions but the maximum City contribution in total shall not be less than 6.2% nor greater than 9% of base salary or 50% of the costs of the benefits, whichever is less.

**Health Benefits:** Medical care or health insurance for retired employees may only be provided to employees who have 20 years of service or more or to employees who receive a service disability retirement. Employees will pay a minimum of 50% of the cost of retiree healthcare.

**Retirement Provisions:** If a defined benefit plan is included it must be based on actuarial assumptions that are risk-free for the City and the employees and the age of eligibility for payment of accrued service retirement benefits shall be 65, except for sworn police officers and fire fighters, whose service retirement age shall be 60. Earlier retirement may be permitted with reduced payments that do not exceed the actuarial value of full retirement.

### 2. **Place Limits on Retirement Benefits for Existing Employees**

Without voter approval of enhancements or increases, retirement benefits for existing employees shall be limited as follows:

**Slow Down the Accrual Rate:** Benefits earned and accrued benefits to date shall not be reduced but additional pension benefits shall accrue at a maximum rate of 1.5% per year of service.

**Increase the Age of Eligibility:** The age of eligibility for service retirement for existing employees shall increase by six months annually on July 1 until the retirement age reaches the age of 60 for police officers and fire fighters and 65 for all other employees. Earlier retirement may be permitted with reduced payments that do not exceed the actuarial value of full retirement.

**Increase Years of Service for Medical Benefits:** The years of service required to qualify for health insurance benefits after termination of service shall increase by six months annually on July 1 until it reaches 20 years, except for employees who receive as service disability retirement. Employees will continue to pay a minimum of 50% of the cost of retiree healthcare.

### 3. **Place Limits on Benefits for Existing and Future Retirees**

Without voter approval of enhancements or increases, retirement benefits for existing retirees shall be limited as follows:

**Slow the Rate of Increase:** Increases in pension payments to retirees shall be limited to the increase in the Bay Area CPI and shall not exceed 1% per year.

**Restrict Bonuses:** Bonuses or other supplemental payments may be made only to long term service retirees or disability retirees whose household income falls below the poverty level (extremely low income) and shall not be funded from plan assets.

**4. Place Additional Limitations on Growth in Retirement Benefits if the Fiscal and Public Safety Emergency Gets Worse**

At any time the city pension or retiree health care plans have unfunded liabilities for pension or retiree healthcare greater than those existing on June 30, 2010, the following limitations shall be in effect for existing employees who have not opted into the benefits program for new employees, except upon prior approval of the voters:

- a. Retirement benefits shall not continue to accrue beyond the minimum benefits specified in the Charter, Article XV.
- b. Calculation of benefit payments shall be based on a 3-year average as specified in the Charter, Article XV.
- c. The age of eligibility for payment of service retirement benefits shall not be less than the retirement age specified in the Charter, Article XV.
- d. Benefits shall not be increased after retirement.
- e. Employees' share of the costs to amortize any unfunded liabilities greater than those existing on June 30, 2010, shall be 50%, unless they have opted into the benefits program for new employees.

At any time the city pension or retiree healthcare plans have unfunded liabilities for pension or retiree healthcare greater than those existing on June 30, 2010, bonuses, increases, or supplemental pension payments to retirees shall not be allowed, except upon prior approval of the voters.

These temporary provisions shall remain in effect until the unfunded liabilities have remained below the level of June 30, 2010 for three consecutive years.

**5. Implementation Provisions**

- a. All pension and retiree healthcare plans must be actuarially sound and unfunded liabilities shall be determined annually through an independent audit using standards set by the Government Accounting Standards Board.
- b. All of the above Charter amendments shall be severable but if any of the above provisions are or become illegal, invalid or unenforceable as to existing employees, then the existing employees' share of the costs to amortize any unfunded liabilities shall be 50%, unless they have opted into the benefits program for new employees.
- c. If any of the above provisions are or become illegal, invalid or unenforceable as to retirees, then all benefit enhancements or increases granted to retirees since the date of their retirement shall be eliminated.
- d. Existing and new employees will continue to pay a minimum of 50% of the cost of retiree healthcare.

- e. The City Council shall retain its power to amend or change any retirement plans under Charter sections 1500 and 1503 and no ordinances, agreements, policies or practices may eliminate that power without approval by the voters.

C. AMEND THE CHARTER IN ORDER TO REQUIRE VOTER APPROVAL OF INCREASES IN OTHER BENEFITS UNTIL THE EMERGENCY HAS PASSED AND ESSENTIAL SERVICES HAVE BEEN RESTORED

**1. Preserve and Restore Essential Services**

The following services are essential to the safety and quality of life for San Jose residents: police protection, fire protection, street maintenance, libraries, and community centers. Any time these essential services are not provided at or above the levels of January 1, 2011, or any time the libraries, community centers, fire stations or police substation built or under construction on January 1, 2011 are not operational, or any time the pension plans have unfunded liabilities, the Mayor, the City Council, the City Manager, the other Officers of the City, the Board of Arbitrators, and other arbitrators are prohibited from making or approving any contract, memorandum, agreement, award, grant, decision, resolution or ordinance to allow or require the City to do any of the following, except upon prior approval by the voters:

- a. Create or increase an unfunded liability for pensions, healthcare or other post employment benefits.
- b. Pay for unused sick leave or unused vacation time, except as required by state or federal law.
- c. Increase compensation for members of bargaining units after contracts expire.
- d. Give automatic step increases or other raises for time in the job that are not based on performance.
- e. Use hours not worked in determining eligibility for overtime or for retirement benefits.
- f. Pay overtime to executive, professional, or administrative employees or to other employees who are exempt from overtime requirements under the Fair Labor Standards Act or who are otherwise exempt from the Act.
- g. Pay workers compensation benefits for disability on top of disability retirement benefits without an offset to eliminate duplication of payments for the same cause of disability.
- h. Pay workers compensation benefits beyond what state or federal law require.
- i. Allow existing or former employees to make decisions to grant workers compensation or disability benefits for existing or former employees.
- j. Calculate retirement benefits on any compensation other than actual base salary paid or years (2080 hours) actually worked for the City of San Jose, except as required by state law.
- k. Make layoff or rehiring decisions without considering individual employee performance.
- l. Pay for more than 50% of the increase in the cost of healthcare benefits.

#### D. OUTREACH TO EMPLOYEES

Direct staff to meet and consult with bargaining units on these potential ballot measures. The outreach plan should include a process to engage immediately with those unions willing to acknowledge the retirement cost crisis and which desire to engage constructively with alternative solutions.

#### E. PREPARE BALLOT MEASURE LANGUAGE

Direct staff to return to Council on August 2 with ballot measure language to submit to the Registrar of Voters for a possible election in November to change the Charter to implement the above recommendations, as may have been modified through the meet and consult process, providing that provisions that are in conflict with express terms of negotiated contracts in effect at the time of voter approval shall be implemented on the expiration dates of those contracts.

#### F. SURVEY VOTERS ON POTENTIAL TAX MEASURES

Direct staff to prepare to survey voters to determine if implementation of these fiscal reforms increases the level of support for a potential tax increase.

### **BACKGROUND**

Over the past decade, vital city services have been reduced repeatedly because costs per employee have grown dramatically. San Jose's unfunded liabilities for retirement benefits have grown by billions of dollars and have driven up San Jose's annual retirement costs by more than \$190 million since 2000 (\$63 million in 2000 to \$255 million in 2011).

Last year we reduced our work force by 800 positions, down to 4200 general fund workers. Our police and fire departments today have about 2400 employees. Now we are facing another huge budget shortfall and are likely to have to cut another 600 positions, including police officers and fire fighters, dropping our general fund staffing down to 3600 positions.

If left unchecked, by 2016 retirement costs will increase, even using optimistic assumptions, to \$400 million per year. That increase in costs will require additional staffing reductions that will drive our general fund staffing down to 3000 employees.

Unfortunately, even greater increases in retirement costs are likely if actuarial assumptions - such as life expectancy, retirement ages or rates of investment return - are modified by the retirement boards to reflect modern conditions. As discussed at our study session on February 14,<sup>1</sup> our retirement costs could jump to \$650 million per year by 2016 as assumptions are updated.

Costs could also go up dramatically as new federal accounting standards are adopted. For example, the Governmental Accounting Standards Board (GASB) is currently considering accounting rules that would lower the permissible discount rate (*Pension Accounting and Financial Reporting by Employers*<sup>2</sup>). That change could result in an increase in annual costs to

<sup>1</sup> View the Council meeting online at [http://sanjose.granicus.com/MediaPlayer.php?view\\_id=22&clip\\_id=4824](http://sanjose.granicus.com/MediaPlayer.php?view_id=22&clip_id=4824). The discussion regarding future retirement costs is at 2 hours, 9 minutes into the meeting.

<sup>2</sup> The full report, *Preliminary Views of the Governmental Accounting Standards Board on major issues related to Pension Accounting and Financial Reporting by Employers*, is online at: [http://gasb.org/cs/ContentServer?c=Document\\_C&pagename=GASB%2FDocument\\_C%2FGASBDocumentPage&cid=1176156938122](http://gasb.org/cs/ContentServer?c=Document_C&pagename=GASB%2FDocument_C%2FGASBDocumentPage&cid=1176156938122).

amortized unfunded liabilities “by 150 to 200 percent above current levels.” (*New Proposals for Pension Books: GASB's potential accounting rules may clobber employers' budgets*, by Girard Millar, *Governing*, May 20, 2010<sup>3</sup>).

Additional huge cost increases to pay for unfunded liabilities would result in enormous reductions in staffing, destroying our ability to protect the public and preserve the quality of life for the people of San Jose. If we fail to act, and retirement costs grow to \$650 million by 2016, the ranks of general fund employees will shrink down to about 1600 workers. Even though it is not the worst case scenario, dropping to 1600 general fund workers would have a devastating impact on our city and leave us unable to provide vital services.

Neither we nor our retirees can afford to take the risk these costs will continue to escalate, pushing the City or the pension funds into insolvency, and putting the reduction of retirement benefits in the hands of a bankruptcy judge.

We must take bold and decisive action to make the changes necessary to save our city from a fiscal and service delivery disaster.

The Charter allows the Council to make changes to retirement benefits and we must exercise that power:

*“...the Council may at any time, or from time to time, amend or otherwise change any retirement plan or plans or adopt or establish a new or different plan or plans for all or any officers or employees.”* SECTION 1500

To make those changes, outlined in the recommendations above, a new section should be added to the Charter as ARTICLE XIX PENSION REFORM, FISCAL STABILITY AND PROTECTION OF ESSENTIAL SERVICES, to help stop spiraling cost increases, avert fiscal disaster, protect the integrity of the retirement system, and put San Jose on the path to rebuild the police force, fully staff fire stations, maintain streets, and keep libraries and community centers open.

These proposed fiscal reforms would not deprive employees of benefits that have been earned and accrued, but they are reasonable and necessary to enable the city to pay for benefits that have been earned and accrued without destroying the city’s ability to protect public safety and provide basic services for the people of San Jose. Our inherent power to make reasonable changes to the pension system, without taking away earned and accrued benefits, in order to maintain the integrity of the system has long been recognized by the California courts.

Some of these fiscal reforms may impact expectations of increases in future benefits that are viewed by some of our employees as vested and, therefore, unchangeable. Yet, these fiscal reforms are appropriate, reasonable, temporary and necessary to resolve this grave fiscal crisis. Thus, they are within the constitutional range of power of the City to protect the vital interests of our community, even if vested contract rights may be affected.

The fiscal emergency that we are dealing with requires action. Our power to act “to protect the lives, health, morals, comfort and general welfare of the public” is recognized under the United States and California Constitutions, even if contract rights are impaired (see *Declarations of*

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<sup>3</sup> Read the article at: <http://www.governing.com/columns/public-money/new-gasb-proposals-pension-bookkeeping.html>

*Fiscal Emergency: a Resurging Option for Public Entities Attempting to Deal with the Current Economic Climate*, California Public Law Journal, Vol. 34, No. 1, Winter 2011<sup>4</sup>).

Some people believe that the pension crisis is imaginary, that we have only to wait until the market goes back up and we'll be fine. That's simply wishful thinking. The \$155 million payment to the retirement funds the City made this year was not imaginary. The \$250 million payment the city must make next fiscal year is not imaginary. The hundreds of jobs that were eliminated this year were not imaginary. The hundreds of employees who will lose their jobs in the next fiscal year are not imaginary.

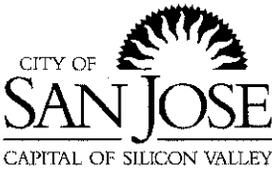
Such erroneous characterizations of our fiscal crisis demonstrate why it is necessary to take these measures to the voters to allow them to prevent a disaster.

Of course, if market gains result in the issue resolving itself by June, as some assert, some of the temporary measures may not be necessary for very long.

Placing these fiscal reforms on the ballot will allow the people of San Jose to decide these critical matters that will have a dramatic impact on their quality of life.

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<sup>4</sup> Online at [www.calbar.ca.gov/publiclaw](http://www.calbar.ca.gov/publiclaw).



# Memorandum

**TO:** Rules Committee

**FROM:** Councilmember  
Donald Rocha

**SUBJECT:** Rules Committee Agenda Item A. 1.

**DATE:** May 18, 2011

Approved

Date

5/18/11

## RECOMMENDATION

Fundamentally I support the need for fiscal reform in order to maintain our services and establish a fiscally sound government in the City of San Jose. The recommended direction below is important for consideration prior to making a decision of such significance as proposed in the memorandum from Mayor Reed, Vice Mayor Nguyen, and Councilmembers Liccardo and Herrera for consideration at the City Council meeting on May 24, 2011 (Item 3.4). I recommend that the City Attorney be directed to:

1. Provide for Mayor and Council consideration in closed session on Tuesday, May 24, 2011 a legal analysis and assessment of legal risk for the specific recommendations contained in the aforementioned memorandum.
2. Provide for Mayor and Council consideration in open session on Tuesday, May 24, 2011:
  - A. An assessment of the workload impact and staff capacity issues that could potentially be created for the City Attorney's Office by a legal challenge to a successful ballot initiative.
  - B. A description of what it means to declare a "fiscal emergency" and "public safety emergency," and an analysis of whether that designation could have implications for the City in terms of increased State oversight, audit of past, current or future expenditures, impact on bond rating, or any other potential impacts.
3. If the City Attorney feels that the above direction cannot be provided for consideration in time for the May 24, 2011 Council date, it is recommended that the item be deferred to the next immediate Council meeting or until staff is prepared and has completed the analysis contained in this memorandum.

I understand that the legal costs, even in the worst case scenario, would pale in comparison to the annual retirement costs and unfunded pension liability as projected by our City Manager and Retirement Director. However, I feel the above analysis will provide important data points that should be available to the Mayor and City Council, as well as the public, as they consider, comment, or vote on the proposed recommendations.



# Memorandum

TO: City Council

FROM: Mayor Chuck Reed

SUBJECT: **DECLARATION OF FISCAL  
EMERGENCY**

DATE: 5/24/2011

APPROVED:

*Chuck Reed* DATE: 5/19/11

## MEMO TO COUNCILMEMBERS

Attached is a copy of *The Law Journal* article referred to in the memo dated 5/13/10  
"Declarations of Fiscal Emergency: A Resurging Option for Public Entities Attempting to Deal  
With The current Economic Climate."

I understand the electronic version may be difficult to access on the State Bar website.

# Declarations of Fiscal Emergency: A Resurging Option for Public Entities Attempting to Deal With The Current Economic Climate

By Jonathon V. Holtzman, K. Scott Dickey, and Steve Cikes\*

In 1978, California voters enacted Proposition 13,<sup>1</sup> which placed significant limitations on the taxing power of local and state governments. In response, a number of California public entities attempted to declare a state of fiscal emergency as a means of reducing costs under existing labor contracts. These efforts were universally rebuffed by the courts, in part, because the state augmented local revenues in the wake of Proposition 13. Since then, conventional wisdom has been that declarations of fiscal emergency do not work.

With the recent sharp downturn in the economy, the conventional wisdom may no longer be correct. Several cities in California are currently engaged in or contemplating efforts to control costs through emergency declarations. Although the question whether such declarations will be effective this time around rests with the courts (and in some instances with arbitrators), there is cause to believe that the unprecedented nature of the economic problems public agencies currently face could yield a different result. A declaration of fiscal emergency may prove to be a critical tool in maintaining public service levels, limiting or eliminating the need for layoffs, and avoiding municipal insolvency through bankruptcy.

## WHY A DECLARATION OF FISCAL EMERGENCY MAY HELP STRUGGLING PUBLIC ENTITIES

The lion's share of most public entities' budgets – sometimes as much as 75 to 80 percent – goes to fund employee wages and salaries. The skyrocketing costs of employee benefits and unfunded labor agreements further exacerbate the budget imbalances towards labor costs. And most of these labor costs are locked in place by collective bargaining agreements that can be extremely difficult to alter, much less unwind. Consequently, most public entities only have control over a small amount of their annual costs. The elimination of 20 to 25 percent of the annual total budget – even if it were possible to do so and continue to provide services – would do little to aid an agency sliding towards insolvency.

A declaration of fiscal emergency may help unlock these otherwise fixed labor costs. Although both the United States and California Constitutions prohibit government from enacting legislation that impairs contracts,<sup>2</sup> courts have long recognized that this prohibition is subservient to government's power "to protect the lives, health, morals, comfort and general welfare of the public" – i.e., a public agency's inherent police powers.<sup>3</sup> For example, in the

seminal case of *Home Building and Loan Association v. Blaisdell*,<sup>4</sup> the United States Supreme Court upheld the constitutionality of a Minnesota law that restricted foreclosures on mortgages during the Great Depression. In doing so, the Court recognized that certain conditions may arise "in which a temporary restraint of enforcement [of contractual obligations] may be consistent with the spirit and purpose of the [Contract Clause] and thus be found to be within the range of reserved power to the state to protect the vital interests of the community."<sup>5</sup> And in *Veix v. Sixth Ward Building and Loan Association*,<sup>6</sup> the U.S. Supreme Court recognized that under the Contract Clause, a state's authority to protect its citizens through statutory enactments affecting contract rights "is not limited to" situations in which the public's "health, morals and safety" are at risk, but "extends to economic needs as well."<sup>7</sup>

Based on these precedents, a number of public entities have attempted to address instances of financial hardship by enacting legislation impairing and/or modifying their own labor agreements. The ability to suspend the provisions of labor agreements during the pendency of a fiscal emergency may, in an appropriate case, allow public entities to dynam-

*Continued on page 12*

Continued from page 11

cally respond to lost or severely reduced revenues, by allowing public entities to "roll back" wages and benefits, thus reducing the impact of those losses without necessarily reducing services or staffing, and without facing insolvency. It is important to emphasize, however, that the law in this area is not well developed, and not every failing agency is failing because of an actual fiscal emergency.

## THE PREREQUISITES FOR A DECLARATION OF FISCAL EMERGENCY

In *Sonoma County Organization of Public Employees v. County of Sonoma*,<sup>8</sup> the California Supreme Court, following Blaisdell, identified four factors for courts to use in determining whether a legislative impairment of a contract will be upheld in the face of a Contract Clause challenge. First, the contract modification must arise out of an actual emergency. Second, relief from the contract must be necessary to protect a basic societal interest rather than for the benefit of a particular group of individuals. Third, the modification or relief must be appropriately tailored to the emergency it was designed to address, and the conditions that result must be reasonable. And finally, the modification imposed must be temporary and limited to the exigency that prompted the legislative response.

These factors are not necessarily absolute. Since Blaisdell, the U.S. Supreme Court has in some cases upheld contractual impairments without some of these factors.<sup>9</sup> In *United States Trust Company of New York v. New Jersey*,<sup>10</sup> the United States Supreme Court acknowledged this shift and stated that while "the existence of an emergency and the limited duration of a relief measure are factors to be assessed in determining the reasonableness of an impairment, ... they cannot be regarded as essential in every case."<sup>11</sup> The Court established a new standard to evaluate whether a contract impairment is constitutional, holding that "an impairment may be constitutional if it is reasonable and necessary to serve an important public purpose."<sup>12</sup>

Generally, a public entity's finding of an emergency necessitating the impairment of contracts will be afforded some deference. Needless to say, however, courts will be less deferential to the decision when it considers a public entity's impairment of its own contractual obligations.<sup>13</sup> As one recent court decision explained, for an impairment to be considered reasonable and necessary in such cases, the public entity must show that it did not "(1) 'consider impairing the ... contracts on par with other policy alternatives' or (2) 'impose a drastic impairment when an evident and more moderate course would serve its purpose equally well,' nor (3) act unreasonably 'in light of the surrounding circumstances.'"<sup>14</sup>

### What Constitutes a True Fiscal Emergency?

One of the challenges faced by public entities in declaring a fiscal emergency is that there is no brightline rule for determining when circumstances justify such a declaration. While certainly a fiscal

emergency may exist before the public entity files for bankruptcy or reaches insolvency, courts considering whether a public entity faces an actual emergency have varied considerably in their assessments.

Several courts have found that a sharp decline in revenues and the concurrent inability to provide essential services constitutes a fiscal emergency sufficient to allow a public entity to impair its own contractual obligations. For example, in *Subway Surface Supervisors v. N.Y.C. Transit Authority*,<sup>15</sup> the New York court of appeals upheld deferral of a wage increase set forth in the city's collective bargaining agreement, where the city's fiscal emergency would have rendered it unable to "provide essential services to its inhabitants or meet its obligations to the holders of outstanding securities,"<sup>16</sup> and without cuts, it would not have been able to pay employee salaries or its vendors and would have defaulted on payments due on other outstanding obligations.

Similarly, in *Baltimore Teachers Union v. Mayor and City of Baltimore*,<sup>17</sup> the court found that salary reductions imposed by the city on police and teachers were reasonable in light of a sharp decline in city revenues, including a significant reduction in state funding. Also, in *Buffalo Teachers Federation v. Tobe*,<sup>18</sup> the court held that the city acted lawfully in imposing a wage freeze on employees after forecasting an increase in its budget deficit from \$7.5 million in fiscal year 2002-03 to \$93-127 million in 2006-07 and after the city had already laid off 800 teachers and 250 assistant teachers in the preceding four years.

In contrast, courts rejecting a declaration of emergency have tended to do so on the grounds that emergency is not a "true" emergency and that a public agency has failed to fully explore other, less intrusive cost saving measures. For instance, in *Sonoma County Organization of Public Employees v. County of Sonoma*,<sup>supra</sup>, the California Supreme Court found that a 6 percent reduction in revenues adopted in the wake of Proposition 13 was insufficient to justify impairment of a county's contractual obligation under its labor agreement with a union, given that the county's actions were based on a projected 22 percent reduction in revenue<sup>19</sup> and the "Legislature almost immediately returned \$5 billion accumulated in the state's surplus to local agencies to alleviate the potential – but not realized – effects of Proposition 13."<sup>20</sup>

The Second Circuit reached a similar conclusion in *Condell v. Bress*,<sup>21</sup> striking down a five-day payroll lag for state employees adopted to address a budget deficit, estimated to be \$1.005 billion. The court reasoned that the legislature had done nothing to address the claimed emergency before it sought to "impair[] contract rights to obtain forced loans to the State from its employees" and, without exploring alternatives first, the state could not legitimately claim a financial emergency existed.<sup>22</sup>

Likewise, in *University of Hawaii Professional Assembly v. Cayetano*,<sup>23</sup> the Ninth Circuit invalidated a state "pay lag" law, enacted to address an estimated budget shortfall of \$143 million. The court found that other, less-intrusive options were available, including a project to obtain additional funding from the federal government, further budget restrictions, and

the raising of taxes. Further, the court pointed out that "Defendants knew of the budgetary crisis at the time the collective bargaining agreement was negotiated and as the history of [the pay lag statute] shows, previously had attempted to implement a similar pay lag plan."<sup>24</sup> This authority might suggest that a true fiscal emergency must arise out of some unforeseeable chain of events occurring well after the underlying contracts were negotiated and entered into. But we believe that too much has been made of this argument.

Not all emergencies occur in an instant, like an earthquake. The current decline in municipal revenues, accompanied by the dramatic escalation in benefit costs is not something even public finance gurus anticipated. Many jurisdictions made labor agreements 'on the way down,' anticipating that the current recession would be like others seen before. Consequently, most negotiated agreements pushed wage increases off into later years – not appreciating the full extent of the collapse of the housing market and the continuing impacts it would have on revenues, or that the decline in the market would lead to the doubling of pension costs. In short, the determination that a concessionary agreement was not 'concessionary enough' in the end does not mean the public agency could or should have anticipated the severity of the problem when it entered into that agreement.

### STOCKTON: A CASE STUDY

An excellent example of these principles in action is the current fiscal emergency in the City of Stockton. The Great Recession that began in the fall of 2008 had a particularly devastating impact on the economic resources of Stockton. Since the start of the Great Recession, the city saw the largest sources of revenue for its general fund – property taxes, sales and use taxes, and utility user taxes – decline precipitously, in some cases by 25 percent or more. The housing market collapse led to a 66 percent decline in median home sale prices, as well as a huge wave of foreclosures. Unemployment, meanwhile, has nearly doubled.

While revenues declined, the city faced dramatically increasing employment costs. Wages continued to increase, driven primarily because of formula-driven raises and other automatic inflators contained in the city's 'closed' labor agreements. Pension and healthcare costs also rose – and continue to rise – at alarming rates.

Because of the decrease in revenues and the persistently increasing employment costs, the city faces a \$23 million budget shortfall for fiscal year 2010-11. The estimated budget shortfall is projected to widen to \$27.3 million in fiscal year 2011-12.

The city had already implemented a variety of cost reduction measures. It had reduced city-wide staff (including police) by 23 percent, renegotiated several labor agreements, imposed furlough days, instituted a hiring freeze, and reduced city operation hours across many departments. It also had eliminated many community programs and services.

But this was not enough. Because nearly 80 percent of the city's general fund budget is attributable to police and fire costs, concessions from these unions were necessary for the city to close its budget gaps. Despite significant efforts to do so, the city was unable to reach agreement with the police and fire unions on concessions. On June 22, 2010 – after weeks of continued negotiations with the police and fire unions, and just over one week before the city was required to approve a balanced budget – the city council adopted resolutions giving the city manager the authority to impose temporary measures on police and fire bargaining units in an effort to reduce costs and close the city's budget gap.<sup>25</sup>

Using its emergency powers, the city froze formula-driven raises for police and fire unions and took one fire truck out of service. The unions have sued,<sup>26</sup> and have sought arbitration under their labor agreements. While the litigation is far from over, and no one would be presumptuous enough to predict the outcome, Stockton's circumstances involve many aspects of what, presumably, should constitute a true fiscal emergency. Based on its history of cost-cutting, the city had few alternatives, and the few it had – primarily cutting additional police officers – were unquestionably dangerous to the public health, safety and welfare. Stockton attempted to work with the unions and to find alternatives, but the unions would only agree to alternatives if the city agreed to extend the untenable labor agreements even further into the future. The city had even attempted to raise revenues, but lost at the polls.

In the fire arbitration, the lead case in Stockton, the firefighters have argued that the city could have raided the workers' compensation fund and other special funds, sold property, eliminated its two assistant city managers, and taken similar short-term steps that, it asserts, might have gotten it through the 2010-11 fiscal year. While the city has argued that, at best, these would have only delayed the inevitable, the union's financial expert has countered: "Frankly, kicking a can down the road is a perfectly acceptable practice in public sector budgeting." It is precisely this kind of myopic thinking that helped develop this problem in the first place.

**OPTIONS FOR AVOIDING FISCAL EMERGENCIES BEFORE THEY HAPPEN**

The effects of the Great Recession will linger for most California cities and counties, and the cost of employee and retiree benefits will soar. Plainly, some jurisdictions will face insolvency. But the question remains whether, for some, declaring a fiscal emergency is a reasonable last resort before bankruptcy. Many other states have specific provisions for dealing with local fiscal emergencies. Most, however, turn local control over to the state. That hardly seems like a good or workable solution for California jurisdictions, where the state's fiscal management makes even the worst-run local governments look like pillars of financial rectitude.

Another alternative is to address the possibility of uncertain financial futures in the collective bargaining agreements themselves. For instance, public

agencies could attempt to negotiate provisions that preclude increases in salaries where the funds have not been certified as available in the budget or by supplemental appropriation. Provisions allowing temporary suspension of cost-of-living adjustments, or requiring temporary increases in employee participation in funding health and pension benefits – or at the very least, permitting a more streamlined process for negotiating such temporary changes with the unions – may prove to be a viable option for some agencies. Public agencies also may wish to coordinate their agreements so that they come up for renewal at the same time, thus avoiding additional – and unforeseeable – future financial problems.

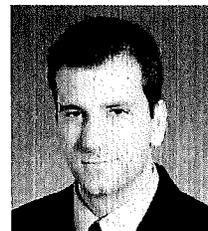
In the meantime, stay tuned. A lot of law on fiscal emergencies is likely to get made in the next few years.



Jonathan V. Holtzman



K. Scott Dickey



Steve Cikes

\* Jonathan V. Holtzman is a founding partner of Renne Sloan Holtzman Sakai LLP, the Public Law Group. He represents local public entities and non-profits across California in labor and employment negotiations and on issues of Government Law. K. Scott Dickey and Steve Cikes are senior counsel with the firm. They represent cities, counties, school districts, and non-profits on a broad range of public sector law issues.

**Endnotes**

- 1 Incorporated into the California Constitution as Article 13A. See [http://www.leginfo.ca.gov/.const/.article\\_13A](http://www.leginfo.ca.gov/.const/.article_13A).
- 2 Article I, section 10 of the United States Constitution, known as the "Contract Clause," states that "[n]o State shall ... pass any ... [l]aw impairing the Obligation of Contracts." Article I, section 9 of the California Constitution similarly provides that a "law impairing the obligations of contracts may not be passed."
- 3 *Manigault v. Springs*, 199 U.S. 473, 480 (1905); see also *Hudson Water Co. v.*

- 4 *McCarter*, 209 U.S. 349, 357 (1908) (Justice Holmes, writing for the Court, stated: "One whose rights, such as they are, are subject to state restriction, cannot remove them from the power of the State by making a contract about them. The contract will carry with it the infirmity of the subject matter.")
- 5 290 U.S. 473 (1937).
- 6 *Id.* at 439.
- 7 310 U.S. 32 (1940).
- 8 *Id.* at 38-39.
- 9 23 Cal. 3d 296 (1979).
- 10 See *Veix, supra*, 310 U.S. at 39-40 (recognizing that an emergency need not be declared and relief measures need not be temporary for an impairment to be deemed constitutional).
- 11 431 U.S. 1 (1977).
- 12 *Id.* at 23 n.19.
- 13 *Id.* at 25.
- 14 See *University of Hawaii Professional Assembly v. Cayetano*, 183 F.3d 1096, 1106 (9th Cir. 1999) (quoting *Condell v. Bress*, 983 F.2d 415, 418 (2d Cir. 1993) ("Courts are less deferential to a state's judgment of reasonableness and necessity when a state's legislation is self-serving and impairs the obligations of its own contracts.") (emphasis in original)).
- 15 *Buffalo Teachers Federation v. Tobe*, 464 F.3d 362, 371 (2d Cir. 2006) (quoting *United States Trust Co. of New Jersey*, 431 U.S. at 30-31).
- 16 44 N.Y.2d 101 (1978).
- 17 *Id.* at 111 n.3.
- 18 6 F.3d 1012 (4th Cir. 1993).
- 19 464 F.3d 362 (2d Cir. 2006).
- 20 23 Cal. 3d at 310-312.
- 21 *Id.*
- 22 983 F.2d 415 (2d Cir. 1993).
- 23 *Id.* at 419-420.
- 24 183 F.3d 1096 (9th Cir. 1999).
- 25 *Id.* at 1107.
- 26 See the staff reports at <http://www.stocktongov.com/clerk/granicusagendas/citycouncil/20100622.pdf>.
- 27 See *Stockton Firefighters' Local 456, Intl. Assn. of Firefighters v. City of Stockton*, San Joaquin County Superior Court Case No. 39-2010-00244326 CU-PT-STK; *Stockton Police Officers' Assn. v. City of Stockton*, San Joaquin County Superior Court Case No. 39-2010-00245197 CU-WM-STK.



# Memorandum

**TO:** HONORABLE MAYOR AND  
CITY COUNCIL

**FROM:** Councilmember  
Donald Rocha

**SUBJECT:** RETIREMENT REFORM

**DATE:** May 20, 2011

Approved

*Don Rocha*

Date

*5/20/11*

## INTRODUCTION

I offer this memorandum as an additional proposal to address the grave structural problems of our retirement system. I agree with some aspects of the memo authored by the Mayor, Vice Mayor and Councilmembers Herrera and Liccardo on this subject, and welcome their direct offer, as stated in their memo, to “engage constructively with alternative solutions.” In that spirit, I propose an alternative solution that I would like staff to analyze. My preference is to avoid as much legal risk and financial loss as possible. We have a potential opportunity for real and responsible fiscal reform and time is of the essence given our current budget situation. It is in our best interest to pursue policies that are most likely to succeed, and proposing government-by-formula charter amendments of the sort that have made California very difficult to govern is not a path I wish to see for the City of San Jose. Therefore, I propose that we adopt the City Manager’s Fiscal Reform plan, with the amendment that we direct staff to prepare both the alternative proposed in my colleague’s memo and the alternative I propose in this memo for side-by-side comparison at the Council’s June 21<sup>st</sup> meeting.

## RECOMMENDATION

Approve the City Manager’s Fiscal Reform Plan, with the amendment that staff be directed to bring back: (1) the proposal recommended in the May 13<sup>th</sup> memo issued by my colleagues and (2) my proposal, described below, for side-by-side consideration at the Council’s June 21<sup>st</sup> meeting.

### **1. First Tier Retirement Reform for Actives**

Direct the City Manager, in consultation with the Retirement Services Director, to design a 2<sup>nd</sup> tier opt-in proposal for the 2<sup>nd</sup> tier plan outlined in Recommendation 3. Such a plan should:

- a. Evaluate the full range of mechanisms by which the City can influence employees to opt into the 2<sup>nd</sup> tier.
- b. Make a proposal as to how 1<sup>st</sup> tier benefits would be treated when an employee opts into the 2<sup>nd</sup> tier.
- c. Make best efforts to gauge potential opt-in cost savings for the 2<sup>nd</sup> tier option discussed in Recommendation 3, similar to the analysis of opt-in cost savings provided in the staff presentation at the May 18<sup>th</sup> budget study session.
- d. Prioritize policy alternatives that minimize legal risk.

**2. First Tier Retirement Reform for Current and Future Retirees**

Direct the City Manager and City Attorney to develop a proposal for changes for current and future 1<sup>st</sup> tier retirees as follows:

- a. Bring forward an amendment to City ordinance that reduces the Cost of Living Adjustment (COLA) to a fixed 1.5% per year increase.
- b. Report back to Council as to whether, other than the COLA, there are benefit enhancements awarded to retirees after the date of retirement that could be rolled back in order to reduce pension costs.

**3. Second Tier Retirement System**

Direct the City Manager to develop cost estimates for 2<sup>nd</sup> tier defined benefit retirement plans. Cost estimates should be provided for both Federated and Police and Fire Retirement Plans based on the below defined benefit plan framework. For each plan, staff should develop two cost estimates, one assuming investment returns with a 50% likelihood of success, and one assuming 75%.

Benefit	Recommendation
Retirement Age	<u>Federated</u> : 62 <u>Public Safety</u> : 57
Early Retirement Reductions	Allow early retirement provided that the benefit does not exceed the actuarial value of full retirement.
Formula	<u>Federated</u> : 2% per year of service for 30 years, to a maximum of 60% of final salary <u>Public Safety</u> : 2½% per year of service for 30 years, to a maximum of 70% of final salary
COLA	Tied to Bay Area CPI and capped at 1.5%
City/Employee Share of Costs	50/50 split for 2 <sup>nd</sup> tier normal costs and unfunded liability
Final Salary	Final 3 year average
Health Care	Employees receive a fixed dollar amount for retiree healthcare costs based on how many years of service they have when they retire (as recommended by staff in the last paragraph of page 41 of MBA #1).
Service Credit	Change the definition of one year of service from 1739 pensionable hours to the number of hours typical Federated and typical Public Safety full time employees work per year.
Opt-in	Design an opt-in program for 1 <sup>st</sup> tier employees and make best efforts to analyze potential opt-in cost savings, as outlined in Recommendation 1.

#### 4. **Analysis of CALPERS Alternative**

Direct staff to contact CALPERS and bring back to the Council the various options available for a current member agency to opt into the CALPERS system with the associated costs and projected savings from the various options.

### **ANALYSIS**

#### **First Tier Reform for Actives**

I believe that an opt-in approach to 1<sup>st</sup> tier reform is a more certain path to budget savings than pursuing potentially vested 1<sup>st</sup> tier benefit reductions through a ballot measure and expected court challenge. It's impossible to know the outcome of a court case, but we do know that a ruling against the City would wipe out planned budget savings and put us back to square one. I'm not ready to gamble the City's future on a court battle. An opt-in system that gives employees incentives to choose the 2<sup>nd</sup> tier—as well as some disincentives to stay in the 1<sup>st</sup>—has the potential to deliver significant budget savings without a lengthy and costly legal dispute.

#### **First Tier Reform for Current and Future Retirees**

Unfortunately, in the case of 1<sup>st</sup> tier retirees, we don't have the opportunity to pursue an opt-in system. With no better option in front of us, I agree with my colleagues that we need to reduce the COLA, and in addition consider rolling back other benefits awarded after the date of retirement. Reducing the COLA isn't fair to retirees, I agree, but neither is reducing or eliminating services that the public has invested in and that have public health and safety implications. San Jose can continue to be a great city, but for that to happen, all of us must make some sacrifice—taxpayers, employees, and retirees alike.

I recommend we pursue a COLA change by ordinance instead of at the ballot. If the Council can accomplish the change on its own, I don't believe that we should spend money on an election, especially when we already have a mandate from the public for reform. If for some reason it is not possible to make this change by ordinance, I would support consideration of a ballot measure as suggested by my colleagues.

#### **Second Tier Option**

We have the opportunity, and I would argue the responsibility, to direct our staff to develop information on a range of viable options before choosing a course of action. At the May 18<sup>th</sup> study session, I made the case for consideration of multiple policy options before making a decision, and the City Manager offered this Council meeting as the venue to make that request. In that spirit, I propose directing staff to return with information on a defined benefit retirement system.

For the defined benefit system, I propose a list of plan criteria and request that staff cost out the proposal. In starting with plan design and working to cost, I'm reversing staff's usual approach of starting with cost and working towards plan design. This approach is intentional: only focusing on cost is just as one-dimensional as focusing only on benefits. As an employer, we must consider both—we need a plan we can afford, but also one that offers a livable retirement. Costing out reduced, but still reasonable benefits, will provide the Council with a useful data point to guide well-informed decision making.

I also ask that staff investigate the idea of opting into CALPERS. As a current member agency (Mayor and City Council are members of CALPERS) we should explore the potential savings of joining that retirement system.

### **Section C of My Colleagues' Memo**

As I hope I have shown in the above recommendations, I have made an honest attempt to incorporate recommendations made by my colleagues and craft a true compromise. However, I want to take a moment to voice my strongest possible disagreement with Section C of their memo. This section would implement government by formula in San Jose, preventing elected officials from making even the most basic decisions necessary to govern the City. The restrictions are referred to as temporary, but the language is written such that the temporary circumstance could persist for decades. The most concerning provision, item c, would prevent the Council from raising pay for members of any bargaining unit. Determining employee pay is one of the most basic functions of governance; if we give up that responsibility, we give up the job we were elected to perform. Successful representative democracy depends on publicly accountable elected officials who can exercise judgment under complex circumstances. Again, the State of California is a living example of the dysfunction that can result when we take away the ability of elected officials to govern basic functions and operations.

### **Conclusion**

We all recognize the unique position that we as elected officials find ourselves in. While balancing the needs of our residents with the need to value the employees who contribute to the service of those community needs, we have an opportunity to rebuild a broken system, and to do so with vision, dignity, and effective discourse. Fiscal reforms, if done correctly, will ensure that our City functions efficiently during any economic situation, good or bad. In my opinion, this option includes significant fiscal reform measures, and I appreciate the Mayor, fellow Councilmembers, and the City Manager for their leadership and commitment to this effort as priority number one for San Jose and its residents.

As policy makers we strive to make the best and most effective policies into realities for our community. I am concerned that if we limit the pool of options that we make those decisions from, we limit our ability to make a decision with all options considered. It is for that reason that I am asking us to bring forward an additional course of action as an option for Council consideration. The attached chart is provided as a convenient way of comparing my recommendations to the ones made in the May 13<sup>th</sup> memo.

# Reform Recommendations and Analysis

## 1<sup>st</sup> Tier Actives

Sec.	May 13 memo Recommendation	Sec.	Proposed Alternative
A	Attempt to alter or take away vested rights through a Charter amendment	1	Design opt-in system for existing employees to transition into the 2 <sup>nd</sup> tier system

## 1<sup>st</sup> Tier Retirees

Sec.	May 13 memo Recommendation	Sec.	Proposed Alternative
B3	COLA tied to CPI and capped at 1%	2	COLA fixed at 1.5%

## 2<sup>nd</sup> Tier

Benefit	Sec.	May 13 memo Recommendation	Sec	Proposed Alternative <small>(Note: for further study and cost analysis)</small>
Retirement Age	B1	Federated: 65 PS: 60	3	Federated: 62 PS: 57
Early Retirement Reductions	B1	Early retirement may be permitted with reduced payments that do not exceed the actuarial value of full retirement.	3	Accept memo recommendation
Formula	B2	No level specified	3	Federated: 2% per year of service for 30 years, to a maximum of 60% of final salary Public Safety: 2 1/3% per year of service for 30 years, to a maximum of 70% of final salary
COLA	B3	Tier 2: No level specified Tier 1: Capped at 1% and tied to CPI	3	Tied to Bay Area CPI and capped at 1.5%

## Reform Recommendations and Analysis

Benefit	Sec.	May 13 memo Recommendation	Sec	Proposed Alternative <small>(Note: for further study and cost analysis)</small>
Share of Normal Costs	4E	50/50	3	50/50 split for 2 <sup>nd</sup> tier normal costs and unfunded liability
Pension Amount		No level specified	3	Final 3 year average
Health Care	B2	20 year vesting	3	Employees receive a fixed dollar amount for retiree healthcare costs based on how many years of service they have when they retire (as recommended by staff in the last paragraph of page 41 of MBA #1)
Service Credit	--	No level specified	3	Change the definition of one year of service from 1739 pensional hours to the number of hours typical Federated and typical Public Safety full time employees work per year.
Additional limitations	4a-e	Adopt Charter-level benefits for Tier 1 employees who have not opted into Tier 2 if the unfunded liability surpasses 6/30/10 levels	1	Pursue opt-in approach
Implementation Provisions	C	Require voter approval of increases in other benefits until essential services have been restored	--	Reject



# Memorandum

**TO:** HONORABLE MAYOR AND  
CITY COUNCIL

**FROM:** COUNCILMEMBER  
NANCY PYLE

**SUBJECT:** CITY MANAGER'S FISCAL  
REFORM PLAN

**DATE:** May 23, 2011

**APPROVED:**

**DATE:**

5/23/11

**RECOMMENDATION:**

If the Council decides to pursue a ballot measure in November 2011, I recommend that we also look at ways to quickly bring in more much needed revenue to the city. My recommendation is to modernize a small portion of the City's Business Tax structure to reflect the conversion of traditionally used retail space to space for businesses offering personal services which are not subject to sales tax.

Direct the City Manager to return to Council on June 21 with a further staff analysis on this proposal.

If Council decides consider this modification to the Business Tax, the City Manager should poll the public to gauge public support for changing the business tax structure for businesses offering personal services so that the business tax is based upon gross receipts instead of number of employees. The poll should also include questions gauging the level of support for a business tax of 1%, 1.5%, 2%.

As a point of reference, a 1% business tax is equivalent to the amount the City would have received if normal sales taxes were collected. A 1.5% tax would be 30 cents on a \$20 haircut, and a 2% tax would be 40 cents on a \$20 haircut.

The polling results should be presented to Council and included in any Council discussion regarding ballot measures for pension or fiscal reform in November 2011.

**BACKGROUND:**

There is no question that the sales tax structure has dramatically changed with the popularity of internet sales. Small businesses that used to occupy our neighborhood shopping centers are forced to compete with both the convenience and the ability of consumers to avoid paying sales tax on most internet based sales. As a result, many of these small retail businesses closed and created vacancies in our neighborhood shopping centers.

At the same time, businesses offering personal services have exploded in popularity and have quickly filled our neighborhood and regional shopping centers. Businesses offering personal services like manicures and pedicures, tattooing, hair styling, spa services (including massage,

tanning, facials and other beauty treatments), pet daycare, educational tutoring and education enrichment services (i.e. art, language and music) currently occupy space traditionally occupied

by retail establishments selling goods subject to sales tax, not space for businesses offering tax exempt personal services. While these are desirable services to our residents, they occupy space designed to be sales tax generating.

Instead of playing the waiting game and hoping that other government agencies will wrestle with the complicated tax issues regarding our change to a service based economy and tax free internet sales, we have the ability to ask our residents make changes to our business tax now. Structuring the business tax on personal service providers as a small percentage of gross receipts will provide these small businesses the ability to cover the tax in a way that everyone is familiar with. We all understand the concept of a sales tax which applies the same rate to all goods regardless of the cost. The proposed gross receipts tax would operate the same way and will apply to all personal service providers regardless of the amount of services they provide.

Other jurisdictions have adopted a similar process. Basing a Business Tax upon gross receipts is the current policy in the city of Los Angeles, Oakland, Pleasanton and Alameda County.

Given that these are personal services, and the value to the business is their location near their client base, any concern with these businesses relocating to another city should only be a mild consideration.



# Memorandum

**TO:** HONORABLE MAYOR AND  
CITY COUNCIL

**FROM:** Debra Figone

**SUBJECT:** SEE BELOW

**DATE:** July 22, 2011

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**SUBJECT: DISCUSSION OF BALLOT MEASURE POLLING RESULTS, DISCUSSION OF STATE BUDGET IMPACTS, UPDATES ON DISCUSSIONS OF BALLOT MEASURE LANGUAGE AND RETIREMENT REFORM NEGOTIATIONS, DEFERRAL OF DECLARATION OF FISCAL AND PUBLIC SAFETY EMERGENCY AND DEFERRAL OF DISCUSSION OF POSSIBLE DRAFT BALLOT LANGUAGE.**

## RECOMMENDATION

- (a) Discussion regarding ballot measure polling results and direction on revenue measures.
- (b) Discussion of state budget impacts.
- (c) Update regarding status of discussions on ballot measure language and retirement reform negotiations with the City's bargaining units.
- (d) Defer to September 20th, discussion and consideration of declaration of a Fiscal and Public Safety Emergency.
- (e) Defer discussion of possible draft ballot language for ballot measures allowing the residents of San José to vote on proposed changes to the Charter.

## BACKGROUND

On June 24, 2011, the City Council directed Staff to return on August 2, 2011, with the above items. This memo is to advise the City Council that on August 2, 2011, Staff will be providing the City Council with updated information related to:

- 1. Labor negotiations
- 2. State budget actions
- 3. Ballot measure polling results

Staff will structure the presentations to facilitate actions related to any or all of the above. In addition, a memorandum on Item 3.5(a) will be distributed prior to August 2, 2011.

## CEQA

CEQA: Not a Project, File No. PP10-068(b), General Procedure and Policy Making, Municipal Code Title 3.

  
DEBRA FIGONE  
CITY MANAGER



# Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Councilmember Sam Liccardo

SUBJECT: SEE BELOW

DATE: August 1, 2011

APPROVED:

8-1-11

**SUBJECT: DISCUSSION OF BALLOT MEASURE POLLING RESULTS, UPDATES ON STATE BUDGET IMPACTS, UPDATES ON DISCUSSION OF BALLOT MEASURE LANGUAGE AND RETIREMENT REFORM NEGOTIATIONS, DEFERRAL OF DECLARATION OF FISCAL AND PUBLIC SAFETY EMERGENCY AND DEFERRAL OF DISCUSSION OF POSSIBLE DRAFT BALLOT LANGUAGE.**

## Recommendation

Accept Staff Recommendations, with the additional recommendation to decline going to the November 2011 ballot with any revenue-raising measure.

## Analysis

The City Manager's analysis of our very limited options to restore the severely reduced city services to our residents included consideration of various revenue-raising measures. Assessing the likelihood of passage of those measures appears integral to focusing our strategy for the year ahead, a year in which we should anticipate another \$100 million hole in the General Fund, after adjustments to retirement plan assumptions have taken effect.

Residents polled by the firm of FM3 have indicated tepid, or worse, support for tax increases. Despite the improving performance of the Valley's high-tech companies, our residents continue to suffer through a severe economic storm, characterized by ongoing double-digit unemployment and bankruptcies in their households and businesses. Although some have criticized the language of the questioning in the poll, City staff reached out to the Chamber of Commerce, South Bay Labor, and the Silicon Valley Leadership Group in advance. Moreover, leaders of both of our Police and Fire unions were provided with drafts of the polling language, and were solicited for their input.

Accordingly, we should turn our focus to the hard work before us: retirement benefits reform. Only through substantial cost reductions can we move into the following fiscal year without another spell of severe layoffs and service cuts.