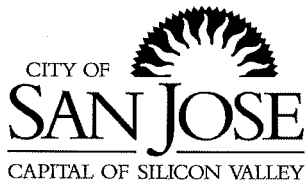
COUNCIL AGENDA: 12-06-11
ITEM: 3.3



Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Debra Figone

SUBJECT: **DECLARATION OF FISCAL AND SERVICE LEVEL EMERGENCY**

DATE: November 22, 2011

RECOMMENDATION

1) Accept the attached *City of San Jose Fiscal & Service Level Emergency Report.*

2) Adopt a Resolution Declaring a Fiscal and Service Level Emergency based on the *City of San Jose Fiscal & Service Level Emergency Report*, including the findings set forth in the Resolution.

BACKGROUND

At the May 24, 2011 City Council meeting, the City Manager's *Fiscal Reform Plan* was agendized for discussion as item 3.4. In a memorandum dated May 13, 2011, Mayor Reed issued a memorandum, co-signed by councilmembers Nguyen, Herrera, and Liccardo, recommending that as part of this discussion, the City declare a fiscal and public safety emergency.

At the May 24th meeting, the Administration was directed to come back on June 21 with draft language relating to that declaration.

On June 15, 2011, the Rules and Open Government Committee moved the discussion to a special meeting on June 24, 2011.

On June 20, 2011, the Mayor issued a memorandum continuing discussion of a *Declaration of Fiscal Emergency* to the August 2, 2011 meeting.

At the August 2 meeting, the City Council approved a recommendation from the City Manager that consideration of a *Declaration of Fiscal Emergency* be deferred to September 20, 2011.

On September 1, 2011, after some of the City's bargaining groups agreed to a framework for bargaining over potential ballot measure language related to fiscal reforms, the Mayor issued a memorandum deferring consideration of a *Declaration of a Fiscal and Service Level Emergency* until after the October 31, 2011 deadline for those negotiations to conclude. The Rules and Open Government Committee approved the Mayor's recommendation on September 7, 2011.

On November 18, the Mayor issued a memo agendizing the *Declaration of a Fiscal and Service Level Emergency* for council consideration on December 6, 2011.

ANALYSIS

As the attached report demonstrates, the City of San Jose is in the midst of an unprecedented structural fiscal crisis caused by dramatically increasing retirement costs that have significantly degraded the City's ability to provide basic services to meet our residents' needs. The City faces a projected $80.5 million deficit in the coming fiscal year, with more than 60% of the deficit resulting directly from an increase in retirement costs. This is unsustainable. Unless the City acts now to reduce these costs, its only choice will be to further reduce services to unacceptable levels. Given the dramatic service reductions to date, further reductions of the magnitude necessary to pay retirement costs will cause the health, safety and well being of our residents to be placed at critical and unacceptable risk.

Given the critical nature of the City's fiscal situation, I am recommending that the City Council adopt the resolution declaring a Fiscal and Service Level Emergency.

DEBRA FIGONE
City Manager

FISCAL AND SERVICE LEVEL EMERGENCY REPORT

An evaluation of conditions
in the City of San José

November 22, 2011

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

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EXECUTIVE SUMMARY

San José faces a crisis. To address ten consecutive budget shortfalls over the past decade, the City has already cut staffing levels sharply, added new revenue sources, eroded reserves, and eliminated services and programs. Nonetheless, to correct for the City's further projected shortfalls over the years just ahead, the level of required cuts will render San José unable to provide even minimally acceptable services. For example, the City is faced with the unthinkable prospect of closing all of its branch libraries and community centers, while still not having enough money to fund acceptable levels of police and fire protection. This statement of crisis is not made lightly, but reflects the Administration's profound concern that San José faces a service-level emergency that can only be classified as a fiscal emergency.

While a number of factors have contributed to this crisis, by far the most significant and difficult to control has been the City's skyrocketing retirement costs. Over just the past two years (from fiscal years 2009-2010 to 2011-2012),[1] the City's budgeted share of annual required contributions for employee retirement benefits across all funds has risen from $133 million to $245 million.

As shown in the following chart, retirement costs are projected to rise from $245 million in 2011-2012 (already more than $100 million above the levels of just two years earlier) to $431 million in 2015-2016.[2] Thus, without corrective action, the City's retirement costs across all funds are projected to more than triple in over just five years.[3]

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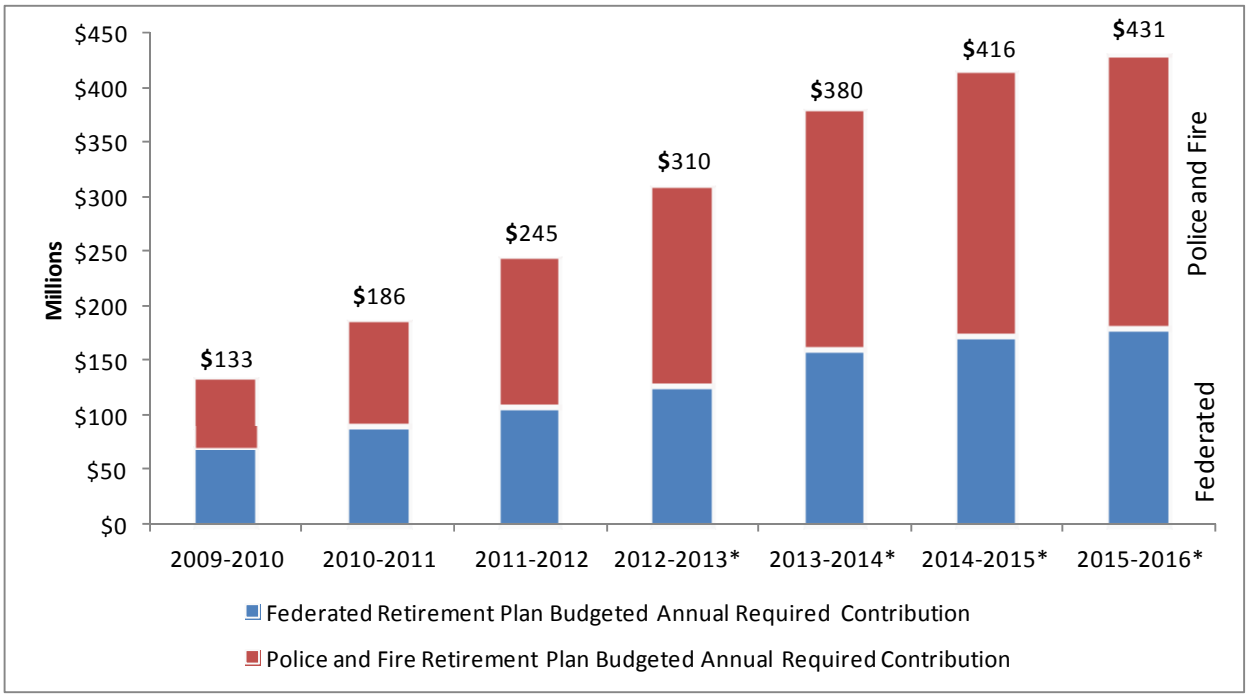
[1] Unless otherwise specified, date references such as "2009-2010" refer to fiscal year 2009-2010. The fiscal year runs from July 1 to June 30.

[2] This projection is provided by Cheiron, the actuary for the Retirement Boards. Please note that the Budget Office's calculation uses $416 million as the retirement cost projection for 2015-2016. This number was based on the Cheiron projection, but includes a prepayment discount that the City receives for the way it administers its retirement payments.

[3] Throughout this report two terms – "pension costs" and "retirement costs" – are used frequently. The term "pension costs" refers specifically to the costs associated with funding the City's two pension plans, but does not include the costs associated with retiree health and/or dental benefits. The term "retirement costs" includes both pension costs, as well as the cost of Other Post Employment Benefits (OPEB) including retiree medical and dental costs.

Past, Current, and Future Retirement Contributions for all funds for Pension and Retiree Health Care Costs (in Millions) [4] [5]



Sources: City of San José's Adopted Budgets 2009-2010 through 2011-2012 and Retirement System Comprehensive Annual Financial Reports, and Cheiron Memorandum dated July 20, 2011.
**forecasted retirement contribution; assumes no significant reform to retirement benefits.*

It should be noted that this report is a snapshot in time and contains data that is the best available data as this is written. Retirement valuations are completed on an annual basis and the data contained herein is primarily 2010 data because it is the only complete data set available at the time of publication. The information contained in this report, including the retirement projections, are updated annually and inevitably will change. At the time of publication, the Retirement Boards are in the process of adopting valuations as of June 30, 2011 that will impact contribution rates for 2012-

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[4] The 2011-2012 total of $186 million is prior to savings achieved by employees paying a portion of the City's share of retirement costs. With those concessions, the City's net share was $179 million.

[5] For 2012-2013, the ARC for the Federated Retirement Plan is based on the June 2011 preliminary valuation by Cheiron, the Federated Retirement Board's actuary, combined with the assumption changes approved by the Federated Retirement Board on October 20, 2011. For the Police and Fire Retirement Plan ARCs, these estimates were calculated by Cheiron, the Police and Fire Retirement Board's actuary, in July 2011. The required contribution related to retiree healthcare was calculated by the actuary in July 2011.

Note that the Budget Office applies a pre-payment discount to the forecasted contribution amounts provided by Cheiron. All budgetary contribution rates and ARCs are discounted because the City pre-paid and it is assumed will continue to pre-pay the full ARC at the beginning of each fiscal year. As such, in the Budget Section of this report, the $431 million valuation is discounted to $416 million.

2013, but they have not yet been finalized. Early indications are that these numbers may show some improvement due, in part, to slowing of the growth in liabilities due to salary reductions and position eliminations. However, the tentative information available to the City at the time of publication is that the degree of improvement will not change the dire circumstances facing the City.

The primary focus of this report is on the City's General Fund, which supports the great majority of municipal services. However, the impact of escalating retirement costs affects all City funds and services. As the retirement cost burden escalates, it drives up the cost for sewer services, the San José/Santa Clara Water Pollution Control Plant, Special Purpose Funds, the Development Fee Program, and other special funded services paid by every resident through monthly fees and other direct assessments.

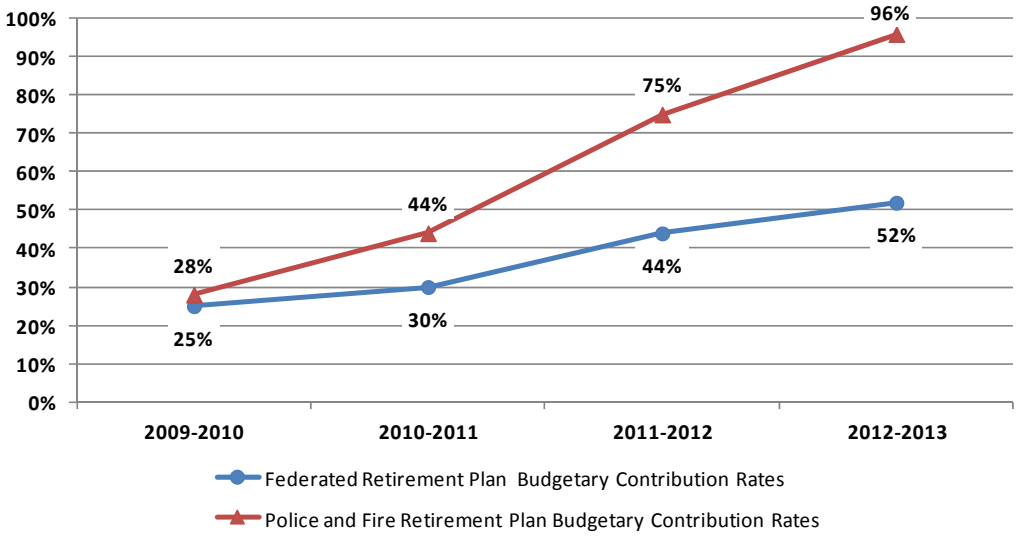
The only way to eliminate a General Fund shortfall is to increase revenues or cut costs. With local voter reluctance to increased taxes, as indicated in polling data, the City's revenue generation options are significantly limited by required majority voter approval (50%+1) for general taxes and two-thirds voter approval for service-specific taxes.

On the expenditure side of the budget, with nearly two-thirds of spending dedicated to employee wages and benefits, achieving sufficient cost containment requires reducing the number of employees and/or reducing the cost for each individual employee. In recent years, the City has already reduced total compensation for all current employees by 10%, made other cost containment measures to control employee costs such as health care changes, and cut the number of employees to the point where basic municipal services are at risk. Since 2008-2009, the City has reduced its sworn police force – already one of the nation's most lightly staffed – by 308 officers, or 22% of the sworn force. Overall, the City has cut General Fund staffing by 1,134 budgeted positions, or 23% since 2008-2009. San José now has its lowest staffing level since 1988-1989, despite population growth over the more than two decades since of nearly 200,000, an increase of more than 25%.

Even after these considerable headcount reductions, and numerous other cost-reduction strategies implemented by the City to address past budget gaps, the General Fund shortfall for 2012-2013 is preliminarily projected at $80.5 million, which represents 9.2% of total projected General Fund Expenditures for the coming fiscal year. Of this shortfall, the primary factor is a projected $50.3 million increase in retirement costs.

The following chart further illustrates the degree to which these costs are increasing at unsustainable rates, presenting the City's pension and retiree healthcare contributions as a percentage of payroll.

Retirement Contribution Rates as a Percent of Payroll or Annual Required Contribution for Pension and Retiree Health Care Costs



Source: City Manager's Budget Office.

As a result of these trends, retirement costs are consuming progressively larger portions of the City's operating budget. Expressed as a percentage of total General Fund Expenditures, retirement costs have risen from 9.9% in 2007-2008 to 21.8% by 2011-2012. Without significant reform to the City's pension and retiree healthcare benefits, these numbers are projected to reach 30.3% of the General Fund by 2015-2016.

In 2000-2001, City retirement contribution rates (including both pension and OPEB) were 16% of pay for Federated employees and more than 15% for Police and Fire. As shown above, in 2012-2013, the City projects that in addition to its direct payroll costs for employees in the Federated Retirement Plan, it will pay an additional 52% toward pension and retiree healthcare. For public safety employees in the Police and Fire Retirement Plan, the City will pay an additional 96% of payroll for retirement benefits. Along with active (i.e., pre-retirement) employee healthcare and other benefits, the City's total cost for a sworn police officer making on average $108,000 will be over $225,000, of which over $103,000 will be the City's contribution to the retirement costs.

Without retirement reform, the choices facing the City in order to balance the 2012-2013 budget have become both stark and unacceptable. To protect public safety as much as possible, the City will first look to all other departments and service areas for savings. Under a likely budget balancing scenario, this would require the City to close most branch libraries by 2013-2014 and all remaining branch libraries by 2014-2015. These branches are a vital service utilized by nearly 4.5 million visitors annually. It will also mean the closure of virtually all City-run recreation programs and centers. Park Rangers will be eliminated. Anti-gang activities, along with graffiti abatement and general code

enforcement, will be reduced to skeletal levels. Street light and traffic maintenance programs, along with pavement maintenance and landscape services will all be reduced below the current bare-bones levels. General Government departments such as Finance, Human Resources, and Information Technology, without which the direct services departments cannot function, will be further devastated despite having already suffered years of difficult cuts.

And even after all of these and other difficult reduction decisions are made, the City Council will still face the unfathomable prospect of cutting more from the public safety budget beyond what has already been cut, likely in the range of $16 million. With Police and Fire Department staffing further reduced, fire response times are expected to rise to more than 10 minutes, well above the current 8 minute standard (which is already higher than the nationally recognized standard). In addition, the City will not be able to provide paramedic services that meet county standards, and the Police Department will be unable to respond in a timely fashion, if at all, to anything except for the highest priority emergencies. These results will be devastating to the fabric of San José, and will make our City a far less desirable place in which to live or locate a business. We must arrest this decline immediately.

Unfortunately, there is no "silver bullet" for containing the alarming increases in the City's retirement costs. The rapid increase in costs is primarily due to a reduction in the funded status of the City's pension plans. That reduction is the result of several factors including:

(1) significant increases in benefits beyond the Charter minimums, including supplemental benefits and increased COLAs for retirees, which were not paid for during the working lives of employees receiving benefits;

(2) enormous investment losses, leading to a failure to meet earnings expectations on plan assets;

(3) actuarial losses and changes in actuarial assumptions based on experience, including increased longevity; and

(4) a dramatic increase in the number of retirees and the size of their pensions.

Retirement funds have three main sources of revenue: contributions from the City, contributions from employees, and earnings achieved by investing the money in the funds. Even if all other factors remained the same, the pension plans have relied upon earning at least 7.75% on their investments each and every year to fund the plans' on-going obligations. During the Great Recession, the City's pension plans actually lost $979 million in calendar years 2008 and 2009 – falling more than 36% below their assumed earnings. Although these losses are "smoothed" over five years, and earnings over the last two years have exceeded expectations, the plans' earnings over the last five years remain far below the expected returns. In addition, the plans have consistently paid out more than they have taken in over the last ten years, in part resulting from the failure to realize other actuarial assumptions. Overall, the Federated Plan has gone from being 104% funded in 2001 to having a

funded ratio of 60% based on market value as of June 30, 2010 (this also incorporates more prudent discount rate assumptions adopted by the Federated Plan trustees). Similarly, the Police and Fire Plan has gone from being 111% funded in 2001 to 69% funded based on market value as of June 30, 2010.

The Fiscal Reform Plan adopted by the City Council in May 2011 contemplates a range of potential solutions to address the General Fund structural imbalance and to restore essential City services that have been recently reduced or eliminated. These strategies are being actively pursued, and include but are not limited to creating a second tier retirement program, investigating raising the City sales tax, reducing retiree medical costs by adopting a lower cost plan, eliminating sick leave payouts, and eliminating the Supplemental Retiree Benefit Reserve (SRBR). Unfortunately, these solutions alone are not projected to be sufficient. Although the City has been successful in achieving some cost reductions, other City proposals will require further collective bargaining with its employee bargaining units and, in some instances, Charter changes via the electoral process. Further, while additional revenue would be very beneficial, increasing revenue rates and/or sources will, again, require a vote of the people, and polling indicates that approval remains doubtful in the current economic environment.

Given all of the above constraints, some have suggested that the City should simply take actions to defer recognition of the problem, such as changing the actuarial assumptions and methodologies used by the retirement boards to "engineer" lower City retirement payments. Unless there is a specific and sound actuarial basis for changing such assumptions, however, this approach could jeopardize the long-term sustainability of the plans. It is important to note that the City's retirement boards are independent and have fiduciary obligations. These boards are composed of employees, retirees, and independent trustees. To date, they have prudently chosen not to adopt changes such as increasing the "smoothing period," and increasing the amortization period, which would only increase what the City ultimately will owe and further undermine the soundness of the plans.

As a result, the City must now address its retirement costs. Because of the unsustainable growth in these costs, San José faces a service-level emergency.

RECOMMENDATION

The outlook for City services, already seriously reduced over the last three years because of skyrocketing pension costs and the severe economic downturn, remains bleak for 2012-2013 and beyond. While the City has been managing deficits since the dot.com bust in 2001, the shortfalls in recent years have become increasingly difficult to resolve as wave after wave of difficult cuts have already been made. The Administration believes that the next round of service cuts required to balance the budget in the face of such a severe deficit will create a service-level emergency. For that reason, the Administration recommends that the City Council adopt a resolution of fiscal emergency based upon the need to find and implement solutions that may require the exercise of the City Council's emergency powers. This report sets forth the basis for such an emergency.

I. FISCAL EMERGENCY

A. What is the Purpose of a City?

The City of San José prides itself on being a city with a long tradition of fiscal prudence and good management. In particular, the City is struggling to balance its budget amid weakened revenues and rising costs, including rapidly-increasing personnel costs. The City is a service organization with approximately two-thirds of the City's General Fund budget attributable to personnel costs.[6] Unlike a private employer, a public agency cannot simply decide to go "out of business" or otherwise stop providing certain essential services to the public.

Under the California Constitution, cities have broad authority and responsibility in the areas of public health and safety. See Cal. Const., Art. XI, § 7 ("A county or city may make and enforce within its limits all local, police, sanitary, and other ordinances and regulations not in conflict with general laws."). However, while a city's powers are derived from the state constitution and other laws enacted by the Legislature, cities themselves are created only by the request and consent of the residents in a given area. Because of this, municipal governments are responsible for providing services that directly affect the lives of their residents. Through fire and police protection, cities safeguard lives and property. Through public works and other programs, cities construct and maintain streets and look after the health, recreational, and social needs of residents. Charter cities like San José are formed when citizens specifically frame and adopt a charter to establish the organization of and basic laws of the city.

The core purpose of the City of San José is to provide essential services to the public as established in its City Charter. San José's essential functions are set forth in its Charter, which identifies the establishment of certain City Departments including Police, Fire, Public Works, Parks and Recreation, Personnel, Planning, Finance, and Library. See San José City Charter, Sections 806 and 807(a). Notably, although the City Council may at any time abolish or discontinue some departments, the City Council is required to provide those departments and services established under the Charter. See City Charter, Section 800.

B. A Service Level Emergency Creates a Fiscal Emergency

In fulfilling its core purpose of providing essential services, the City must navigate between City Charter requirements and City Council mandates. On the one hand, the City Charter establishes departments as set forth in the paragraph above for the purpose of providing basic municipal services. See generally, City Charter Sections 806 and 807. Further, the City Council established the service levels as of January 1, 2011 as the minimum baseline service level for City residents. See Appendix C for a description of the Baseline Service Level.

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[6] Based on the 2011-2012 Adopted Operating Budget.

On the other hand, the City Charter requires the City to balance its annual budget. See City Charter, Section 1205. The City has been, up to this point, fortunate enough to be able to comply with both of these City Charter mandates and provide basic municipal services to City residents. Unfortunately, on July 1, 2011, the City Council was forced to reduce services below those levels acknowledged by the City Council as the baseline for basic municipal services in order to balance its annual budget for 2011-2012. All projections show that the crisis will deepen profoundly and additional cuts will be required to balance the upcoming 2012-2013 budget, as required by the Charter.

The meaning of the term "emergency" may vary depending on the context in which it is used.[7] While some courts have defined an "emergency" as "an unforeseen situation calling for immediate action," not all emergencies occur in an instant, like an earthquake. An employer's dire financial condition – which worsens over a period of time – may qualify as an emergency justifying the suspension or modification of certain contractual obligations.

A public agency's inability to provide essential services is a strong indication of a fiscal emergency. As noted by the Governmental Accounting Standards Board (GASB), the common themes that have been either formalized or are working definitions of financial sustainability include the ability to continue public services and/or existing programs.[8] This comports with the definition of "financial condition" adopted by the International City/County Management Association (ICMA).[9] In particular, ICMA defines a municipality's financial condition as the ability to (1) maintain existing service levels, (2) withstand local and regional economic disruptions, and (3) meet the demands of natural growth, decline, and change. ICMA also categorizes financial solvency in four distinct ways:

1. ***Cash solvency*:** government's ability to generate enough cash over a 30 to 60 day period to meet its obligations.

2. ***Budgetary solvency*:** government's ability to generate enough revenues over its normal budgetary process to meet its expenditures and not incur deficits.

3. ***Long-run solvency*:** government's ability to meet expenditures that may not be addressed as part of normal recurring annual budgetary process.

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[7] For example, in a recent opinion letter, the Legislative Counsel stated that the City's current fiscal crisis does not constitute a "local emergency" within the meaning of California Emergency Services Act ("CESA") (Gov. Code § 8550 et seq.). CESA is intended to address the effects of natural, man-made or war-caused emergencies on a local agency, according to the Legislative Counsel. To be clear, the City does not rely upon CESA as the basis for its authority to suspend and/or modify existing contractual obligations in order to cope with its current economic crisis. Rather, as discussed in the Legal Authority section that follows, that authority stems from the City's inherent authority to act in the public's interest to preserve the health, safety and well-being of City residents.

[8] Government Accounting Standard Board, Economic Condition Reporting: Fiscal Sustainability.

[9] Evaluating Financial Condition – A Handbook for Local Government, International City/County Management Association, 4th ed., 1986.

4. ***Service-level solvency*:** government's ability to provide services at the level and quality that are required for health, safety, and welfare of the community and its citizens desires.

This report focuses on the last category: whether the City is able to provide services at the level and quality that are required for health, safety, and welfare of the community and its citizens desires. As a well-run and forward-looking City, San José will budget to avoid a fiscal default because it maintains reserves and ensures that budgetary shortfalls are addressed through balancing actions each year. However, the City has reached the point at which those budget balancing actions combined with the budgetary outlook for 2012-2013 and beyond have triggered a service-level emergency, jeopardizing the health and safety of San José's residents. The threat posed by continued service reductions is imminent, and despite all other measures taken to this point and those still to be implemented, no viable alternative sufficient to address this problem has been identified without major changes in the retirement system. As such, the Administration believes San José faces a service-level emergency, a form of fiscal emergency.

C. Fiscal Emergency Legal Authority

It is important to recognize as an initial matter that the City Charter expressly reserves the right to make changes in benefits, consistent with the minimum benefits set forth in the Charter. Thus, it is possible that San José's pension benefits, particularly those outside of the minimum benefits in the City Charter, could be modified by the City so long as such modifications are not inconsistent with the Charter. Moreover, courts throughout the United States have held that in limited circumstances, legislative bodies may take emergency measures that would otherwise impair contract rights. In 1934, this principle was articulated by the United States Supreme Court in *Home Bldg. & Loan Assn. v. Blaisdell*, 290 U.S. 398 (1934) (hereafter "*Home Bldg & Loan*").

In *Home Bldg & Loan*, the Supreme Court considered the Minnesota Mortgage Moratorium Law, which authorized the lower court to extend the period of redemption from foreclosure sales "for such additional time as the court may deem just and equitable." The legislation was enacted in the midst of the Great Depression. The Supreme Court held that the legislation was valid even if a contract right was impaired. See also *Manigault v. Springs*, 199 U.S. 473, 480 (1905) ("It is the settled law of this court that the interdiction of statutes impairing the obligation of contracts does not prevent the State from exercising such powers as are vested in it for the promotion of the [benefit of the general public] or are necessary for the general good of the public, though contracts previously entered into between individuals may thereby be affected.").

The California Supreme Court follows the general standard established in *Home Bldg & Loan*. See *Sonoma County Org. of Public Employees v. County of Sonoma*, 23 Cal. 3d 296, 305 (1979).

The criteria often considered by State and Federal courts to test the lawfulness of a legislative enactment that impairs a contract obligation are summarized in *Board of Administration v. Wilson*, 52 Cal. App. 4th 1109, 1154 (1997):

(1) the enactment serves to protect basic interests of society;

(2) there is an emergency justification for the enactment;

(3) the enactment is appropriate for the emergency; and

(4) the enactment is designed as a temporary measure.

In this report, the focus of the evaluation of conditions for declaring a fiscal emergency has been on the primary causes of the current condition, which are retirement costs and other employment cost-drivers. Therefore, the focus has been on developing a solution that appropriately addresses the primary causes of the City's current fiscal situation. Should the City Council elect to declare an emergency, the purpose of the emergency should be to address these costs, especially retirement costs.

Moreover, the factors noted above are not necessarily absolute. Since *Home Bldg & Loan*, the Supreme Court has, in some cases, upheld contractual impairments without some of these factors. See *Veix v. Sixth Ward Bldg. & Loan Assn.*, 310 U.S. 32, 39-40 (1940) (recognizing that an emergency need not be declared and relief measures need not be temporary for an impairment to be deemed constitutional). In *United States Trust Co. of New York v. New Jersey*, 431 U.S. 1 (1977), the Supreme Court acknowledged this shift and established a new standard to evaluate whether a contract impairment is constitutional. The Supreme Court noted 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." *Id.* at 23 n.19. Consequently, the Supreme Court held that "an impairment may be constitutional if it is reasonable and necessary to serve an important public purpose." *Id.* at 25.

In determining the "reasonableness" of the impairment, a court will look at the extent of the impairment as well as the public purpose to be served. A court will more closely scrutinize an impairment of its own contracts than those only involving private parties. See *University of Hawaii Professional Assembly v. Cayetano*, 183 F.3d 1096, 1107 (9th Cir. 1999).

Another California court described the factors to consider as: "the nature, importance and urgency of the interest to be served by the challenged legislation; and whether the legislation was appropriately tailored and limited to the situation necessitating its enactment." *Donlan v. Weaver*, 118 Cal. App. 3d 675, 682 (1981).

While no California cases have upheld an impairment of a government entity's own contract, case law from other jurisdictions supports the notion that a public agency's inability to provide essential services is a strong indication of a fiscal emergency. In those jurisdictions, courts have recognized that a sharp decline in revenues coupled with the concurrent inability to provide essential services constitutes an "emergency" justifying the impairment of contractual obligations. For example, in *Subway-Surface Supervisors v. N.Y.C. Transit Authority*, 44 N.Y.2d 101 (1978), the New York Court of Appeals upheld the City's suspension 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," 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. *Id*. at 110. [10]

Federal and State courts recognize the constitutional power of a local municipality in response to an emergency to act in the public's interest, to preserve the health, safety and well-being of City residents. The scope of the power includes the ability to impair contract obligations under certain limited circumstances.

D. Evidence of San José's Fiscal Emergency

1. San José's Inability to Provide Services at Required Levels to Date

As demonstrated below, the sharp rise in retirement costs combined with decreased revenues (which have declined in absolute terms, and are not projected to grow at a rate sufficient to keep up with these expenditure increases) have staggering implications on San José's ability to provide essential services. The San José City Charter provides guidance as to which services are "essential" to the City: Police, Fire, Public Works, Library, and Parks and Recreation are some of the service-providing departments specifically established pursuant to Section 807 of the City Charter. Other departments, such as Finance, Personnel, and Planning, are also established by City Charter, and are obviously necessary to support the City's operations.

In 2011-2012, a General Fund shortfall of $115 million was addressed with 70% ongoing solutions and the elimination of approximately 440 positions in all funds. Previous budgets closed $565 million in General Fund shortfalls by eliminating 1,614 positions in all funds, through a combination of strategies: reduced/eliminated services, cost savings, and new revenues (2002-2003 to 2010-2011).

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[10] Similarly, in *Buffalo Teachers Federation v. Tobe*, 464 F.3d 362 (2d Cir. 2006), the Second Circuit Court of Appeals upheld a wage freeze imposed by the city after forecasting an increase in its budget deficit from $7.5 million in fiscal year 2002-2003 to $97-127 million in 2006-2007. The court concluded that the wage freeze was reasonable and necessary. The city had already exhausted other, more drastic measures, including school closings and layoffs, and only implemented the wage freeze as a last resort. The court noted that the city's only other option was the elimination of more municipal jobs and school closures. Based on these facts, the court found the wage freeze was both necessary and reasonable to address the "very real fiscal emergency in Buffalo." *Id.* at 373.

These figures do not include General Fund deferred maintenance and infrastructure needs that the City has been unable to fund, which are now estimated at $474 million ($105 million ongoing). General Fund shortfalls are expected to continue in the future with projected deficits totaling $116 million over the next four years.

A significant portion of the costs of providing services to the community are the salaries and benefits paid to City employees, with nearly two-thirds of the City's General Fund tied directly to personnel costs. This is because municipal services are generally labor-intensive, with City employees such as police officers and firefighters providing essential services. In an effort to maintain service levels, the City has implemented cost control measures, including the following:

- an organization-wide hiring freeze since November 2001, with exemptions based on requests critically necessary to perform essential functions of the department;
- expenditure controls on technology, marketing, office furniture, equipment, and vehicle purchases;
- voluntary furloughs and special reduced work weeks;
- use of departmental Cost/Position Management Plans to force savings during a fiscal year;
- employee wage freeze in 2005;
- a salary freeze for unrepresented employees (including executives and professionals) and most City bargaining groups for 2009-2010; and
- 10% reduction in the total compensation (from the baseline 2009-2010 fiscal year) for all City employees, including the roll-back of cost-of-living increases received by two unions.

Persistent General Fund budget shortfalls have necessitated deep service reductions in departments that rely on the City's General Fund, including cuts to Police and Fire services, the inability to open and operate new library facilities, a reduction in the days and hours of operation of the City's libraries, and a reduction in the number of neighborhood community centers and services provided by the Parks, Recreation and Neighborhood Services Department. With escalating retirement costs, the budget shortfalls in the last two years have been the most severe. As shown in the following chart, the staffing level for the City of San José has been reduced by 28% since 2001-2002, with the majority of the impact experienced in 2010-2011 and 2011-2012. As staffing continues to erode at a rapid pace, the City's capacity is diminished to provide the essential services set forth in the Charter. Staffing reductions to date have severely impaired the government's ability to provide services at the level and quality that are required for the health, safety, and welfare of the community.

Staffing Level Chart (All Funds) (2001-2002 Adopted Budget through 2011-2012 Adopted Budget)					
	2001-2002 FTEs	**2009-2010 FTEs**	**2010-2011 FTEs**	**2011-2012 FTEs**	**% Chg 01-02 to 11-12**
Public Safety					
Fire	847.0	852.0	770.5	752.0	-11%
Police	1887.0	1806.7	1622.9	1510.9	-20%
Total	**2734.0**	**2658.7**	**2393.4**	**2262.9**	**-17%**
Community Services					
Library	359.6	365.4	300.6	271.4	-25%
Parks and Recreation	862.0	707.6	628.1	459.7	-47%
Other services (combined)	1448.1	1188.5	1012.5	996.2	-31%
Total	**2669.7**	**2261.5**	**1941.2**	**1727.3**	**-35%**
Capital Maintenance	**1418.0**	**1038.1**	**906.9**	**865.6**	**-39%**
General Government	**631.6**	**665.1**	**598.2**	**544.2**	**-14%**
Total Department Staffing	**7453.3**	**6623.4**	**5839.7**	**5400.0**	**-28%**

Sources: City of San José Adopted Budgets 2001-2002 and 2009-2010 through 2011-2012.

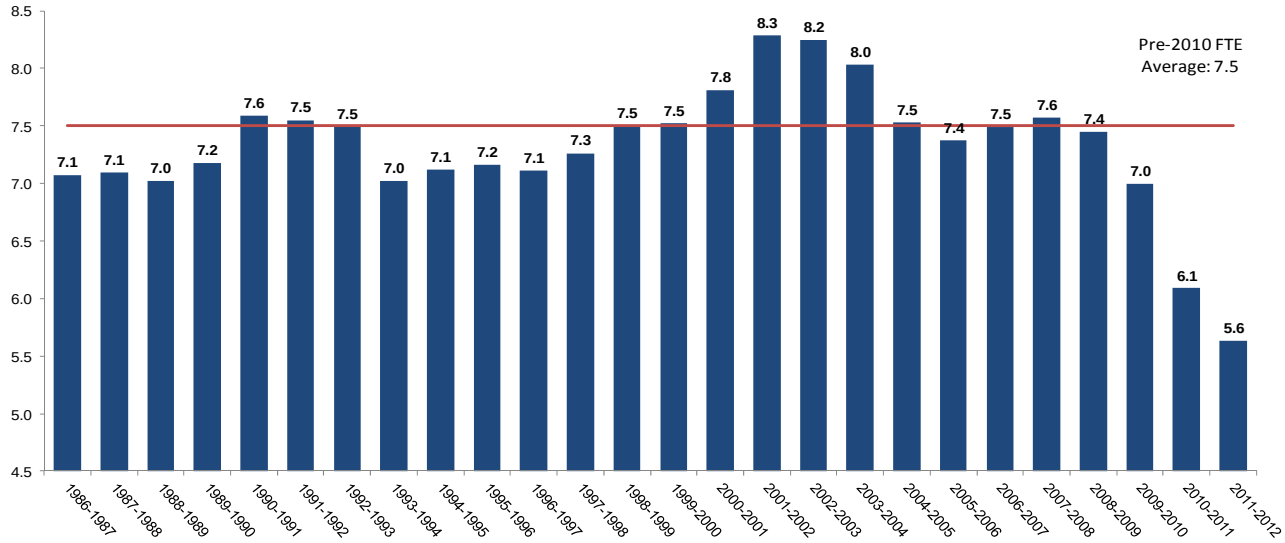
With the drop in staffing levels and the magnitude of the General Fund shortfalls, no service area has been spared from deep cuts.

In 2000-2001, when retirement costs were at their low watermark for the last decade, the City had 7,024 full time equivalent employees. In 2010-2011, when retirement costs were at the highest in the last decade, full-time equivalent employees were significantly reduced to 5,840. With the position reductions in the 2011-2012 Adopted Budget, San José dropped to staffing levels not seen in over 20 years (5,400 positions). Over roughly the same 20-year period (1988-1989 to 2000-2011, as measured in January of each fiscal year), the City's population grew from 765,300 to an estimated 958,789 – a 25.3% increase.[11] As a result, the number of City employees per 1,000 residents has fallen from 7.0 to 5.6 across this period.[12] Without corrective action, even with no further population growth, this ratio will fall to 5.1 in 2012-2013.

[11] City of San José Department of Planning, Building & Code Enforcement compilation of Census and California Department of Finance data.

[12] The California Department of Finance has not projected population levels for 2012. This analysis assumes that the City's population will remain the same in 2012 as it was in 2011. San José's population has actually grown each year since 2004.

Full-Time Employees per 1,000 Population
Fiscal Years 1986-1987 through 2011-2012



Sources: City of San José Adopted Budgets and California Department of Finance Population Estimates.

2. Service Level Impairment Will Worsen Significantly in Foreseeable Future

Although there is much evidence to conclude that even the service impairment to date rises to the level of an emergency, a critical consideration is whether economic conditions and rising employee costs will further impair the ability to provide public services into the foreseeable future. As demonstrated below in the Service Impact Analysis Section and in Appendix A following this report, that answer, unfortunately, is a resounding "yes." As described in detail below, the retirement cost increases to date coupled with the retirement cost increases projected in the next few years will make dramatic service-level reductions a necessity to balance the budget.

As noted by the national accounting standards board for governmental employers (GASB), financial insolvency is directly tied to the ability of an entity "to continue public services and/or existing programs."[13] By that standard, the City will experience a service-level emergency if it continues on its current path. The likely budget balancing scenarios over the next three years include:

Police Department

- Responses will increasingly be limited to only high priority, violent crimes.

[13] Government Accounting Standard Board, Economic Condition Reporting: Fiscal Sustainability.

- Response times will increase dramatically:
    - the average response time for Priority 1 and 2 calls[14] will increase from the current 6 minute and 12 minute averages (respectively) to over 8 minutes and over 30 minutes (respectively);
    - the average response time for Priority 3 and 4 calls (which is currently in the 40 minute range) is projected to be in the 1.5 to 2 hour range, with many of these kinds of calls going without any response at all.
- Misdemeanor and property crimes will likely go uninvestigated, as the Department will lack resources to investigate all but the most serious crimes.
- The City will be unable to respond effectively to multiple critical events concurrently.
- Community policing efforts will continue to decline, leading to a reduced sense of safety, less confidence in the police force, diminished effectiveness of the police force, and a potential increase in criminal activity.

Fire Department

- Response times for fires and medical emergencies will increase to over 10 minutes, and will, on a regular basis, likely hit 12 minutes, leading to increased risk of loss of life and significant property damage.
- An additional nine fire companies and a second fire station will close, leading to unacceptable on-duty staffing levels at less than half the national per capita average.
- The Hazardous Incident Team and the Urban Search and Rescue Team will both be completely eliminated. Airport Fire protection services will no longer be provided by the San José Fire Department and Advance Life Support Services at the Airport will be diminished.
- The City will consider alternative service provision models as necessary to keep most fire stations open and operational.
- The Department will have no capacity to respond to two or more sustained structure fires that occur within the same time period, and very limited capacity to respond to wild land fires. Moreover, as the largest firefighting force in the County, the Department cannot rely on mutual or automatic aid from neighboring jurisdictions to provide basic levels of fire and emergency medical services; typically, other agencies rely on SJFD for assistance.

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[14] For a description of the San José Police Department's call prioritization method, please refer to the "Response Time Increases" subsection in Appendix A, Section A, Sub-Section 3.

- The Department will need to consider whether to continue to provide advanced life support services from fire companies. If paramedic services are no longer provided by the Fire Department, one of two outcomes is probable. The first potential outcome is that patients will wait longer for advanced life support services. This will be particularly concerning for the seriously ill or injured patients and will lower the potential to resuscitate pulseless, non-breathing patients. The second possible outcome is that ambulance company staffing will have to be significantly increased to meet the current advanced life support response times, leading to a dramatic increase in user fees to maintain the existing level of pre-hospital emergency medical services.

Library Services

- Six to eight branches, out of the 18 currently operational branches, will be open 3 days per week and the remainder closed in 2012-2013. At the end of fiscal year 2014-2015, all branch libraries will close, leaving the central Dr. Martin Luther King Jr. Library (King Library) as the *only* City library.[15]

- 90% of library programming, including the educational programming, will be eliminated.

- Many residents and students will be without access to any library; King Library, the only library that will remain open, does not have the capacity to serve nearly 4.5 million annual branch library visitors.

- 880 literacy education programs at family learning centers with 20,555 attendees will be shut down; 2,000 story times serving 81,000 children will no longer take place.

- Over 700 school-aged children visiting branch libraries after school each day, many of whom are not accompanied by a parent or caregiver, will no longer have a safe, constructive, and educational after-school option.

- Property values for the homes in close proximity to the closed branch libraries may decrease.

Parks, Recreation and Neighborhood Services

- All City recreational programs will be discontinued, and the City's fifty-four Community Centers, all but 11 of which are already operated by area non-profits through the reuse program, will be closed unless partner agencies are able to pay operations and facility overhead.

- The Senior Nutrition Program, which provides approximately 1,000 hot meals a day, will be at severe risk.

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[15] The San José Public Library System's (SJPL) main library is the King Library. It is located in downtown San José and was opened in 2003. The King Library is the first joint-use library in the United States, shared by a city and a major public university (San José State University). In addition to the King Library, the SJPL has 22 branch libraries. However, four of those branches – which were recently constructed following bond measures - are not operational due to budget restraints, leaving only 18 currently operational branches.

- The Grace Community Center, which provides therapeutic services for adults with mental, physical and developmental disabilities will close.
- Teen programs will be eliminated. Gang-intervention and graffiti abatement programs will be reduced to skeletal levels.
- Property values for the homes in close proximity to the shuttered Community Centers may decrease.
- Ability to coordinate and engage 500,000+ hours currently served by volunteers to improve City property will be lost.

Impacts on Other City Services

- Traffic maintenance programs will be further reduced, impacting traffic sign maintenance, roadway striping, and marking maintenance.
- Further reductions in City facility maintenance and fleet maintenance.
- General Government departments such as Council Appointees, Finance, Human Resources, Information Technology, and Mayor and City Council will be further cut, resulting in reduced staffing for oversight, management, internal controls, and compliance.

These public services are essential to the functioning of San José. In the absence of these essential city services, firms and residents will perceive a disconnect between taxes paid and services provided. "[Taxes] unmatched by tax-financed, compensating service benefits for taxpayers – whether property owners, consumers, or firms – will drive those taxpayers from the city. Property values fall, business sales decline, and the city's job base shrinks."[16] The City must avoid this potential downward spiral by working to maintain services that provide social and economic benefits to its residents.

In conclusion, San José has experienced a sharp increase in service delivery costs, driven primarily by fast-rising retirement costs, in tandem with absolute declines and ongoing weakness in City revenues. In turn, to maintain budget balance, these factors have required year after year of escalating service cuts. Given the extent of these service reductions to date, and the anticipated impact of the next round of cuts to be required if no corrective action is taken, these unsustainable trends have now reached the point of fiscal emergency.

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[16] Andrew F. Haughwout, et al., *Local Revenue Hills: Evidence from Four U.S. Cities* (March 2003), PIER Working Paper No. 03-012 at 30.

II. BUDGET

A. The City's Budget (2011-2012)

The San José City Charter requires the City to have a balanced budget in place before the beginning of each fiscal year. To develop this budget, the City follows a thorough process that provides for detailed review, extensive public input, and consideration of both current-year and longer-term concerns.

As of 2011-2012, the Adopted Operating and Capital Budgets for the City of San José total $2.8 billion, divided into three categories:

- General Fund: used for regular operating expenditures (such as public safety, parks, and libraries);
- Special Purpose Funds: used for operations that receive direct and dedicated funding, restricted to use for a specific purpose, such as the Water Pollution Control Plant, Special Purpose Funds, and the Airport; and
- Capital Funds: used for infrastructure improvements (such as transportation, airport, and parks).

Because of the restrictions on the other types of funds, this Report generally focuses on the General Fund. The 2011-2012 General Fund Adopted Budget totals $906 million.

B. Structural Deficit and Efforts to Balance Budget

1. Recurring Shortfalls (2002-2003 through 2011-2012)

In each and every year of the past decade, the City of San José has been required to address General Fund budget shortfalls, totaling $680.3 million in the aggregate. These shortfalls have been driven both by declines and ongoing weakness in City revenues in the wake of two recessions and by an unsustainable cost structure fueled by rapidly increasing retirement and benefit costs.

To correct for these imbalances, the City has adopted a combination of strategies. These strategies have included lowering personnel costs through compensation reductions and active healthcare changes, revenue enhancements, new service delivery models to lower costs and improve efficiency, and drawing down from City reserves. Given the severity and structural nature of the City's budget shortfalls, however, San José has also had to significantly reduce City services and staffing levels in both public safety and non-public safety areas. Across the General Fund as well as other City funds, San José has eliminated 2,054 positions during this period, or 28% of the workforce ten years ago. This decade of corrective actions has exhausted the City's most manageable budget balancing alternatives.

When population growth is taken into account, the impact of staffing cuts is even greater. From 2001-2002 to 2010-2011 (measured as of January in each fiscal year), the City's population grew from 899,796 to 958,789 – or nearly 7% – while 28% of City positions were eliminated.

Fiscal Year	Total General Fund Shortfall
2002-2003	($46.3 M)
2003-2004	($92.1 M)*
2004-2005	($81.7 M)*
2005-2006	($58.0 M)
2006-2007	($34.9 M)
2007-2008	($19.9 M)
2008-2009	($29.6 M)
2009-2010	($84.2 M)
2010-2011	($118.5 M)
2011-2012	($115.1 M)
TOTAL	**($680.3 M)**

As shown above, over this ten year period, the City has absorbed a General Fund shortfall of $680.3 million, which have been significantly increasing since 2008-2009. A majority of these position cuts have taken place within the past three years – and at an accelerating rate within the General Fund.

General Fund Full-Time Employees (2008-2012)

	2008-2009 Adopted Budget	2009-2010 Adopted Budget	2010-2011 Adopted Budget	2011-2012 Adopted Budget	Total Change 2008-2009 to 2011-2012
Positions	**4,893**	**4,701**	**4,249**	**3,759**	**-23%**
Change		**-192**	**-452**	**-490**	**-1,134**

From 2008-2009 through 2011-2012 alone, the City's Adopted Budgets have cut the number of General Fund positions by nearly one-fourth, eliminating over 1,100 positions.

2. Factors Driving the Structural Deficit

The City's budget shortfalls have persisted because San José faces a structural budget gap: the growth in the cost of the City's recurring expenditures – most significantly and recently, for employee retirement benefits – outpaces the growth in City revenues. While revenue weakness from the economic downturn has exacerbated this dynamic, an unsustainable imbalance preceded the

Great Recession – and will continue beyond it without additional corrective action. Summarized below, these factors are more fully detailed in Appendix B to this report.

In terms of available resources, San José's primary revenue streams are highly sensitive to the overall economy and have been eroded by the economic downturn. The City's two largest revenue sources, property taxes and sales taxes, alone, comprise nearly half of overall General Fund revenues.[17] Both have experienced recession-driven declines. Median single family home sales prices in San José have fallen. They are down over 5% in September 2011 when compared to September 2010, and are now 38% below peak 2007 levels.[18] At the same time, unemployment within the San José metropolitan area stood at 9.6% as of September 2011, and has doubled since the onset of the recession. Since March 2009, the region has experienced double-digit unemployment in all but two months.[19]

With fewer people working and reduced business activity, sales tax receipts are still below pre-recession levels. Beyond property and sales taxes, other significant City revenue streams, including business taxes and many of the City's licenses and permits, are also linked to general economic performance.

Overall, the adopted 2011-2012 General Fund revenue estimates of $764.8 million (excluding beginning fund balance) remain 7.6% lower than the pre-recessionary level of the $827.7 million received in 2007-2008, despite voter approval of four separate ballot measures to strengthen General Fund revenues during this period (further detailed in a subsequent section of this report). Based on the 2012-2013 Preliminary Forecast, which excludes one-time revenues and grants, and aggregate General Fund growth rates in the City's 2012-2016 Forecast for 2013-2014 through 2015-2016, General Fund revenues are not expected to return to 2007-2008 levels by 2015-2016.[20]

The chart below shows the long-term impact of significant declines in General Fund Revenue growth for San José. The upper dotted line with triangular markers shows hypothetical revenue totals if revenues had increased 3% each year from the pre-recession peak in 2007-2008. The solid blue lower line reflects the City's current reality and, in blue dots with diamond-shaped markers, the projection forward if we assume revenue growth incorporated into the 2012-2016 Forecast, ranging from 2.74% to 3.22% per year, from our current position.

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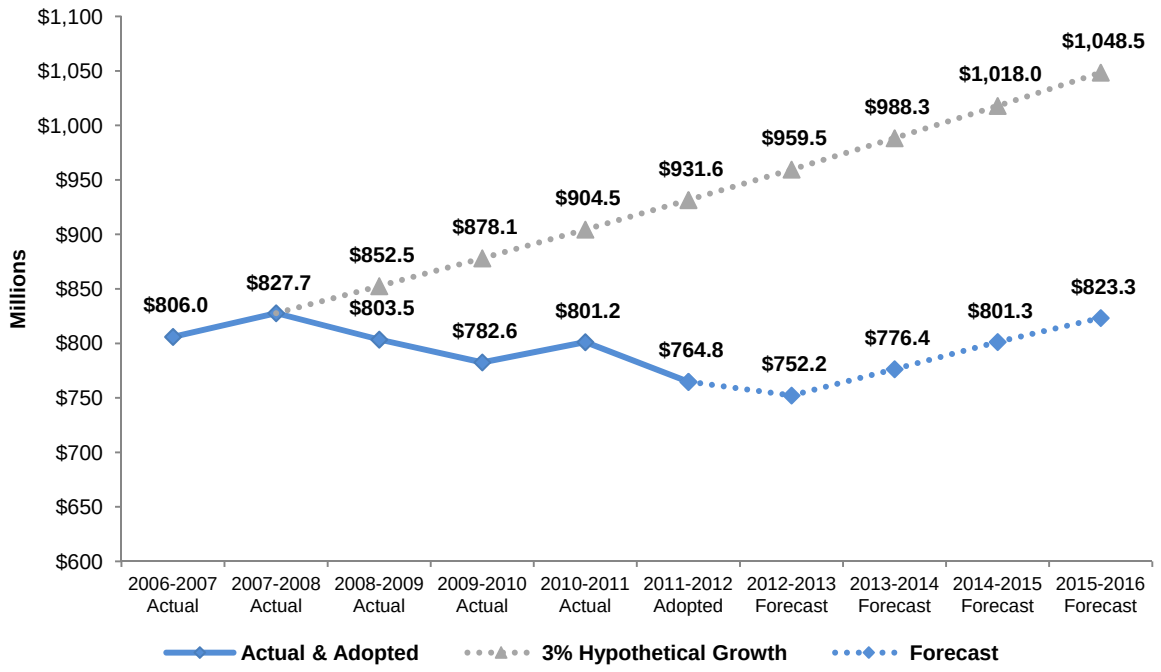
[17] Excluding use of Fund Balance.

[18] Santa Clara County Association of Realtors, September 2011 median home sales prices (single family) in San José of $481,500, down from $510,000 in September 2010 and $772,050 in June 2007.

[19] Employment Development Department, Labor Market Information Division, San José-Sunnyvale-Santa Clara MSA, October 21, 2011.

[20] From the 2012-2013 General Fund Preliminary Forecast, applies the annual growth rates included in the February 2011 Forecast for fiscal years 2013-2014 through 2015-2016.

General Fund Revenue Growth
2006-2007 to 2015-2016 [21]



Sources: San José Adopted Budgets 2006-2007 through 2011-2012, Five Year Forecast (February 2011), 2012-2013 Preliminary General Fund Forecast (November 2011).

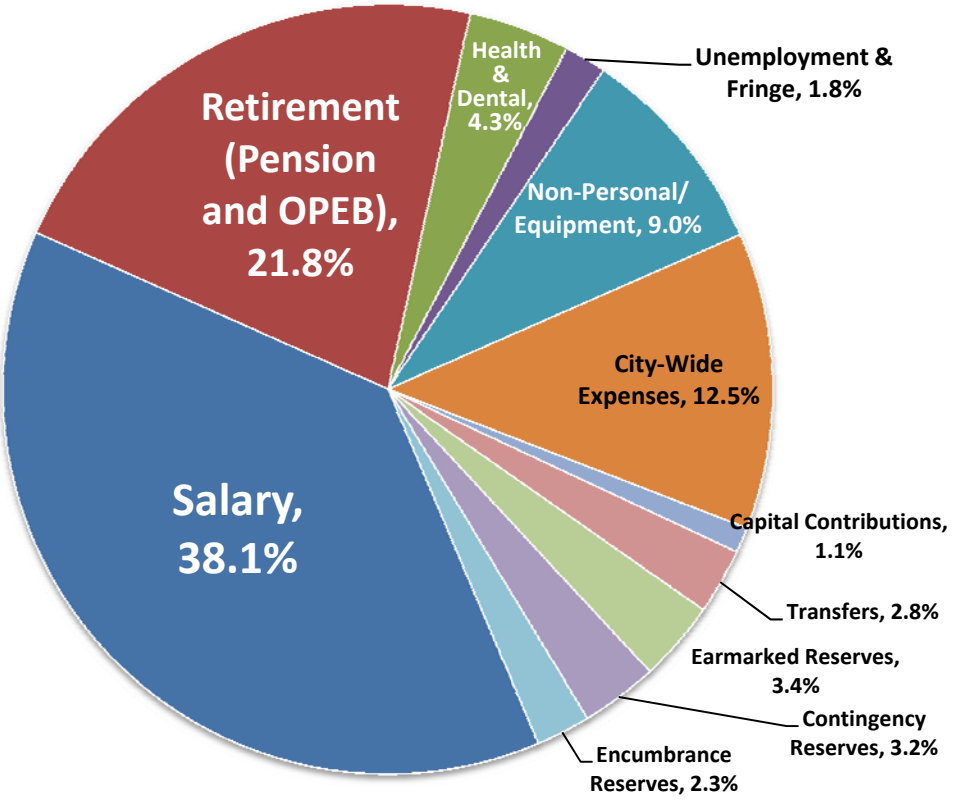
At no point during the forecast period are General Fund revenues projected to approach what they would have been had growth continued at 3% per year since 2007-2008. Adopted 2011-2012 General Fund revenue estimates are $166.8 million lower than hypothetical General Fund revenues of $931.6 million, assuming revenues had grown at 3% per year from 2007-2008.

While these revenue impacts from the economic downturn have been severe – and have now "reset" the baseline for available City resources at a new level far below what was anticipated just a few years ago – the primary cause of the City's current crisis has less to do with current revenue levels than it does with the recent dramatic *increases* in employee-related costs, especially pension and retiree health costs. At the same time that revenues have declined or experienced only minor growth, the cost of delivering City services has increased rapidly.

[21] Note, the actual and adopted revenue figures include one-time revenues and grants; the 2012-2013 Forecast figure is based on the 2012-2013 Preliminary Forecast and is likely understated as it does not include one-time revenues and grants.

Service delivery is personnel-dependent – relying on the municipal workforce to patrol the streets, respond to emergencies, provide services at libraries and community services, and deliver the other direct and supporting services of San José. As a result, employee wages and benefits account for nearly two-thirds of the total General Fund Adopted Budget[22] in 2011-2012 at a total cost of $596.9 million. This total would be even higher, but for approximately $58.5 million in gross savings ($39.6 million net savings, excluding retirement costs that must be paid) from the continuation of 10% employee compensation reductions and a roll back of any general wage increases in 2010-2011 for all City employees.[23] [24]

2011-2012 Adopted Budget / General Fund Uses by Spending Category



Source: City of San José Adopted Budget 2011-2012.

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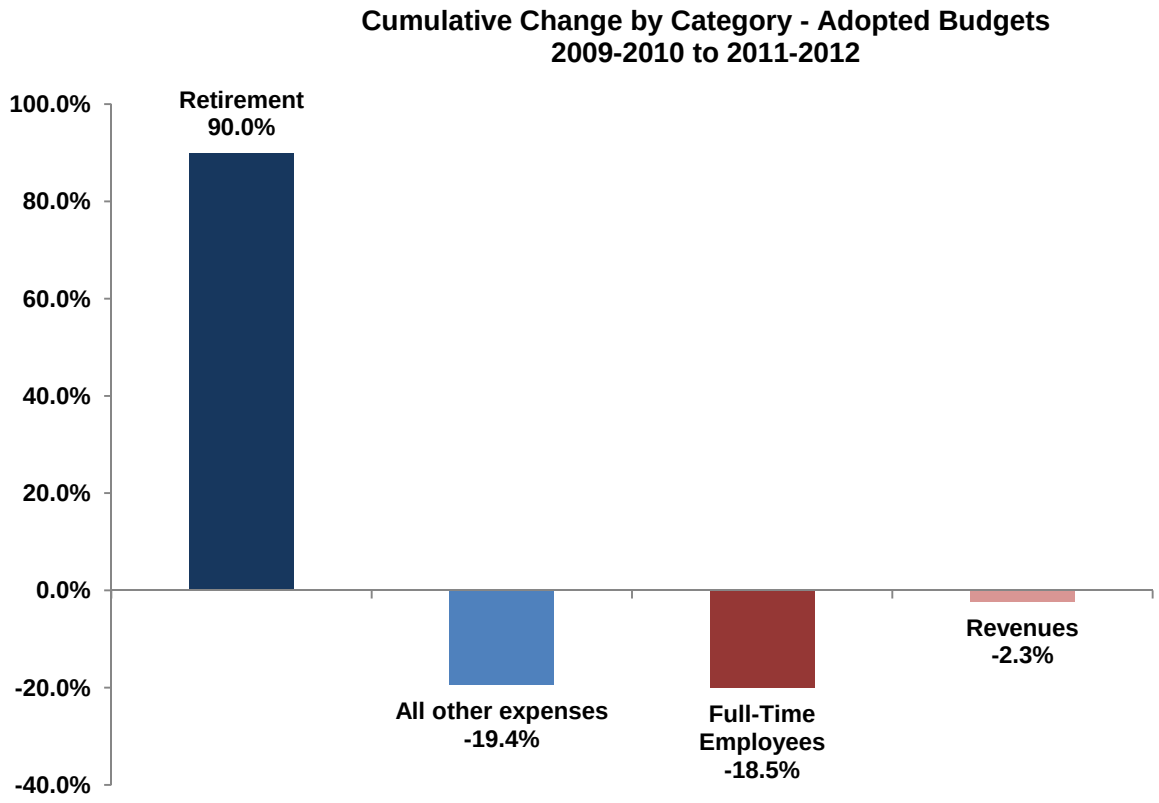
[22] Includes budgeted reserves. To the extent that reserves are not fully spent in any year, personnel costs will represent an even higher percentage of actual, year-end spending.

[23] City of San José, 2011-2012 Adopted Budget, Budget Message.

[24] The Police Officers' Association (POA) is currently scheduled for binding interest arbitration over whether the 10% total compensation reduction for POA employees is an ongoing reduction or whether it was a one-time reduction. If an arbitrator rules it was a one-time reduction, then this will dramatically reduce these savings.

Nonetheless, while City revenues (excluding beginning fund balance) declined by 2.3% from 2009-2010 to 2011-2012, the average total *cost* of wages and benefits per full-time equivalent position rose by 18% in just two years – from $120,418 to $141,918. Largely to offset this growth in costs per employee, the City cut total General Fund headcount by 942 FTEs (20%) over this two-year period.

As shown in the following chart, retirement costs were the primary drivers of the City's personnel cost growth across this period:



Source: City of San José Adopted Budgets 2009-2010 through 2011-2012.

The factors underlying the rapid increase in City retirement costs are further outlined in Section III of this report.

3. Corrective Actions To Date – Options Increasingly Exhausted

To address and attempt to resolve the City's structural budget problems, the Mayor and City Council, even before the full onset of the economic downturn, directed the Administration in 2007 to develop

a General Fund Structural Deficit Elimination Plan.[25] This 2008 Plan, which was the result of an effort involving Council leadership, a cross-section of community stakeholders, and technical expertise from the City Administration, has provided a blueprint for addressing the City's revenue and expenditure imbalance. The Plan has guided actions to mitigate San José's ongoing budget shortfalls with approaches in three primary areas: (1) revenue strategies; (2) cost savings strategies; and, (3) as other options are exhausted, service reductions and elimination.

a. Revenue Strategies

Since 2008, voters have approved four ballot measures that have sustained, added, or increased existing revenue sources of approximately $57 million:

- Establishment of a Telephone Line Tax in November 2008, replacing the existing Emergency Communication System Support Fee to secure ongoing collection of $20.5 million;
- Reduction and broadening of the Telephone Utility Tax in November 2008, restructuring the tax to ensure ability to collect in the future, generating $30.8 million;
- Increasing the Cardroom Business Tax rate and number of cardroom tables allowed in June 2010, to generate an estimated $3 million; and,
- Establishment of a Marijuana Business Tax in November 2010, generating $2.5 million.

In addition, the City has adjusted its fees and charges for various services to ensure that the City is recovering allowable costs and has maximized transfers from other funds to the extent permissible and appropriate. Where available, various one time funds (such as revenue from legal settlements and from sale of properties) have also been incorporated into the annual budgets to help achieve current-year balance, even though these sources are not recurring. Many other revenue ideas were evaluated and tested through City Council and community discussions. The results of these discussions continue to serve as a benchmark for various levels of re-evaluation.

As budget shortfalls continue, however, many one-time revenue sources have been exhausted. For example, the City's Economic Uncertainty Reserve – totaling $15.8 million a decade ago (2001-2002) has been spent down to zero as of 2011-2012. In addition, as fees and charges have been steadily hiked to maximize cost recovery levels, there is now less room for further increases within permissible cost recovery levels. Looking at tax revenues, changes generally require voter approval, significantly constraining the opportunity for growth.

As a result of such dwindling revenue options, the City has increasingly relied on expenditure reductions to address its ongoing shortfalls.

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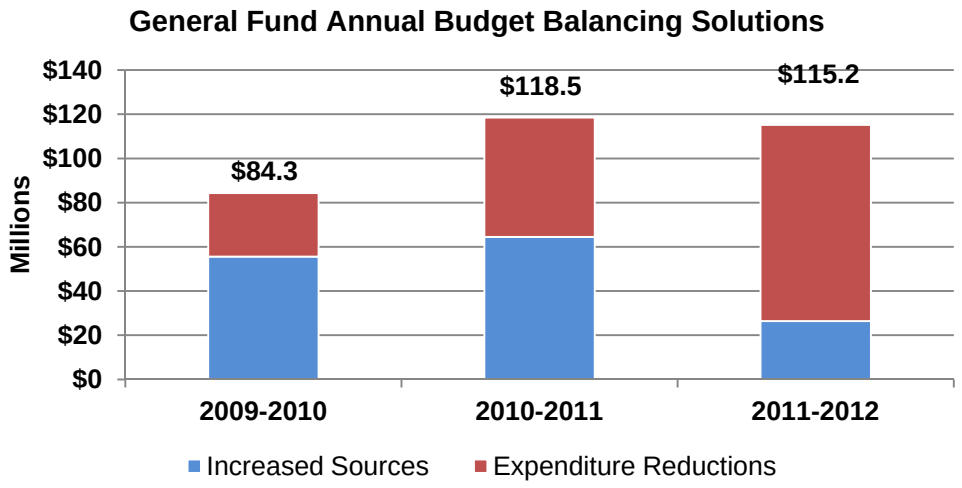
[25] The General Fund Structural Deficit Elimination Plan is available at: http://www.sanjoseca.gov/budget/FY0809/GFStructuralDeficitEliminationPlan112008.pdf.



Sources: City of San José Adopted Budgets 2009-2010 through 2011-2012.

As recently as 2009-2010, nearly two-thirds of the City's budget gap was balanced with revenues. Over half of the shortfall was addressed with revenue solutions in 2010-2011. By 2011-2012, however, available revenues were insufficient to address even one-quarter of the City's shortfall.

b. Cost Savings Strategies

On the expenditure side of the City budget, multiple cost savings and efficiency strategies have been brought forward in an effort to address budget shortfalls in the General Fund (as well as other City funds) while minimizing service impacts. For example, several services have been outsourced at a lower cost, including custodial services, parks maintenance, and graffiti abatement. To capture available economies, the City has also consolidated operations and services – such as merging the Public Works and General Services Departments, and consolidating special events functions (at a significantly reduced level). In additional examples of productivity initiatives, the Library Department has implemented new technology to reduce the staffing necessary to operate the branch libraries, and the Police Department has civilianized functions that could be performed by non-sworn staff at a lower cost.

In addition, the City has developed public-private partnerships to stretch meager City resources and soften the impact of service reductions. Specifically for park maintenance services, the City:

- engaged volunteers through organizations such as the Parks Foundation, the Guadalupe River Park Conservancy, and Friends of the San José Rose Garden, generating over 500,000 volunteer hours across City parks;
- established a Community Facilities District (CFD) for the maintenance of 17 acres of park facilities at the Hitachi site off of Cottle Road;

- received in-kind maintenance of McEnery and Piercy Parks through Adobe Corporation and a Home Owners Association, respectively, and will receive in-kind maintenance for the future Buena Vista Park through the local neighborhood association;
- authorized credits against a developer's parkland in-lieu fee for maintenance of future parks at Newhall, Mabury and River Oaks; and,
- received funding through development agreements for the future North San Pedro and Vista Montana Parks.

In addition to identifying efficiencies and cost savings in the delivery of service, the City has acted to slow the growth in personnel costs on a per employee basis – undertaking cost savings actions including 10% total compensation reductions, rollback of any general wage increases in 2010-2011, modifications to medical benefit plans and cost sharing, reductions/elimination of vacation sellback, and reductions/elimination of disability leave supplement pay.

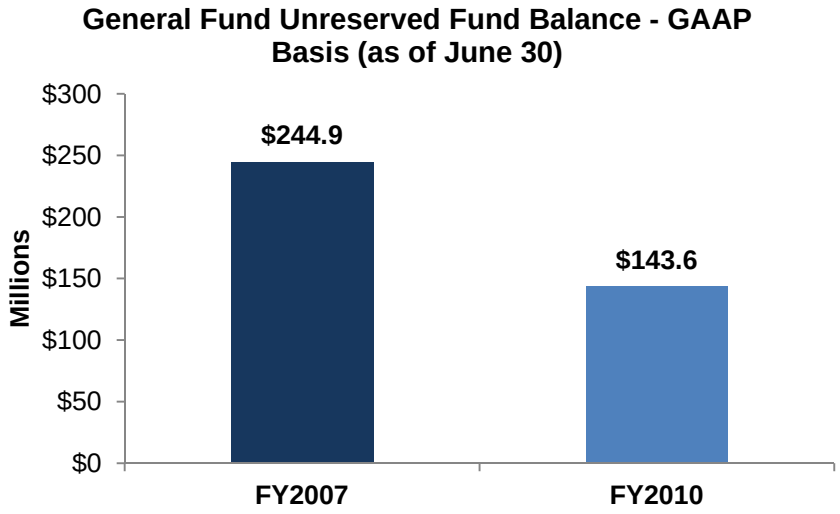
c. Service Reductions/Eliminations

With the decreasing availability of revenue and cost savings options, the City has had to implement significant service reductions and eliminations – severely impacting all major service areas, including sworn Police and Fire. These service reductions are detailed in Section IV and in Appendix A of this report.

4. Actual General Fund Performance and Fund Balance Reflect Structural Deficit

Reflecting the trends outlined above, the City's Fund Balance levels have declined significantly since 2006-2007, as reported in the City's Comprehensive Annual Financial Reports (CAFRs). CAFR statements are developed consistent with Generally Accepted Accounting principles (GAAP) and will sometimes vary from the balances reported on a budgetary basis primarily due to accounting adjustments for loans and advances, reserves for encumbrances, and unrealized gains and losses.

While there are some differences between the CAFR and budgetary figures, the audited financial statements reporting unreserved fund balances are useful indicators of the City's overall fiscal position. As shown in the chart below, within the General Fund, Unreserved Fund Balances reported in the CAFR declined by more than $100 million in just the three years from 2006-2007 to 2009-2010. The majority of this decline reflects the drop in reserves and ending fund balance allocations (which account for the majority of the unreserved fund balance) from $158.7 million at the end of 2006-2007 to $87.3 million in 2009-2010. As a percentage of General Fund revenues, the City's Unreserved Fund Balance in the CAFRs declined from 36.3% at the end of 2006-2007 to 22.1% as of the end of 2009-2010.

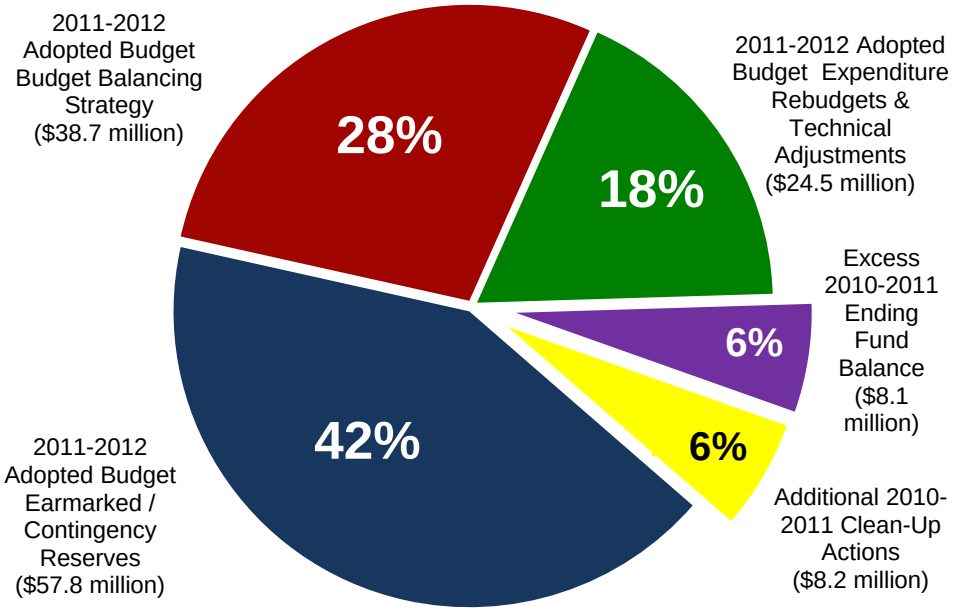


Source: City of San José Comprehensive Annual Financial Reports.

While a 22% Unreserved Fund Balance may still seem healthy, the accounting term "unreserved fund balance" can create a misleading impression that such resources are fully available going forward, when in actuality the remaining balance in the General Fund at the end of a fiscal year is assumed and already allocated by the City for the following fiscal year.

For example, in 2010-2011, the General Fund had an ending balance of approximately $137 million. As a part of the 2011-2012 budget planning process, the City assumed a 2010-2011 balance of $121 million, which was allocated to balance part of the 2011-2012 budget shortfall, to rebudgeting for projects carrying over from the 2010-2011 fiscal year, and to maintain certain reserves, including the Contingency Reserve and the Workers Compensation/General Liability Catastrophic Reserve. As shown in the chart below, the 2011-2012 Adopted Budget had assumed all but $16.3 million of the actual 2010-2011 ending fund balance in the development of the budget. After adjusting for clean-up actions to exclude the development fee program and true-up rebudget actions previously approved by the City Council ($8.2 million), the excess fund balance available at the end of 2010-2011 totaled only $8.1 million. This additional fund balance represented only 0.4% of the budgeted 2010-2011 sources and uses in the General Fund.

2011-2012 Beginning Fund Balance Reconciliation
($137.3 million)



In short, the unreserved fund balance reflected in the CAFRs has already been assumed as a funding source in the annual budget and is not available for allocation.

The erosion of unreserved fund balance available to carry-over to the following fiscal year also has a negative impact on the City's credit rating. In fact, Fitch Ratings has already downgraded the City's rating from AAA on March 18, 2011, providing the following rating rationale: "The downgrade to 'AA+' for the GOs is based on the reduction in fund balance following several years of structural imbalance, high and rising retiree costs and reduced expenditure flexibility following significant labor concessions and service reductions already implemented."

San José is at high risk of further downgrades if ongoing expenditures cannot be aligned with ongoing revenues. As recently as March 16, 2011, for example, Standard & Poor's cited the City's unreserved General Fund Balance levels as a factor in affirming the City's rating, noting that:

> *"If management does not respond to potential revenue volatility in a timely basis such that reserves fall below what we consider to be strong levels, we could take negative rating action."*

Similarly, Moody's Investors noted in a March 15, 2011 report that:

> *"If the city does not implement budget adjustments sufficient to largely preserve its current level [of] reserves, negative pressure could be applied to the rating."*

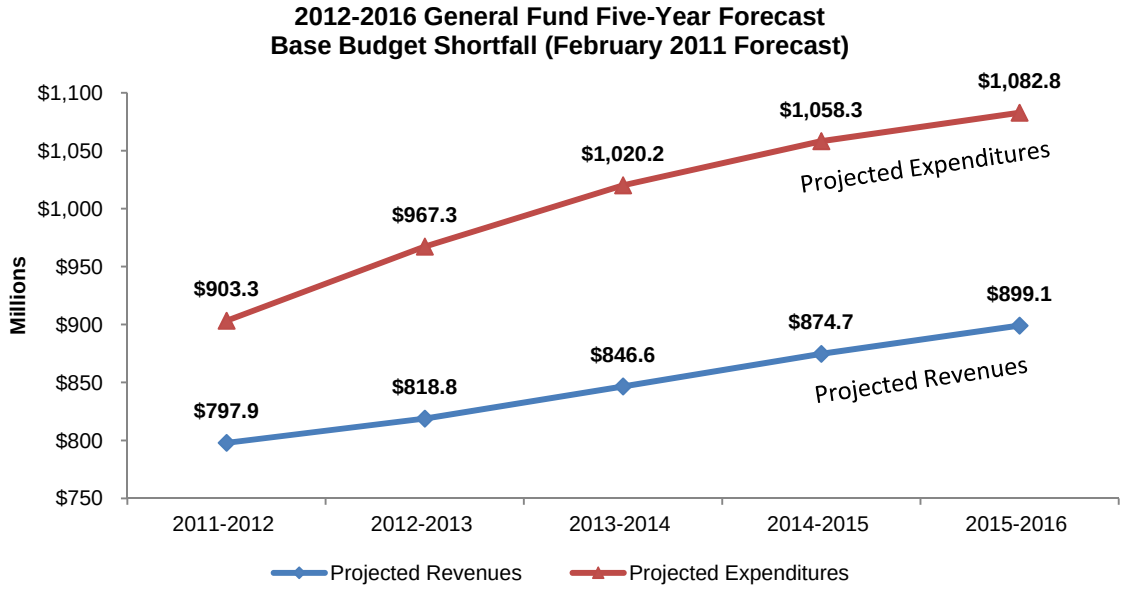
Fund Balance levels are important to the credit rating agencies because reserves provide a critical buffer against revenue losses and volatility, and against unanticipated spending demands due to natural disasters and other unforeseen events. In turn, strong credit ratings are important for maintaining the City's access to the capital markets for borrowing at reasonable rates, and they are also a widely viewed indicator of the City's overall fiscal condition.

C. Without Corrective Action, Budget Pressures Will Continue

1. Gap Between Revenues and Expenditures Is Widening

As detailed in subsequent sections of this Report, the impact of the City's service reductions required to maintain a balanced budget have already reached untenable levels – and the next round of cuts to address any further shortfalls will severely worsen this service-level crisis. If no changes are adopted to contain the projected growth in benefit costs, then the unsustainable trends now in place will drive worsening deficits.

The chart below, based on the February 2011 Five-Year Forecast and Revenue Projections, shows the widening gap between revenues and expenditures as costs are forecasted to continue to outpace revenues.



Source: City of San José Five-Year Forecast (February 2011).

Of note, this projected gap *widens* despite the following assumptions:

- **No** cost-of-living salary increases over the five-year period;
- Moderate revenue growth assuming continued slow economic recovery;
- No funding for deferred and unmet General Fund infrastructure needs of $474 million one-time and $105 million ongoing; and,
- No additional costs associated with the adoption of more prudent actuarial practices that may be approved by the Retirement Boards in future years.

Since the release of the February 2011 Forecast, the City Council approved the 2011-2012 Adopted Budget in June 2011, which closed a final General Fund budget shortfall of $115 million, with 70% ongoing solutions. The portion of the 2011-2012 shortfall addressed with one-time solutions ($34.9 million) will carry over to 2012-2013. In November 2011, the Administration released the 2012-2013 Preliminary General Fund Forecast, reflecting a 2012-2013 General Fund shortfall figure of $80.5 million. This figure incorporates the $34.9 million in one-time budget solutions used to solve the budget shortfall in 2011-2012.

Assuming the revised budget shortfall for 2012-2013 and the budget shortfalls previously projected for 2013-2014 through 2015-2016 in the February 2011 Forecast, the General Fund budget deficit would begin at $80.5 million in 2012-2013 and grow to $115.7 million by 2015-2016, if no corrective actions were taken in any year.

2013-2016 General Fund Forecast
($ in Millions)

	2012-2013	2013-2014	2014-2015	2015-2016
Cumulative Annual Deficit (No Corrective Action From Year to Year)	**($80.5)**	**($105.6)**	**($115.6)**	**($115.7)**

Sources: 2012-2013 Preliminary General Fund Forecast and February 2011 Five-Year Forecast.

It is important to note that there are a number of significant factors that may impact the City's General Fund condition. The revenue and expenditure categories that may experience significant changes in 2012-2013 based on updated information include contributions to the retirement plans, San José Redevelopment Agency-related impacts, and economically sensitive revenues, such as sales tax.

In addition to the assumption risks outlined previously, the 2012-2013 Preliminary Forecast does not incorporate the following:

- Police Officers' Association (POA) Arbitration Results/Negotiated Labor Agreements: The

Preliminary Forecast assumes the compensation reductions approved in 2011-2012 for employees represented by the POA will be ongoing. However, it is currently unsettled whether those reductions were one-time or ongoing in nature, and the issue is scheduled for arbitration in the near future. If the City does not prevail and the arbitrator determines that the compensation reductions are one-time, the 2011-2012 budget shortfall would increase by approximately $25 million. In addition, there are currently no agreements in place for four of the City's bargaining units (MEF, CEO, OE 3, and IBEW) and no salary adjustments have been factored in for those groups for 2012-2013. In addition, the agreement with ALP expires June 30, 2012 and therefore no salary adjustments have been factored in for that group for 2012-2013 either.

- One-Time Revenues/Expenditures: Because the Forecast compares ongoing revenues and expenditures, it generally does not factor in one-time funding sources or one-time expenditure needs.

The 2012-2013 Preliminary Forecast will be refined over the next several months as additional information becomes available. The formal 2013-2017 General Fund Five-Year Forecast will be issued in February 2012, and updated Base Budget revenue and expenditure estimates will be included in that document. Base Budget estimates will continue to be adjusted through the release of the 2012-2013 Proposed Budget in May 2012.

2. Budget Impacts: Actual and Three-Year Projections

The critical question stemming from all of this information is: *what will the impact be on the City's ability to provide services to the residents of San José?*

The table below illustrates the ongoing impact of the City's budget shortfalls on funding for public services. The left side of the table shows the nearly $318 million cumulative General Fund shortfall already addressed by the City over the past three years from 2009-2010 to 2011-2012. Even after the adoption of significant revenue measures, this has required cumulative cuts of more than $171 million spanning across almost every City service area.

Looking forward, as shown on the right side of the table, continued shortfalls are projected to emerge – and to grow on a cumulative basis if no corrective action is taken – from $80.5 million in 2012-2013 to over $115.7 million by 2015-2016. With a reduced level of available revenue solutions (this scenario assumes the identification of $15 million in ongoing revenues), such shortfalls would require even deeper cuts into service levels that have already fallen below community standards in many areas. Illustrative budget impacts are shown in the chart for each major service category, and the resulting service impacts will be discussed in subsequent sections of this report.

General Fund Forecast Budget Balancing Scenario[26]

	Adopted	Forecast			
	2010-2012	2012-2013	2013-2014	2014-2015	2015-2016
Cumulative Annual Shortfall	**(317,983,792)**	**(80,475,000)**	**(105,593,000)**	**(115,625,000)**	**(115,737,000)**
Revenue Solutions	146,553,196	15,000,000	15,000,000	15,000,000	15,000,000
Cumulative Annual Shortfall with Revenue Solutions	**(171,430,596)**	**(65,475,000)**	**(90,593,000)**	**(100,625,000)**	**(100,737,000)**
Cumulative Expenditure Reductions		**Cumulative Projected Expenditure Reductions**			
Public Safety Departments					
Fire	(38,486,130)	(5,500,000)	(12,906,000)	(14,044,000)	(14,044,000)
Police	(62,458,774)	(13,315,000)	(24,274,000)	(26,415,000)	(26,415,000)
Library	(6,343,661)	(13,585,000)	(13,585,000)	(13,585,000)	(13,585,000)
Parks, Recreation & Neighborhood Services	(16,532,157)	(11,390,000)	(13,665,000)	(15,940,000)	(15,940,000)
Other Community Services Depts. (combined)	(3,406,375)	(500,000)	(600,000)	(700,000)	(700,000)
General Government Departments *(combined)*	(26,530,537)	(11,415,000)	(14,268,000)	(17,121,000)	(17,121,000)
Capital Maintenance Departments *(combined)*	(14,420,402)	(3,850,000)	(5,375,000)	(6,900,000)	(6,900,000)
Non-Departmental *(combined)*	(3,252,560)	(5,920,000)	(5,920,000)	(5,920,000)	(6,032,000)
TOTAL	**(171,430,596)**	**(65,475,000)**	**(90,593,000)**	**(100,625,000)**	**(100,737,000)**
Remaining Shortfall	-	-	-	-	-

Sources: City of San José Adopted Budgets 2009-2010 through 2011-2012, Five-Year Forecast (February 2011), and 2012-2013 Preliminary General Fund Forecast (November 2011).

The allocation of expenditure reductions for departments noted above is illustrative only. Council direction is required to formally and finally allocate such reductions. However, in performing this analysis, the City Manager's Budget Office has taken into consideration past and current budgetary prioritization messages from the City Council and known allocation restraints in trying to predict how the anticipated shortfalls will be spread across the departments. For example, the Administration in this analysis is trying to limit the impact on the Police and Fire Departments to the maximum extent possible.

[26] Chart assumptions: The retirement costs are included in the shortfall numbers, and are spread across department cuts, because they are a fixed payment for the City. This table also does not include such costs as vacation/comp time payouts, unemployment insurance contributions, and other payments that may be required due to additional layoffs; moreover, 15% of cuts are non-personal/equipment related cuts. Further, the out-year targets under Public Safety are weighted because of federal grant restrictions on Fire Department staffing levels in 2011-2012.

Through the last ten years of budget balancing actions, the City net reduced over 2,000 positions or 28%, while increasing General Fund departmental budgets by 26% primarily due to higher personnel costs. Looking over the same period, 77% of the position reductions (all funds) occurred in non-public safety departments such as Finance, Human Resources, Information Technology, Library, Parks, Recreation and Neighborhood Services, and Transportation. The General Fund departmental budgets for Police and Fire increased during these ten years by 56% while the General Fund departmental budgets for non-public safety departments decreased by 10%.

In an effort to understand the impact on service levels that these General Fund budget balancing efforts have had and will continue to have on departments throughout the City, this document provides in-depth analysis of service-level reduction and elimination impacts for several departments. See Section IV and Appendix A. While the focus of the discussion in Section IV and Appendix A is limited to the Police, Fire, Library, Parks, Recreation and Neighborhood Services, and select other City services, it is generally representative of City services as a whole.

III. RETIREMENT COSTS

A. Introduction

It is projected that over the next five years, the City's cumulative retirement contributions will exceed $1.8 billion in all funds with projected annual contributions totaling $323.4 million in 2012-2013, increasing to $431 million by 2015-2016.[27] This is not the worst case scenario. As the Retirement Boards for both the Federated and the Police and Fire Retirement Plans continue reviewing actuarial assumptions to make them more realistic, annual required contributions into the retirement funds could very well increase.

This is *not* simply a short term issue. These costs are growing at such a rate and are of such a magnitude that they require an ever-increasing share of the City expenditures regardless of the program or revenue source; it is not only the General Fund impacted by increased retirement pension costs. Retirement reform is needed for the long-term sustainability of the retirement plans and in order to continue to provide even the most basic municipal services to the public.

For the purposes of understanding the root causes and likely outcomes of the City's deteriorating financial condition, it is essential to understand certain aspects of the City's pension and other post-employment benefits (OPEB) (collectively referred to as "retirement"). The key points in this section are the following:

- The City's pension and OPEB costs have been increasing at a rapidly accelerating rate, and have already resulted in broad impairment of the City's services;
- Over the next two to three years, the projected increase in retirement payments is expected to continue at a pace that will overtake most of the City's remaining services;
- The rapid increase in the costs of retirement benefits is due, in part, to increased benefits, but also to numerous factors beyond the City's control, including very large investment losses, the likelihood that the plans will not attain current investment return assumptions, actuarial losses, changes in actuarial assumptions based on experience, and the increasing number of retirees relative to active employees.
- The expected changes in GASB pension accounting rules, while not directly addressing changes in funding, will recognize additional liabilities by requiring public entities to more

[27] Cheiron Five Year Retirement Contribution Projections (August 11, 2011) available online at http://www.piersystem.com/external/content/document/1914/1161647/1/08-12-11%20CMO.PDF; As noted previously, the Budget Office's calculations rely on the Cheiron projections, but also include a prepayment discount that the City receives for the way it administers its retirement payments (resulting in a total of $416 million).

accurately portray their pension liabilities.[28]

- The impact of these factors will worsen over time and contribute to a dramatic increase in the unfunded liabilities of the plans, with a resulting rapid increase in annual retirement costs;
- The increased retirement costs that the City will experience are unsustainable; and therefore,
- Immediate, major intervention is necessary now.

B. How San José's Retirement System Works

The City has two separate retirement systems, each governed by its own Board of Administration. The Police and Fire Department Retirement Plan covers sworn employees in the City's Police and Fire Departments. The Federated City Employees' Retirement System covers all other full-time and certain part-time City employees. Each system maintains its own asset portfolio and provides benefits determined through collective bargaining, and, in the case of police and fire unions, binding interest arbitration.

1. Overview of Pension Benefits

The City provides a pension benefit for retirement system members based on a member's years of service and his or her final average compensation at the time of retirement.[29] The City Charter (Charter) spells out the minimum benefits the City's two retirement plans must provide for current members. The current minimum benefits were approved by San José voters in 1965. The Charter authorizes the City Council, at its discretion, to grant greater or additional pension benefits. For police and fire, in the event that the City is unable to reach agreement with the San José Police Officers' Association or the San José Fire Fighters, International Association of Fire Fighters Local 230 on benefit levels, the parties will submit the matter to an independent arbitrator for binding determination.

The Charter minimum benefit for Police and Fire members is 50% of final compensation at age 55 upon completion of 20 years of service and final compensation is defined as the average compensation in the final three years of service. The Charter minimum benefit for Federated members is 2% of final compensation per year of service for the first 25 years of service, plus 1% for

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[28] As discussed in greater detail below in Section V, B (3), GASB's proposed changes in governmental financial statements will only change the standards for financial reporting. Funding or contribution decisions remain a matter of policy. However, as has been the case in the past, the proposed rule change, specifically with respect to amortization periods, appears to be one that retirement boards will consider in their actuarial policies.

[29] For example, a civilian employee in the Federated Plan with final compensation averaging $80,000 and 30 years of service would received an annual pension of $60,000 (30 x 2.5% x $80,000). This is in contrast to a defined contribution plan such as a 401(k) Plan, whereby retirement benefits are solely determined by the amount of assets available in the funds accumulated over time by employer and employee contributions and investment earnings. Employees in the Police and Fire Plan are eligible for up to 90% of their final average salary.

each year beyond 25. The Charter provides that an employee is eligible for the benefit at age 55, and the benefit is subject to an 85% maximum (or at age 70 regardless of years of service).[30]

Current Base Pension Formulas for the City's Retirement Plans

	Police and Fire	Federated
Age and Years of Service Eligibility	Age 50 with 25 years of service, 55 with 20 years or any age with 30 years	Age 55 with 5 years of service or any age with 30 years
Benefit Formula	2.5% of final compensation for each of the first 20 years of service, plus: Police: 4% per yr of svc in excess of 20 yrs Fire: 3% per yr of svc if 20 or more yrs	2.5% of final compensation for each year of service
Max. allowable benefit	90% of final compensation	75% of final compensation
COLA	Guaranteed 3% per year	Guaranteed 3% per year
Final Compensation	Average base pay of employee's highest 12 consecutive month period with the City; excludes overtime and expense allowances	Average base pay of highest 12 month period with the City;[31] typically does not include overtime or specialty pay

Source: San José Municipal Code.

The Charter authorizes the City Council, at its discretion, to grant greater or additional pension benefits. The following chart shows the chronology of changes made to the City's retirement plans.

Police & Fire Department Retirement Plan			
	Charter Minimum Set in 1965	**Changes**	**Year of Change**
Age and Service Requirement	At 55 with 20 yrs svc or at 65 regardless	At 50 with 20 years of service or at any age with 30 yrs svc	1968
Multiplier	50% of final salary	+ 1.66% per yr in excess of 20	1968
		+ 2.5% per yr in excess of 20	1970
		2.5% of final salary for first 20 yrs svc + 3% per yr in excess 20	1996[32]
		+ 4% per yr in excess of 25	2000

[30] Last year, the City Charter was amended, such that for *new employees*, the City Council may provide a retirement plan or plans that are not subject to the Charter's minimum requirements, including the 8:3 contribution ratio.

[31] Not to exceed 108% of the second highest 12 consecutive months.

[32] This change (awarded through binding interest arbitration) was made in 1998, retroactive to February 1996, for members who were at least 55 at time of retirement or had 30 years of service.

		+ 4% per yr in excess of 20	2006 (Police only)
Maximum (percentage of final salary)	50%	66.66%	1968
		75%	1970
		80%	1998
		85%	2000
		90%	2006 (Police) 2008 (Fire)
Final Salary	Average of last 3 yrs	Highest 12 mos. svc. (capped at 108% of final 12 mos.)	1970
COLA	*Benefit not included in charter*	CPI not to exceed 3%	1970
		Guaranteed 3% per year	2002
Supplemental Retiree Benefit Reserve (SRBR)	*Benefit not included in charter*	Granted	2001
Health Benefits	*Benefit not included in charter*	Granted to Full-time Employees	1984
Dental	*Benefit not included in charter*	Granted to Full-time Employees	1986

Source: Office of the City Auditor, Pension Sustainability: Rising Pension Costs Threaten the City's Ability to Maintain Service Levels – Alternatives For A Sustainable Future (September 2010).

Federated City Employees' Retirement System			
	Charter Minimum Set in 1965	**Current Benefits**	**Year of Change**
Age and Service Requirement	At 55 with 25 years of service	At 55 with 5 years of service or at any age with 30 yrs svc	1975
Multiplier	2% of final salary for first 20 yrs + 1% per yr in excess of 20	2.5% for each year of service	1975
Maximum	85%	75%	1975
Final Salary	Average of last 3 yrs	Highest 12 month period	2001
COLA	*Benefit not included in charter*	CPI not to exceed 3%	1975
		Guaranteed 3% per year	2006
Supplemental Retiree Benefit Reserve (SRBR)	*Benefit not included in charter*	Granted	1986
Health Benefits	*Benefit not included in charter*	Granted to Full-time Employees	1984
Dental	*Benefit not included in charter*	Granted to Full-time Employees	1986

Source: Office of the City Auditor, Pension Sustainability: Rising Pension Costs Threaten the City's Ability to Maintain Service Levels – Alternatives For A Sustainable Future (September 2010).

As a result of these changes, 56% of current Federated pension costs and 50% of Police and Fire pension costs are attributable to benefit enhancements above the charter minimums. The average Federated benefit in 2009 was 169% of what it was a decade earlier, and the average Police and Fire benefit was 175% of what it was a decade earlier.[33]

In addition, retirees receive an annual 3% cost of living adjustment (COLA), regardless of the CPI or the state of the retirement funds. This guaranteed COLA was added to the plans in 2002 (Police and Fire) and in 2006 (Federated), replacing a previous benefit that was tied to the Consumer Price Index (CPI). The City Auditor's analysis estimates that the guaranteed COLA accounts for about 28% of the total cost of the Police and Fire Plan and 26% of the total cost of the Federated Plan.

In 1986, the City Council established the Supplemental Retiree Benefit Reserve (SRBR) for the Federated Plan. The SRBR allocates investment income earned by retirement fund assets that exceeds expected returns to an account that funds new, or supplemental, benefits for retirees. The SRBR was adopted for Police and Fire in 2001. As discussed in detail below, this provision impairs the plans' ability to offset bad years with good years, an important tool for managing large pension funds. Under this system, the SRBR provides a supplemental "13th check" benefit under certain conditions. The pay is in addition to the monthly pension payments, disability and survivor benefits, the annual 3% guaranteed cost of living adjustment and retiree healthcare benefits eligible retirees receive.

Pensions are paid out of retirement funds administered by the Retirement Services Department. Both plans are designed to prefund pension benefits, meaning annual contributions made over the course of an employee's career (by both the City and the employee) along with investment earnings are expected to pay for all future pension benefits. The "normal cost" of pension benefits refers to the contribution amount allocated to an employee's current year of service. The Charter provides that the City must share the normal cost of pension benefits with employees in a ratio of 8:3. In other words, for contributions for retirement benefits allocated to an employee's current year of service, the City pays eight dollars for every three the employee contributes.

Separate and apart from the normal cost, additional payments may be necessary due to market losses, retroactive benefit enhancements, unmet assumptions or other circumstances that may result in plan underfunding. The Charter does not address the allocation of cost between the City and employees for payment of unfunded liabilities. The City currently pays for 100% of the payments attributable to unfunded liability for pension benefits.

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[33] For Federated, the average annual allowance was $20,360 in 1999, compared to $34,537 in 2009. For Police and Fire, the average annual allowance was $38,747 in 1999, compared to $67,984 in 2009. This is the average of all retirees, including beneficiaries.

2. Overview of Other Post-Employment Benefits (OPEB)

The City's retirement plans also provide for other post-employment benefits (OPEB) retiree medical and dental coverage, which were added to the City's plans in 1984 and in 1986, respectively. Generally, employees are eligible for retiree medical insurance coverage after fifteen years of service. Employees are eligible to retire at pre-Medicare age[34] (55 for Federated and 50 for Police and Fire), which contributes to the significant cost of the benefit.

For eligible retirees, the benefit covers 100% of the premium cost for the lowest priced plan available to active employees for either single or family coverage. This is a better benefit than active employees receive (who are required to pay a portion of the premium). This is an anomaly, since retiree healthcare benefits are commonly less than what is provided to active employees and are often a fixed dollar amount rather than being tied to the full cost of premiums for single or family coverage.

The OPEB plans are funded through separate trust funds associated with each of the two retirement systems. Each has its own independent actuarial analysis, so there are contribution rates and funding levels for each OPEB plan. Unlike pension costs, retiree medical costs are shared 50/50 between the City and employees, including payments toward unfunded liabilities.[35] Until recently, the City's OPEB benefits were only very modestly pre-funded, and were primarily funded on a pay-as-you-go basis. However, between 2009 and 2011 the City and its employee groups began phasing into full pre-funding OPEB benefits over a five year period.[36] As of June 30, 2010, the unfunded liability for OPEB benefits was $1.7 billion. The Federated Retiree Healthcare Plan was 12% funded, and the Police and Fire Retiree Healthcare Plan was 6% funded.

C. The City's Retirement Contributions Are Increasing at an Alarming Rate

By any standard, the City's pension and OPEB costs have been increasing, and are expected to continue to accelerate at a dramatic pace. Because of this, over the past 10 years, the City has experienced a profound increase in the percent of payroll that it pays to the retirement plans for retirement benefits. As the chart below demonstrates, the City spent a combined total of $73 million

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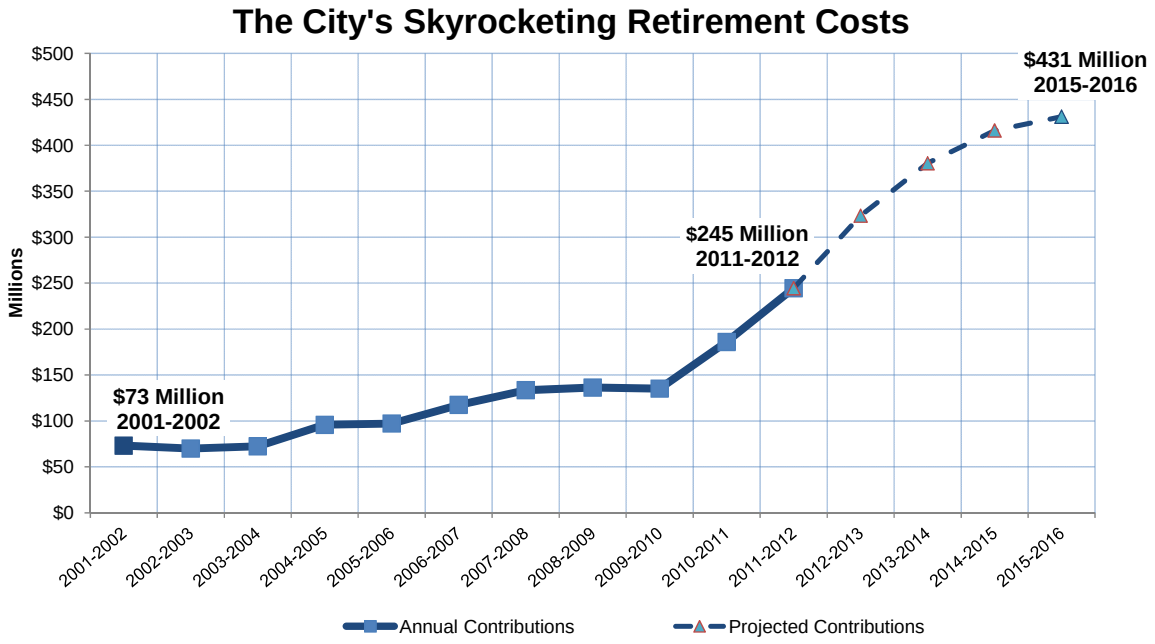
[34] Employees hired prior to April 1, 1986 did not contribute to Medicare and do no not have eligibility based on City employment.

[35] Retiree dental costs, which make up a small amount of OPEB liability, are split at different ratios depending on plan.

[36] For Federated, the annual incremental increase shall not be more than 0.75% of pensionable pay in each fiscal year for employee contributions, and likewise for City contributions. For Police and Fire, the incremental increase is limited to 1.25% of pensionable pay in each fiscal year for employee contributions, and to 1.35% of pensionable pay for City contributions. The Police and Fire agreements include meet and confer obligations if the contribution rates exceed 10% of pensionable pay for employees or 11% of pensionable pay for the City. These limitations may preclude full funding of the annual required contribution within the five year period.

on pension and OPEB benefits in 2001-2002. In 2011-2012, the City spent $245 million on retirement benefits. Absent swift action to reduce the cost of these benefits, by 2015-2016, the City is expected to be required to contribute more than $431 million for pension and OPEB costs in 2015-2016 – only four years from now. This is more than the entire 2011-2012 Operating Budgets for the Fire Department, Office of Economic Development, Department of Transportation, Convention Facilities, Housing, Parks, Recreation and Neighborhood Services, Planning, Building and Code Enforcement, and all City libraries combined.



Sources: City of San José's Adopted Budget 2011-2012; Retirement System Comprehensive Annual Financial Reports 2001-2002 through 2010-2011; Preliminary General Fund Forecast 2012-2013 (November 2011); Fiscal Reform Plan; and Cheiron Memorandum dated July 20, 2011.[37]

Unfortunately, this is not even the worst-case scenario. Future investment losses would increase the unfunded liability, as would actuarial experience losses, and/or decreases in investment earnings assumptions. If the Retirement Boards ultimately determine that new GASB rules should impact how the plans are funded, then, the accounting changes proposed could increase these contribution levels even further.

[37] As noted previously, the Budget Office's calculations rely on the Cheiron projections, but include a prepayment discount that the City receives based on the manner in which it administers its retirement payments (resulting in a total of $416 million).

While these estimates cover all fund sources, the impact on the City's General Fund will be particularly devastating.

Retirement costs are expected to rise from 10.6% of the general fund budget in 2009-2010, to over 30% in 2015-2016.

San Jose's General Fund Employee Retirement Costs					
Year	2007-2008 Adopted Budget	2009-2010 Adopted Budget	2011-2012 Adopted Budget	2013-2014 Forecast*	2015-2016 Forecast*
% of General Fund	9.9%	10.6%	21.8%	28.4%	30.3%
$ Amount of Cost	$ 101,808,373	$ 103,831,982	$ 197,314,432	$ 291,719,659	$ 332,270,406
% Increase Each Year	N/A	2.0%	90.0%	47.8%	13.9%

Source: City Manager's Budget Office.

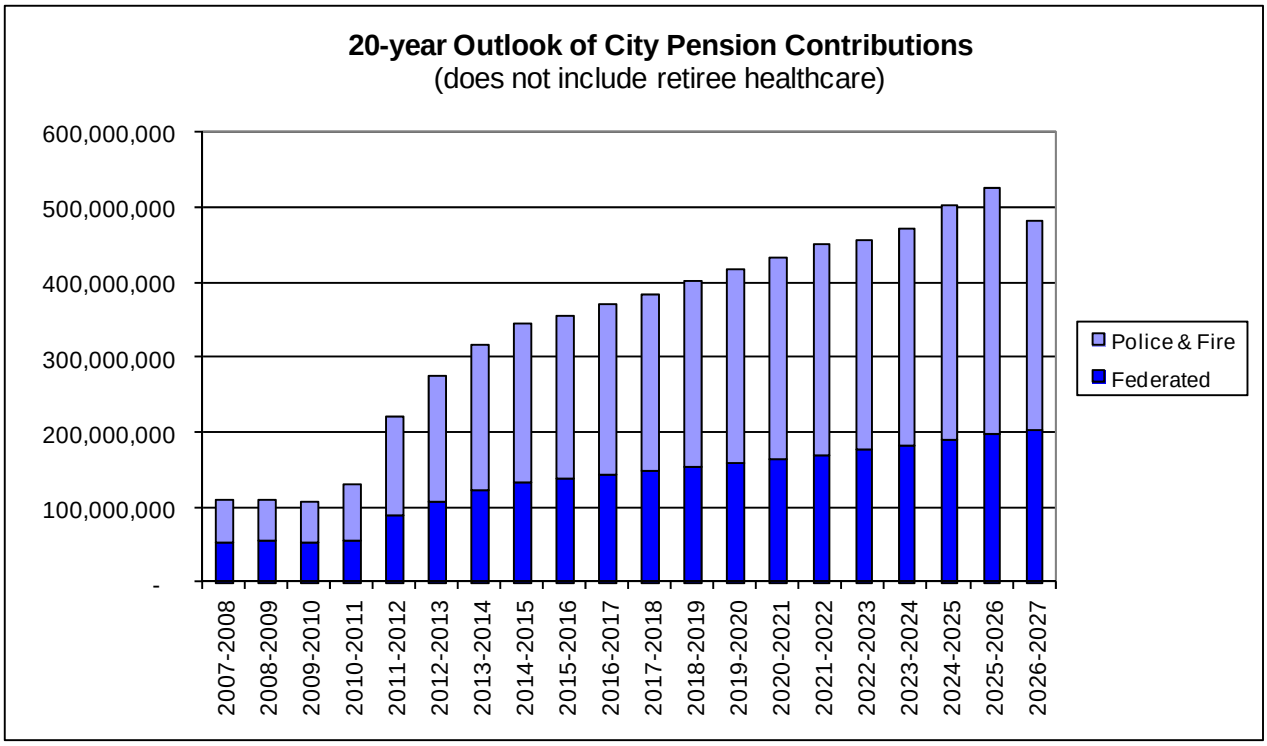
** Assumes costs included as part of the February 2011 Forecast. Retirement numbers have been revised based on updated information from Cheiron (July 20, 2011 report), the actuary for the Retirement Boards.*

As set forth later in this report, the problem is immediate because the City's services were already decimated by declines in revenue, increases in retirement costs, and other cost-drivers. The cuts necessary to pay for the increases over the next several years will require the City to face the unthinkable prospect of closing all of its branch libraries and community centers, while still not having enough money to fund acceptable levels of police and fire protection. The City will be rendered unable to provide even minimally acceptable services.

Although this report focuses on the next five years, it is important to recognize that retirement costs are projected to get worse, not better, unless changes are made to reduce costs.

The chart below shows the projected pension contribution amounts over the next 20 years for these two plans.[38] Importantly, this chart and the 20 year chart that follows do not take into account any further assumption changes that the Boards' trustees may make such as adopting more realistic earnings assumptions and modification to the life expectancy assumption. Such changes may very well cause these numbers to increase.

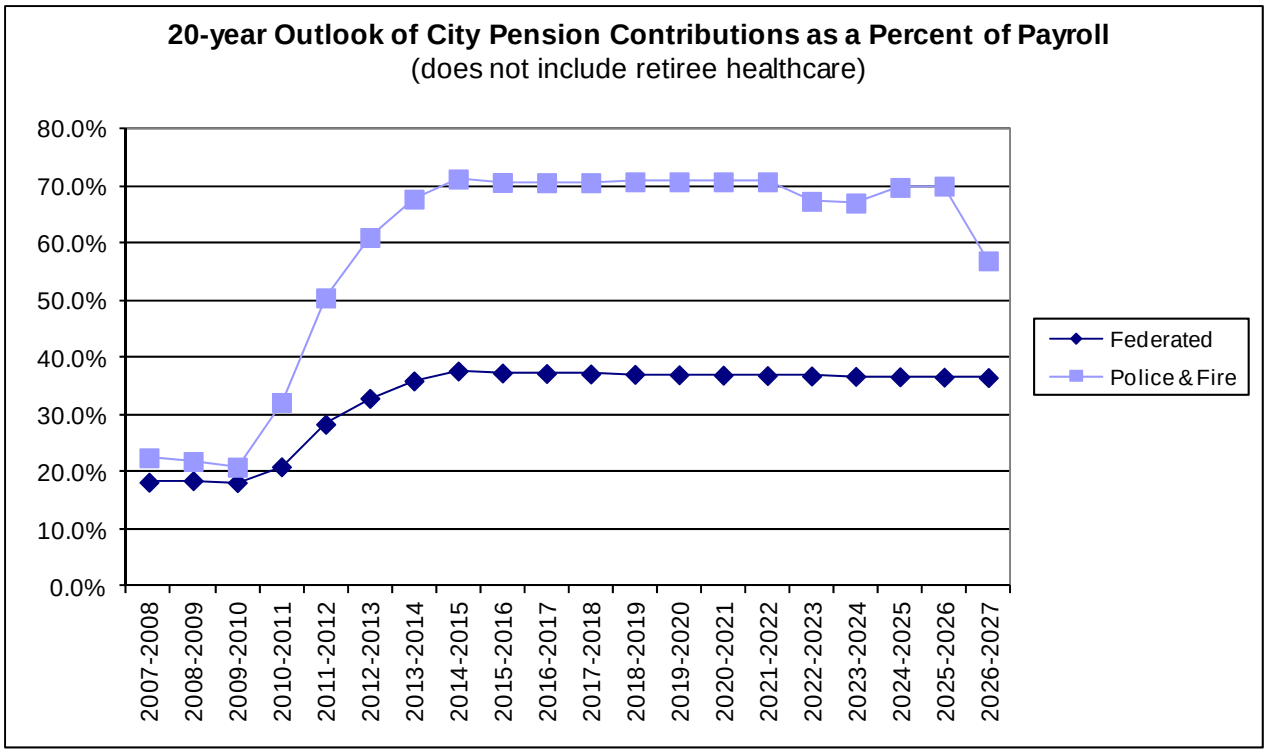
[38] Please note that these charts do not include OPEB contributions, because the City does not have OPEB contribution projections beyond five years out.



Sources: Retirement System Comprehensive Annual Financial Reports and Cheiron Memorandum dated July 20, 2011.

Proposed new accounting standards may require that changes to unfunded liabilities be incorporated into the City's pension expense on an accelerated basis compared to current requirements. Specifically, the City would be required to immediately incorporate into its pension expense any change in liability resulting from the granting of new benefits. Other changes in unfunded liabilities would be recognized immediately for retirees, and amortized over the remaining service lives for active employees. In addition, consistent with the plans' current policies, the City would be required to recognize (smooth) differences between projected and actual earnings over five years for financial reporting purposes. To the extent that the Retirement Boards incorporate any of these changes into funding calculations, this could create even greater cost pressure.

This issue may also be viewed from the perspective of cost as a percent of salary. The chart below shows the pension contribution amount over the next 20 years, reflected as a percentage of payroll.



Sources: Retirement System Comprehensive Annual Financial Reports and Cheiron Memorandum dated July 20, 2011.

The Police and Fire Department Retirement Plan 20-year outlook chart shows a decline starting in 2024. This is because the Police and Fire Department Retirement Plan uses a 16 year amortization period. The Federated Employees' Retirement System chart does not show a decline because the Plan uses a 28 and 20 year layered amortization period and any decline would be in the years past what is shown on the chart. As noted in the beginning of the report, these charts are based on 2010 data.

As set forth below, in 2000-2001, City retirement contribution rates (including both pension and OPEB) are 16% of pay for Federated and more than 15% for Police and Fire. By 2012-2013, however, the City's contribution rates are expected to increase to more than 52% of pay for Federated and to more than 96% of pay for Police and Fire. The key reason for the rapid increase in these rates is that the plans have begun to recognize the losses from the 2008 collapse and from the change in actuarial assumptions.

City Contribution Retirement Rates (as a Percent of Payroll)[39]

	2000-2001	2012-2013
Federated	16.09%	52.09%
Police	15.70%	96.44%
Fire	15.70%	98.62%

Sources: 2000-2001 Comprehensive Annual Financial Report and 2012-2013 Automated Budget System.

These costs are not just rising for the City, they are also escalating for employees. In 2011-2012, City employees are contributing anywhere between 11% and 17% of their base wages to the retirement systems (for both pension and retiree healthcare), and these contributions will consume an even larger portion of employees' paychecks as costs continue to rise.

D. The Primary Cause of The Dramatic Increase In Retirement Costs Is a Significant Increase in Unfunded Liabilities

It is important to recognize that the problems leading to this huge increase in retirement costs cannot be addressed by continuing with business as usual. Absent major changes in the pension and OPEB programs, retirement costs will overtake available resources, rendering the City unable to provide even the most basic services to the public.

In general, the increasing costs of pension benefits are attributable to a dramatic increase in the plans' unfunded liabilities. Because unfunded liabilities must be "amortized" over the remaining life of a retirement plan, the amount that must be contributed to pay off that liability must also increase.

1. Actuarial Methods For Financing Pension Benefits and OPEB

The funded status of a defined benefit retirement plan is a reflection of the plan's overall health. Funded status is determined by comparing the plan's assets (the money available to pay for the benefits) to the present value of the plan's future liabilities (the money which the plan will eventually have to pay out). If Plan Assets (PA) equal or exceed the Actuarial Accrued Liability (AAL), then the plan is fully funded. If the PA is less than the AAL, then the plan is underfunded.

Plan Assets refer to the money you have "in the bank." This is valued in two ways: (1) based on the ***market*** value of assets, and (2) based on the ***actuarial*** ("smoothed") value of assets. The actuarial value discounts the impact of current market conditions by spreading the impact of market gains and losses over a number of years. For instance, a five-year smoothing would spread recent market gains

[39] These rates are before any negotiated employee pickup of a portion of the City's contribution rate. The above rates do not include the pre-payment discount rate. The pre-pay discount refers to a discount the City achieves by paying the full annual required contribution at the beginning of the year rather than throughout the year as the liability is accrued. The discount is calculated taking into account the expected earnings on plan assets, applied to the contributions.

and losses across five years so that one single year's market fluctuations do not result in volatile contribution rates.

A negative difference between the AAL and the PA is the unfunded actuarial accrued liability (UAAL) of the plan. The UAAL is typically calculated in two ways, based on the market value of assets and based on the actuarial value.

The ratio of plan assets to plan liabilities determines the plan's funded ratio. If plan assets are greater than liabilities, then the funded ratio will be over 100%. Alternatively, if plan liabilities exceed plan assets, the funded ratio will be less than 100%.

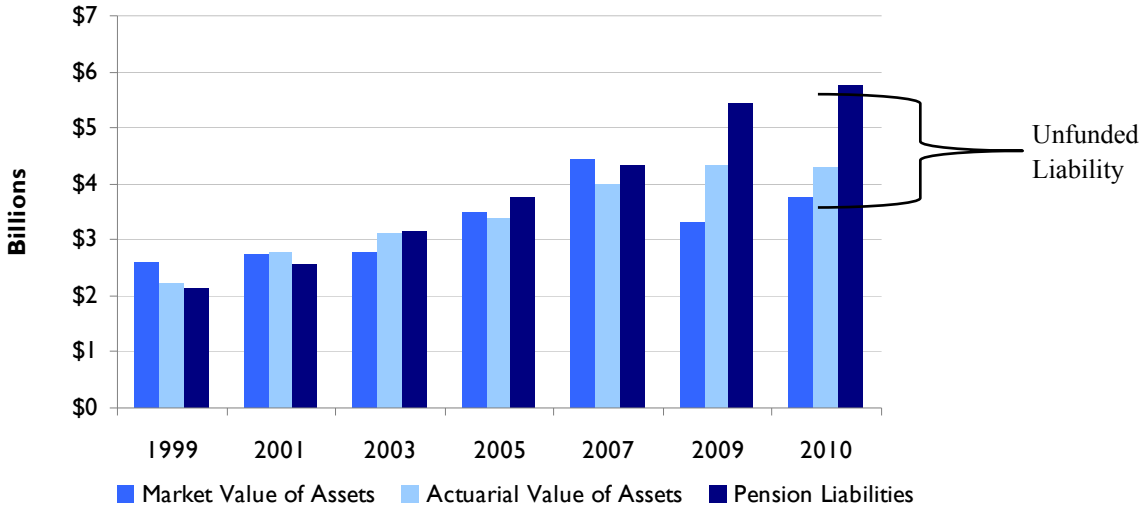
2. The City's Unfunded Liabilities

a. Unfunded Pension Liabilities

The most current estimate of the City's total pension liability is $5.74 billion based on the June 30, 2010 actuarial valuation. In other words, there should be $5.74 billion "in the bank" to assure sufficient funding for pension promises already made. As of June 30, 2010, the two plans had a combined $3.75 billion in assets (market value), or $1.99 billion less than what was needed. Thus, using the market value of assets, the City's unfunded liability for both pension plans totaled approximately $2.0 billion as of June 30, 2010. Using the actuarial value of assets, the City's combined UAAL was $1.43 billion (or, less than the market value because the full effect of recent market losses has not yet been recognized).

The following chart shows the market and actuarial values of the combined plan assets compared to pension liabilities from 1998-1999 through 2009-2010.

Market and Actuarial Values of Plan Assets
Compared to Pension Liabilities 1998-1999 Through 2009-2010



Source: Auditor analysis of retirement plan actuarial valuations, 1999 through 2010.

b. Unfunded OPEB Liabilities

Unlike pension benefits, which have traditionally been (at least partially) funded during the working life of an employee, little money was set aside to pay for retiree health benefits – even though, like pension benefits, an actuarial liability arose. In fact, as GASB's adoption of Statements 43 and 45 in 2004 demonstrated, when actuarial studies were required, many cities and counties found they had a very large liability. In San José's case, this has resulted in an estimated $1.3 billion in unfunded liabilities as a result of promised OPEB benefits.

As of the June 30, 2010 actuarial valuations, the estimated unfunded liability for Police and Fire retiree healthcare (i.e. OPEB) benefits had increased from $706 million (as of June 30, 2009) to $888 million. For Federated, OPEB benefits unfunded liability had increased from $711 million (as of June 30, 2009) to $818 million as of June 30, 2010.[40]

c. Unfunded Liability Equals More Than 500% of Annual Payroll

The table below summarizes the unfunded liabilities of the City's retirement plans.

[40] As of June 30, 2009, the total accrued liability for Federated OPEB benefits was about $796 million; for Police and Fire the total accrued liability was about $762 million.

Unfunded Liability as of June 30, 2010

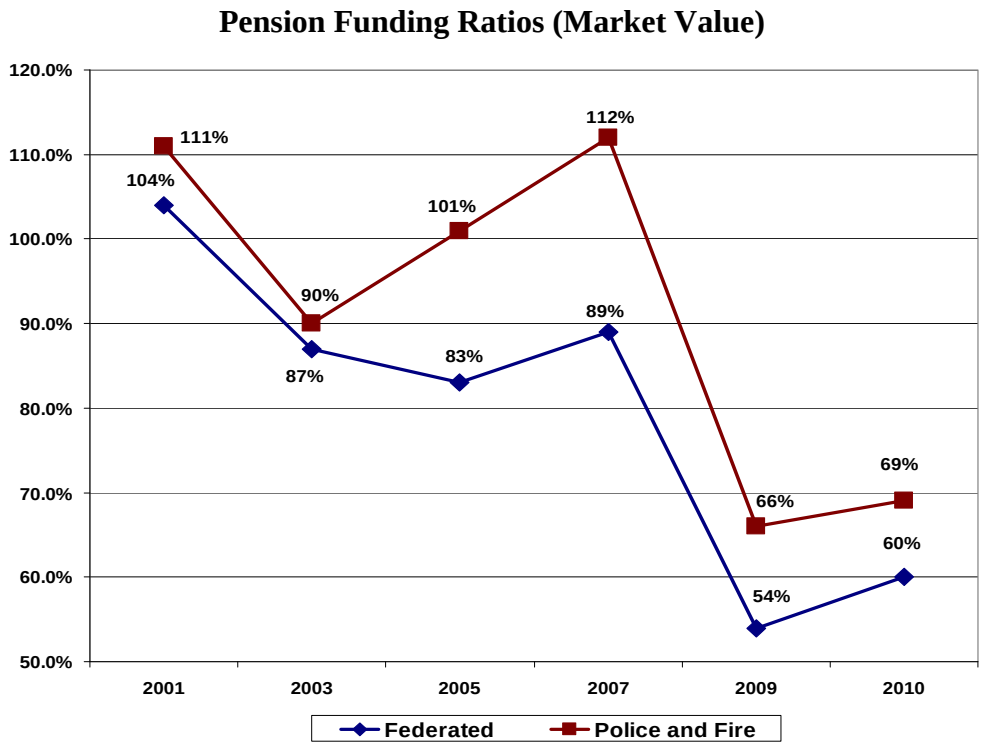
Retirement System/Plan	Pension		Retiree Healthcare (OPEB)		Total Unfunded Liability	
	Market	**Actuarial**	**Market**	**Actuarial**	**Market**	**Actuarial**
Federated	$0.99	$0.78B	$0.82B	$0.82B	$1.81B	$1.60B
Police and Fire	$1.00B	$0.65B	$0.89B	$0.89B	$1.89B	$1.54B
Total	**$1.99**	**$1.43B**	**$1.71B**	**$1.71B**	**$3.70B**	**$3.14B**

Source: City of San José Retirement Services Department.

To put these figures in perspective, for 2011-2012 the City's total annual payroll (for all funds) is $580.3 million ($318.6 million for Federated and $216.7 million for Police and Fire). Thus, the actuarial value of the unfunded liability of the pension and OPEB plans ($3.13 billion) equals more than 500% of the City's annual payroll. These figures greatly exceed the fiscal year General Fund Budget ($906 million) and even exceed the total adopted operating and capital budgets for the City in 2011-2012 ($2.8 billion).

d. Funded Ratios Have Fallen

Adequate funding of a retirement plan is often viewed as a percentage of full funding. As noted earlier, a plan that is fully (100%) funded has all of the assets necessary to pay for the present value of all benefits already earned. The funded ratios of the retirement plans have fallen dramatically, and are the central cause of the crisis the City now faces. This is causing the Retirement Boards, which set the amounts charged for the plans, to set higher and higher rates, which fall predominantly on the City.



Source: City of San José Retirement Services Department.

While both plans were 100% or more funded on a market value basis in 2001, and the Police and Fire Plan was fully funded on a market value basis as recently as 2007, the pension funded ratios as of 2010 are well below accepted norms.[41] On an actuarial basis, San José's pension funded ratios as of 2010 are lower than at any actuarial valuation since at least 1981-1982. Comparing the market value of plan assets to the estimated pension liability, the Police and Fire Plan was 69% funded, and the Federated Plan was 60% funded as of June 30, 2010. OPEB funding ratios are far lower, as actuarial funding was inaugurated only recently.[42]

[41] See for example, U.S. Government Accountability Office, "State and Local Government Pension Plans: Current Structure and Funded Status," GAO-08-983T (July 2008).

[42] As noted in the chart below, the OPEB liability has a funding ratio of only approximately 10%. The City and all employees are contributing so that the benefit can begin to be funded at the level necessary to pay for the benefit. Funding the current retiree healthcare benefit highlights how expensive it is for both the City and the employees.

Funding Ratios – June 30, 2010

Pension Ratios		
	Federated	**Police and Fire**
Market Value	60%	69%
Actuarial Value	69%	80%
Retiree Healthcare (OPEB) Ratios		
	Federated	**Police and Fire**
Market Value	12%	6%
Actuarial Value	12%	6%

Source: June 30, 2010 Actuarial Valuations.

The table above shows both plans' funded status for pension benefits using both the actuarial value and the market value of plan assets. Among other things, the difference between the market and actuarial values illustrates the effect that *smoothing* has on the actuarial value of assets, in this case by deferring the impact of market losses and gains.

E. Underlying Causes of The Increase In Unfunded Liability

There are four major causes of this increase in unfunded liability:

(1) significant increases in benefits beyond the Charter minimums, including supplemental benefits and increased COLAs for retirees, which were not paid for during the working lives of employees receiving benefits;

(2) enormous investment losses, leading to a failure to meet earnings expectations on plan assets;

(3) actuarial losses and changes in actuarial assumptions based on experience, including increased longevity; and

(4) a dramatic increase in the number of retirees and the size of their pensions.

These factors have combined to take the pension plans from being at or above full funding levels during the last decade, to significantly underfunded.

1. The Impact of Improved Benefits

Over the years, the City Council has increased pension benefits dramatically over charter minimums, and has added OPEB benefits. These changes occurred both as a result of bargaining with unions and as a result of binding interest arbitration awards. The impact of these changes cannot be overstated. Generally, these increases fall in a few major categories: (1) increases in pension formulas (age of service, years of service, multiplier, maximum percentage earnable, and calculation

of final compensation); (2) increases in cost of living and other benefits for those already retired (COLA and SRBR); and (3) adding retirement health and dental benefits. Each of these improvements has had a profound impact on the cost of retirement benefits.

Importantly, in the case of virtually every pension improvement, the improved benefits have been applied to an employee's full service with the City, including service which occurred before the change. These retroactive adjustments have a direct impact on the City's unfunded liability. As an example, consider an employee whose pension formula is enhanced after 29 years of service. For this employee, the City and the employee had contributed to the plan at the lower rate for 29 years. Then, the employee's formula is converted to the higher rate retroactively, regardless of years served under the lower benefit plan. Therefore, neither the City nor the employee contributed to the plan for 29 years at the level necessary to fund the higher level of benefit that this employee will now receive for all 30 years of service when the employee retires a year later. This difference gets added directly to the unfunded liability.

a. Pension Formulas

With respect to pension formulas, the most dramatic changes have occurred in the Police and Fire Plan. The Charter requires that Police and Fire members may earn up to 50% of their final salary. Currently, they may earn up to 90% of final salary. In addition, the minimum retirement age has been lowered from 55 to 50.

The City changed the determination of final compensation from highest three-year average compensation to highest 12-month average compensation for both plans. Although the highest one-year provision took effect in 1970 for Police and Fire, the Federated benefit was changed more recently, in 2001. The City Auditor's analysis estimates the cost of determining final salary from the highest one-year average salary versus the highest three-year average salary accounts for about 6% and 4% of the total plan costs for Police and Fire and Federated respectively.[43]

b. COLA and SRBR

Arguably, the most profound and costly deviation from the charter is the cost of living allowance (COLA). San José's pension plans guarantee annual cost-of-living increases, even in the first year of members' retirement. The current system provides that all pensions receive an automatic 3% increase, regardless of actual changes in the cost of living. Because the COLA is effective on a date certain for each plan, a Police and Fire member can retire on January 31st at 90% of salary and on February 1st – the COLA adjustment effective date – receive a 3% increase, resulting in a pension of 92.7% of final salary.

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[43] The City Auditor's Office has previously recommended the City return to using a three year average in pension calculations rather than the highest compensation earnable in any twelve month period.

This guaranteed COLA was negotiated in 2002 for Police and Fire and in 2006 for Federated. It replaced a previous benefit that was tied to the Consumer Price Index (CPI) and capped at 3%. In years that the CPI was greater than 3%, the excess was banked to offset years in which the CPI was lower than that mark. The City Auditor's analysis estimates the guaranteed COLA accounts for about 28% of the total cost of the Police and Fire Plan and 26% of the total cost of the Federated plan.

The impact of the Supplemental Retiree Benefit Reserve (SRBR) is also considerable. The Police and Fire Retirement Plan SRBR was established in 2002 and the Federated SRBR was established in 1986. Each plan had a funded ratio greater than 100% the year their respective SRBRs were established. These SRBRs provide a supplemental "13th check" benefit under certain conditions as specified in the Municipal Code.[44] The pay is in addition to the monthly pension payments, disability and survivor benefits, annual 3% guaranteed COLA and retiree healthcare benefits eligible retirees receive.

The SRBRs allow for supplemental benefits to retirees which are derived from plan "excess" earnings. When the plans' actual investment returns exceed the expected returns, then a portion is siphoned off into the SRBR for later distribution as a supplemental benefit. Regardless of the unfunded liability in each plan, the SRBR can still result in the distribution of SRBR payments to retirees. This is because, under the current definition, "excess" earnings can be declared and transferred to the SRBR even if other actuarial assumptions have not been met and even if the plans are significantly underfunded, as they are currently. As such, the SRBR reduces returns in the good years, reducing the ability of the plans to offset bad years with earnings from good years.

The City Auditor's analysis estimates that SRBRs account for about 4% of the total cost of each plan. Put another way, the cost to the Retirement Funds to siphon off excess earnings to the SRBR is about 0.3% of earnings. That is, if the plan is normally expected to earn 8% in investment earnings in the long term, it will need to actually earn about 8.3% to account for SRBR transfers for the years when the plan exceeded 8.0%. No provision was made by the plan trustees at the time of these changes to reduce the discount rate for this impairment of the funds' ability to earn income, which resulted in insufficient contribution rates all these years and an actuarial shortfall that must now be restored to the plans.

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[44] The parameters for when each plan makes a distribution to retirees differ and distributions are not made every year. In general, when distributions are made, the amount per retiree depends on years of service and years retired. As of June 30, 2010, the balance in the SRBR for Police and Fire is $32.1 million and for Federated is $28.3 million.

c. OPEB (Retiree Health and Dental) Benefits

As discussed above, the Charter does not require the payment of retiree health and dental benefits. At the time those benefits were granted, their cost was minimal, and it is safe to assume that no one involved fully anticipated the long-term consequences. Over time, of course, the cost of medical benefits has skyrocketed, and the problem is compounded by lower retirement ages, meaning more years before a retiree, who is eligible to receive Medicare, is covered by Medicare. As a result, as noted previously, the City has an estimated $1.7 billion in unfunded liabilities resulting from promised OPEB benefits.

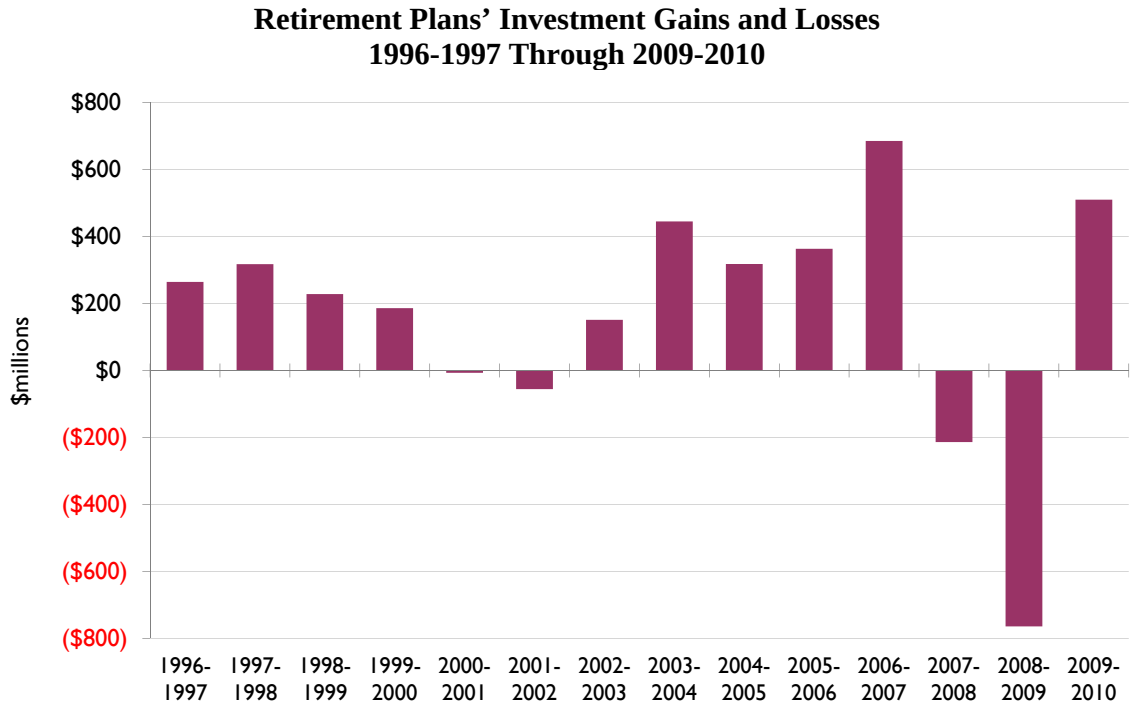
Pursuant to the Municipal Code, 50% of retiree medical costs belongs to the City's employees, and, between 2009 and 2011, the City and employee unions began pre-funding the City's OPEB obligations over a 30 year closed amortization period. That pre-funding will be phased in over 5 years. Fully funding the annual OPEB obligation alone (that is, fully funding the annual required payment over the next 28-30 years) is predicted to increase the City's costs by $35 million – from $40 million in 2011-2012, to $75 million per year by 2015-2016.

2. Failure To Meet Earnings Expectations

The cost of increasing pension benefits was masked, to some degree, during the decade preceding 2008 because of rising equity markets, leading to both plans becoming fully funded. However, with the recession beginning in 2008, the plans became underfunded rapidly, and are not expected to recover quickly.

By far the largest variable responsible for the huge increase in unfunded liabilities is the failure of the plans to achieve the annual earning assumptions on which the plans have been premised. The Police and Fire Plan assumes annual earnings on investment of 7.75% for the June 30, 2010 valuation. Until 2009, the Federated Plan assumed earnings of 8.25%. In 2009, the Federated Retirement Board began phasing in a reduction of the earnings assumption to 7.75%. From 2006-2007 to 2008-2009, 77% of the new unfunded pension liabilities were caused by investment losses and adjustments. As this report goes to publication, the Federated Retirement Board has adjusted its assumed earnings rate to 7.50%.

The following exhibit shows the investment gains and losses from 1996-1997 through 2009-2010.



Sources: Comprehensive Annual Financial Reports, Police and Fire Department Retirement Plan and Federated City Employees' Retirement System, 1996-1997 through 2009-2010.

Critically, the Federated Plan lost 3.1% in 2008 and 16.8% in 2009. The Police and Fire Plan lost 5.1% in 2008 and 18% in 2009. And these numbers only tell part of the story. Because the plans' assumed rates of return were between 7.75 and 8.25% in those years, the effective loss between *what was earned* and *what was expected to be earned* was 36% for Federated and 39% for Police and Fire.

Even strong returns are unlikely to be able to make up for recent market losses. During 2009-2010, each plan saw strong net investment returns, 15.3% for Federated and 13.7% for Police and Fire. Even stronger returns were realized in 2010-2011. However, it would take extraordinary returns over a sustained period to make up for the very severe losses in calendar years 2008 and 2009 – and few are predicting such returns. Indeed, even the very positive returns for 2010-2011 have undoubtedly been eroded by declines in the equities markets since June 2011.

The problem is made more intractable because of the nature of compounded interest. To illustrate: If a $100 investment loses 20% of its value in year one, the balance is $80. If, in year two, the investment earns a 20% return, then the value of the investment is only $96, not $100. To get back to even, the investment would need to earn a 25% return on investment in the second year ($20 divided by $80). And this won't be "even" because plan liabilities will have increased in the ensuing year, by approximately the discount rate (7.75%). Thus, the funding ratio can only be restored with a 35% market increase to compensate for a 20% decline.

Because the plans are mature with negative cash flow from contributions versus disbursements, to be sustainable, investment earnings must account for a large portion of the additions to the retirement funds.

Nationally, the trend for earnings assumptions has been downward, to reflect: (a) the lower yields on bonds comprising 30-40% of pension portfolios, and (b) reduced expectations for equity (stock) investments given the global overhang of sovereign and consumer debt. If the Boards react to this by reducing the actuarially assumed investment rates of return, the UAAL for the plans would increase because the difference would need to be made up in contributions. On the other hand, if the Boards were to leave the earnings assumptions unchanged, and the actual rate of return on invested assets falls below the plans' assumptions, then the UAAL would increase due to the disparity between actual investment results and the actuarially assumed investment rates of return.

Either way, the amortization of those differences would increase the City's annual required contribution beyond current projections.

3. Changes In Actuarial Assumptions Based on Experience and Proposed Accounting Standards from GASB

While a change in the assumed rate of earnings would have the most significant effect (among actuarial changes) on the plans' funding needs, other actuarial assumptions have also increased the cost of the plans. Most notably, in 2007 and 2009, new post-retirement mortality assumptions were adopted by the Boards to reflect longer life expectancies.

Pension costs may ultimately increase even more under new accounting standards with shorter UAAL amortization periods.[45] The Governmental Accounting Standards Board (GASB) has released its Exposure Draft of proposed changes in pension accounting and financial reporting standards for state and local governments.[46] Importantly, the City is not required to actually change its amortization periods to meet the new GASB standards at this time. However, anticipating these changes must inform the City's decisions today. GASB's stated goals are to improve the visibility and quality of pension information in governmental financial statements and to encourage intergenerational equity. These far-reaching changes impact every public employer providing pensions to employees. Parallel standards are expected to eventually extend to OPEB plans, including retiree medical benefits arrangements.

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[45] The proposed new rules are currently in an exposure draft and will soon undergo a comments period. While the rules have not yet been finalized or adopted, the City must consider potential impacts on its accounting for liabilities that the rule change may have.

[46] The GASB Exposure Drafts can be found at: http://www.gasb.org/cs/ContentServer?site=GASB&c=Page&pagename=GASB%2FPage%2FGASBSectionPage&cid=1175804830991.

These proposed changes in governmental accounting standards encourage the City to shorten its 16 to 20 year amortization periods to levels as low as 12 to 15 years, so that unfunded liabilities are liquidated before the employees retire. If the Retirement Boards determine that these changes apply to funding, the financial impact on the City would be dramatic; cost-driver projections over the next few years would be even higher than the data shown elsewhere in this report.

4. Increase in the Number of Retirees

Another major factor in the increase in pension costs – and one that will get significantly worse over time – is the rising number of retirees relative to active employees. As the Pew Center has observed, "When a pension system is fully funded, the ratio of workers to retirees matters little, because the money for retirees is already in the bank. But when a plan is underfunded, making the payouts can become extremely burdensome."[47]

The declining ratio of employees to retirees and beneficiaries creates a risk of even higher future contribution rates. This means that the annual cost to pay down the unfunded liability is spread across fewer active employees. The following chart shows the steady, declining trend in this ratio. Some examples from this dataset are helpful to consider.

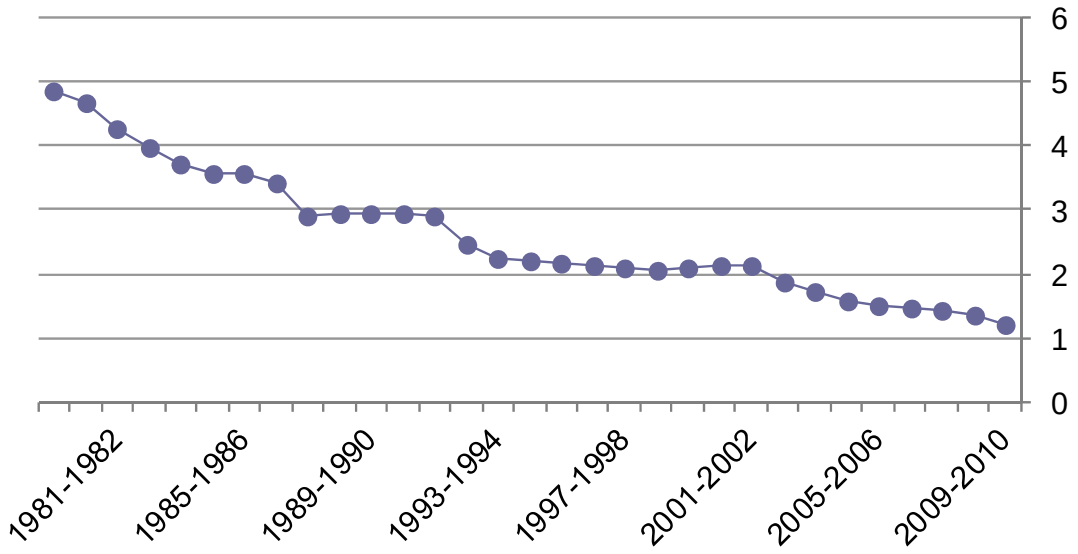
	Active Employees	Retirees / Beneficiaries	Ratio
1979-1980	3,941	784	5:1
1990-1991	5,500	1,750	3:1
2009-2010	6,660	4,891	1.4:1

Source: City Auditor analysis of data from Retirement Plan Comprehensive Annual Financial Statements.

Thirty years ago, there were about 5 active employees for every one retiree / beneficiary; ten years later, that ratio had fallen to 3 to 1. In 2009-2010, the ratio further declined to 1.4 to 1. This number will soon be 1 to 1. The City anticipates this trend will continue such that there will soon be more retiree / beneficiaries than active employees. The chart below shows the decline in the ratio of employees to retirees since the early 1980s.

[47] The Pew Center on the States, "Promises with a Price" (December 2007) (footnote from original quotation omitted).

Decline in the Ratio of Employees to Retirees and Beneficiaries 1980-1981 Through 2009-2010



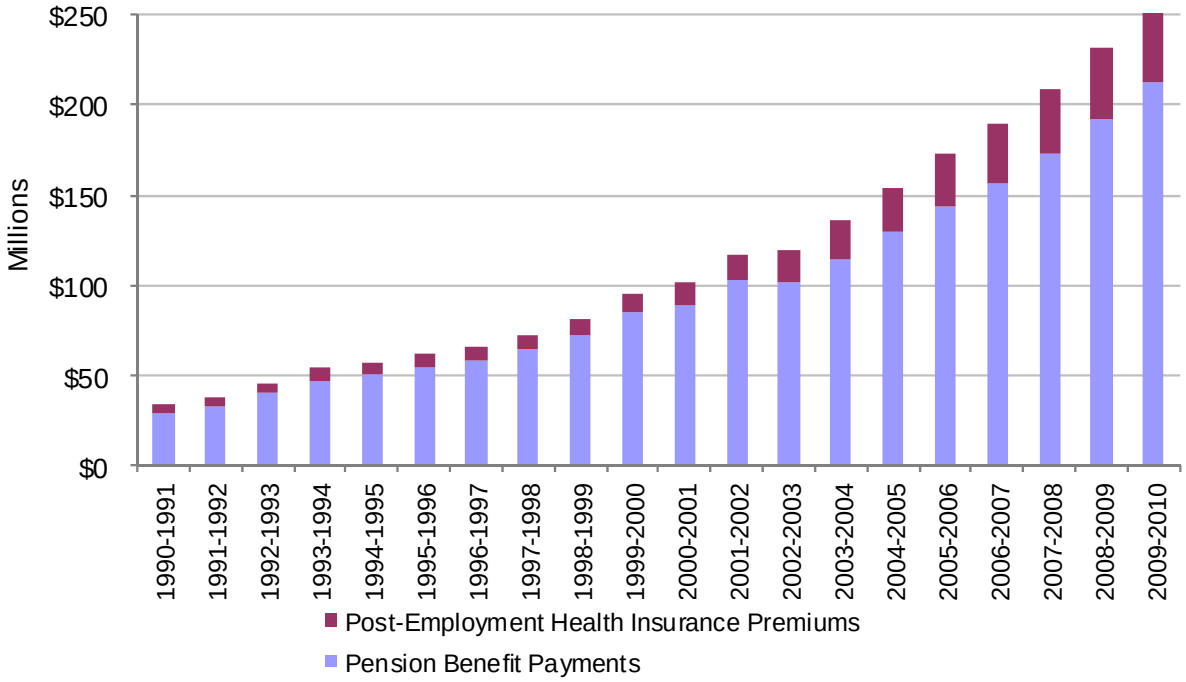
Sources: City Auditor analysis of data from Retirement Plan Comprehensive Annual Financial Statements, 1980-1981 through 2009-2010.

Recently, the Retirement Boards approved a methodology change regarding the City's Annual Required Contribution (ARC) to the Retirement Plans by requiring the City to pay a fixed minimum annual contribution amount versus a percentage rate of payroll. Starting with 2011-2012, the City's budgetary contribution rates are set to ensure the full funding of the fixed minimum Annual Required Contribution.

In San José, as the number of active employees as a percentage of overall pension plan membership has decreased, the payments for retirees out of the plans have exceeded payments by active employees into the plans. The negative effect of this maturation of the plans during a down market cannot be overstated. As a result of the confluence of events, the impact of negative investment performance is exaggerated because the system has a negative cash flow. With not enough new money flowing in, the system is forced to sell assets at historically low values, when it should be "buying low" in anticipation of the eventual market recovery. Now the cost of recovering from a recessionary market decline escalates.

Moreover, the increase in the number of retirees and the increase in the size of retirement benefits have a synergistic effect. All told, there has been a *seven-fold* increase in the total retirement benefits paid out of retirement funds in the last 20 years. This is in part because the average annual pension benefit increased by about 175% for Police and Fire and by 150% for Federated, and in part because the number of beneficiaries is two and a half times larger than it was in 1990-1991.

Retirement and Other Post-Employment Benefit Payments
1990-1991 Through 2009-2010



Sources: Comprehensive Annual Financial Reports, Police and Fire Department Retirement Plan and Federated City Employees' Retirement System, 1990-1991 through 2009-2010.

In 2009-2010, the retirement plans paid out more than $210 million in pension benefits, compared to $72 million in 1998-1999 and $30 million in 1990-1991.[48] Over that same time, the number of retirees and beneficiaries grew from 1,816 to 4,891. These trends are likely to continue into the future as approximately one-third of the City's workforce was within five years of retirement eligibility as of August 2011.

5. Pension Benefit Payments Have Exceeded Contributions Since 2001

Largely as a result of the increased number of retirees and increases in benefit levels, pension benefits have exceeded contributions since 2001, and the gap between contributions and the amounts paid out has grown.

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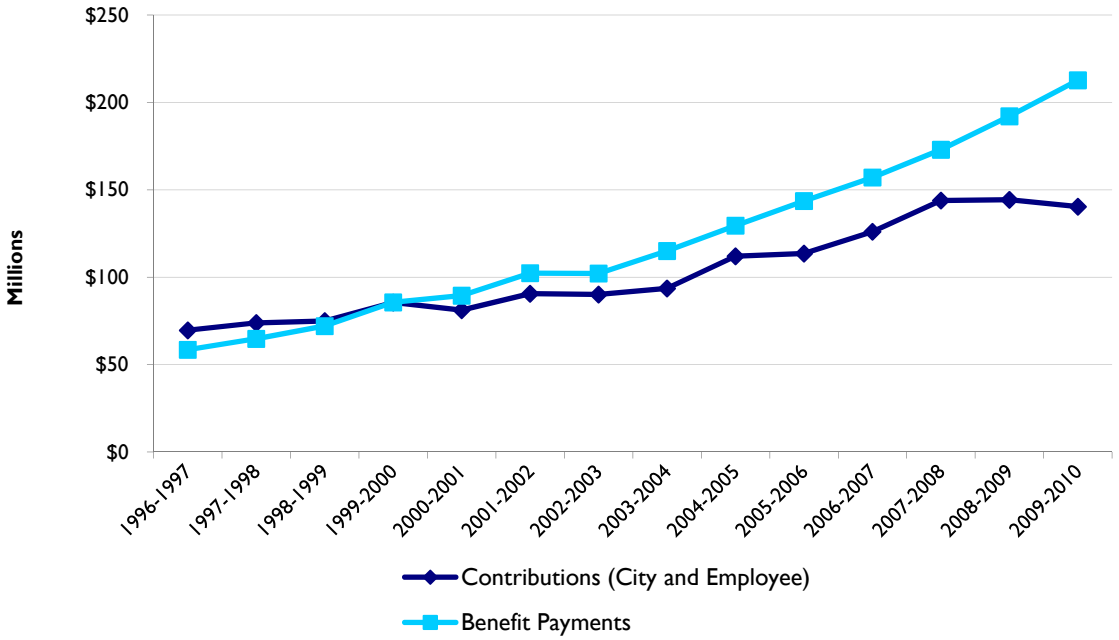
[48] These figures are unadjusted for inflation and do not include payments for other post-employment benefits such as the cost for retiree health and dental benefits. In 2008-2009, the Retirement Plans paid nearly $40 million for post-employment health insurance premiums.

Pension Benefit Payments Have Exceeded Contributions Since 2001



Sources: Comprehensive Annual Financial Reports, Police and Fire Department Retirement Plan and Federated City Employees' Retirement System, 2006-2007 through 2009-2010.

This further draws down the plan's assets. Even if investments yield expected returns, pension obligations are expected to grow much faster than available plan assets unless contribution rates are raised.

6. Unfunded Liabilities

As the number of retirees and life expectancies increased and the City enhanced benefits, the City's pension liabilities grew dramatically. In 1999, the City had an estimated $2.1 billion in pension liabilities. By 2010, the City had an estimated $5.74 billion in pension liabilities.

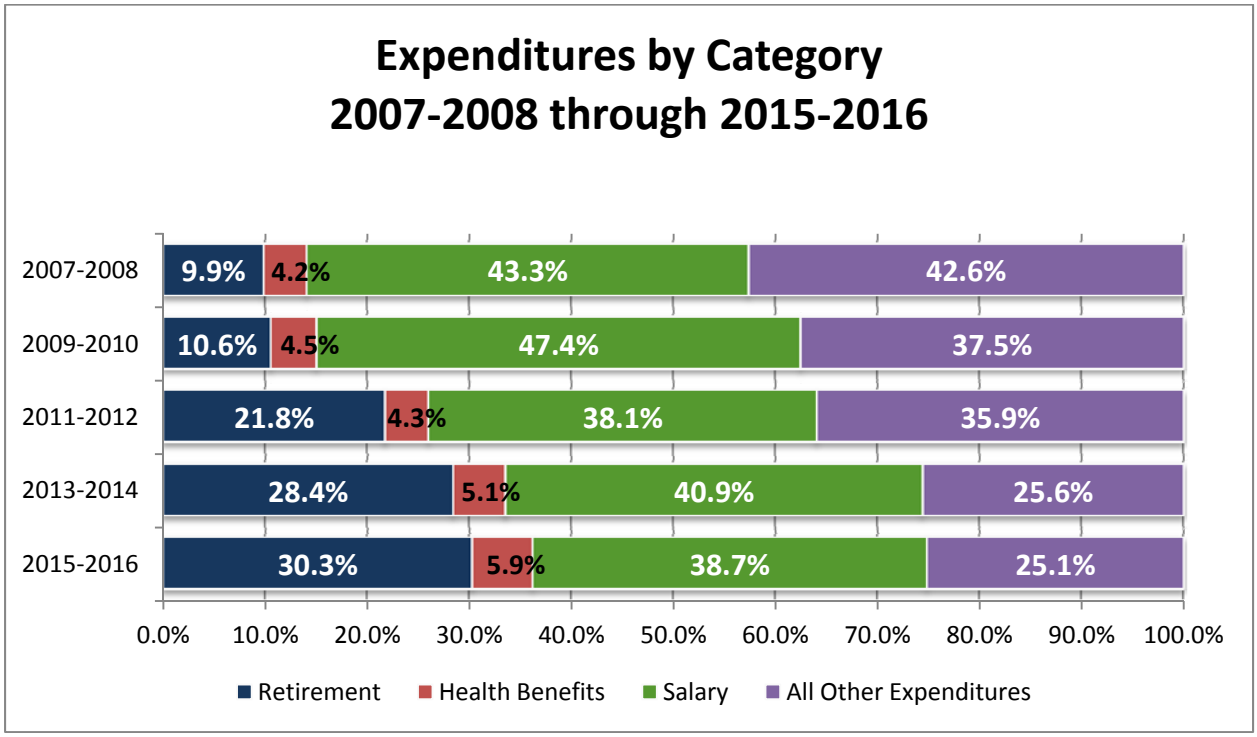
Although the City and its employees have deposited substantial sums into the retirement plans (generally fully funding the annual required contributions established by the independent boards of its retirement plans), San José is underfunded by approximately $2.0 billion on a market value basis. This means that San José is nearly $2 billion short of how much money it should *already* have set aside to pay benefits already earned by its pension system members.

To properly fund retirements, those shortfalls must be paid into the system by the City and its employees during their remaining service periods before retirement. That is impossible to accomplish without draconian cuts to employee compensation and citywide services.

F. Conclusion

According to the City Administration's economic forecasts, without significant retirement reforms, pension and OPEB contributions are expected to amount to roughly 28.5% of total General Fund Expenditures by 2015-2016 (totaling about $304.5 million). By comparison, these contributions accounted for 6% of General Fund Expenditures in 2000-2001. In 2009-2010, this percentage had jumped to 10.6%; in 2011-2012, it had doubled to 21.8%. These increases occurred despite the significant headcount reductions over this period of time.

The chart below shows the proportion of personnel costs, retirement and OPEB contributions, and other expenditures in the General Fund.



Sources: City of San José Adopted Budgets 2007-2008 through 2011-2012 and February 2011 Five-Year Forecast;For 2011-2012, a final reconciliation will be completed as part of the Annual Report in Fall 2011 in order to fund the annual required contribution based on restored costs included in the 2011-2012 Adopted Budget.

This point is critical. Fitch Ratings, for example, has indicated that they will now be carefully evaluating when pension contributions (excluding OPEB) exceed 10% of an entity's operating budget. The City of San José has now passed, and is poised to dramatically exceed, that threshold.[49]

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[49] "Enhancing the Analysis of U.S. State and Local Government Pension Obligations," Fitch Ratings [available at www.fitchratings.com] (February 17, 2011).

The following excerpt from a Fitch Ratings special report, addresses this budget threshold which is viewed to be of rating agency concern:[50]

> *"Fitch considers the level of pension contributions not only as a percentage of ARC, but also as a percentage of the rated entity's budget over time… Assessing the contributions against the general fund, in the case of most entities, provides an indication of the affordability of the pension commitments and whether spending for pensions is or could be expected to start crowding out spending for other needs."*

In absolute dollars, San José's General Fund employee pension costs have risen from $103.8 million in 2009-2010 to $197.3 million by 2011-2012, and are projected to reach $304.5 million by 2015-2016 if no reforms are adopted – in total, a $200.7 million increase in annual spending.

Unsustainable retirement costs are not San José's problem alone. Retirement costs have skyrocketed across the country. Concern about how to pay for retirement benefits is a national issue. What is important to grasp from these increases is that the City has worked very hard to absorb these increases to date. There have been severe consequences to this: cutting staff and reducing or eliminating services (discussed at length above and in the following section). Following those efforts, the City is already far below historical levels for both Police and Fire and for other government services. It cannot absorb further increases without devastating its ability to provide services. And yet, the structural imbalance remains and the retirement cost projections indicate that further increases are large and inevitable without immediate intervention. The City Administration believes that the City has exhausted its capacity to pay for the next projected jump in retirement costs by using traditional methods.

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[50] Fitch Ratings, "Enhancing the Analysis of U.S. State and Local Government Pension Obligations" (February 17, 2011).

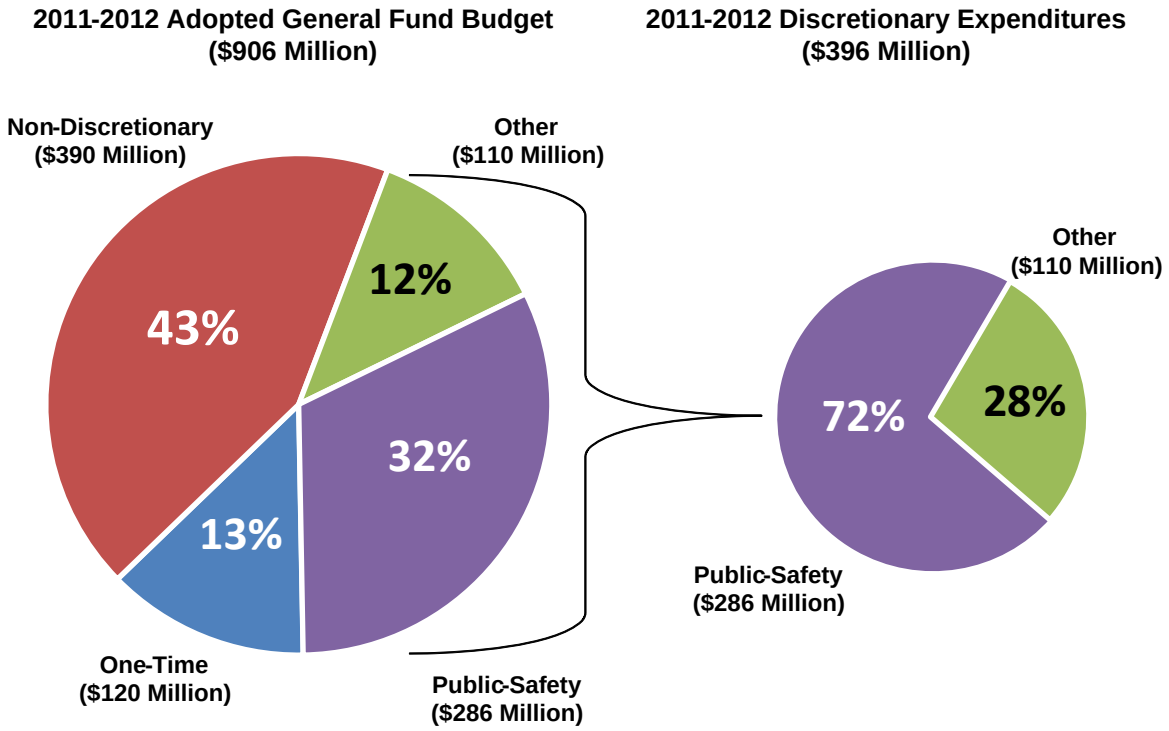
IV. SERVICE IMPACT ANALYSIS

The dramatic rise in retirement costs, coupled with declines in revenues as a result of the severe recession, have forced the City to make difficult and drastic cuts to essential services. Unfortunately, that rise in costs is expected to continue for the foreseeable future. The City continues to face a structural deficit that must be addressed once and for all in order to balance its budget. With limited revenue options, expenditure cuts are the most likely option for addressing that deficit. If expenditure reductions are not achieved through retirement reform or other cost savings measures, then they will have to be achieved through service-level cuts.

To mitigate the impact of such cuts in core municipal services, the City will continue to explore and aggressively pursue strategies to further improve efficiency and cost-effectiveness. Such approaches will include further review of non-personal/equipment costs and contract renegotiation, overtime analysis and reduction, fee adjustments to achieve optimal cost recovery, outsourcing and service delivery model changes, and the sale, lease, and/or re-use of municipal assets. After a decade of budget shortfalls and commensurate gap-closing actions, however, many such strategies have already been utilized and it is not expected that the additional work that will be completed in these areas will generate sufficient savings or revenues in the short term.

Further, the City's cost containment options are significantly limited by the high percentage of the City's General Fund Budget that is non-discretionary in character. Non-discretionary expenditures include those expenses that the City is customarily required to pay – such as debt service, retirement, and workers' compensation costs. In addition, non-discretionary expenditures include grant, reimbursement, or fee related expenses, where cutting such costs would have a net-zero effect on the General Fund.

On the left hand side of the following chart, based on the 2011-2012 Adopted Budget, 43% ($390 million) of the City's Adopted General Fund Budget is shown to be non-discretionary. After further factoring out the portion of the budget allocated to one-time expenses, including reserves, one-time grants and carryover projects, only 44% ($396 million) remains as discretionary expenditures.



On the right hand side of the chart, among such remaining "discretionary" expenses, public safety now makes up 72% ($286 million) of the Adopted Budget, with only 28% ($110 million) remaining for all other City services. Accordingly, unless the cost of non-discretionary expenditures can be reduced, the City must look to this remaining $396 million of spending – again, primarily dedicated to public safety -- to identify additional budget balancing solutions. Within this context, after ten consecutive years of budget reductions, continued shortfalls will require additional and severe cuts to core City services – to the extent that no acceptable service-level reductions choices remain.

In the early years of the budget shortfalls, reductions were focused on lower priority services. In recent years, however, significant reductions to the City's highest priority services, including public safety, have been unavoidable. In addition, several new City facilities, including the Police sub-station, four branch libraries, and one community center, remain closed due to lack of funding to operate these facilities.[51] Based on projected General Fund shortfalls for the next four years currently estimated at $116 million, continued service reductions are anticipated, with limited options now available to reduce those services without jeopardizing the primary functions performed by the City.

[51] These facilities were constructed following the passage of bond measures.

To appreciate the practical impact of these and potential future cuts on service levels, the Administration has worked closely with the Police, Fire, Library and Parks, Recreation & Neighborhood Services departments in developing this analysis. Cuts in these departments are highlighted because they would be the most visible service reductions noticeable to the community, and because they are among the departments identified in the City Charter as core to the operation and functioning of San José. This analysis is in no way intended to downplay the very real and severe cuts to other City departments and service areas. As noted earlier, the General Fund budget shortfall will also force similarly drastic reductions in the General Government departments without which the Police, Fire, Libraries and Parks, Recreation & Neighborhood Services departments could not function. And other departments are affected, as well. For example, the City has been unable to invest in street maintenance at nearly the level it should, an underinvestment that will result in the further deterioration of the City's roadways, which will lead to significantly higher long-term costs.

The budgetary cuts projected for the foreseeable future will severely reduce and potentially eliminate vital City-wide services. These impacts go beyond diminished social and economic benefits. The viability of the City is on the line.

A. Impacts on the Police Department

The San José Police Department (SJPD) has traditionally operated with lean staffing levels when compared to other large cities in the nation. In recent years, SJPD's staffing levels have fallen even further. Although the Department's budgeted dollars have remained relatively stable since 2007-2008, operating costs have increased by roughly $62 million. As a consequence, SJPD has cut 308 sworn positions – over 20% of its sworn police force – in the past four years.

If budget reductions at the level identified in the budget balancing scenario are necessary, SJPD will have to eliminate another 177 sworn positions through 2014-2015. The Department is already operating with the lowest level of civilian staffing determined to be feasible, and additional position cuts will have to come directly from sworn personnel in patrol, investigations, and community policing operations. Because the Department has already absorbed significant cuts in the past several years, further reductions in staffing and service levels would be unsustainable.

The two most critical responsibilities a police department has are responding to 911 calls and investigating crimes. Extended response times will reduce productivity, increase victimization, and decrease citizen satisfaction. With the projected additional reductions, the Department will become a reactive policing department. Over time San José will likely experience an increase in crime, including a more dramatic increase in street-level crime and quality of life issues.

Response times have already been on the rise over the past few years for events of all priority levels. These increases have occurred despite the implementation of time-saving GPS technology. Response times to Priority 1 calls, which involve an ongoing threat to life, now exceed the Department's target of six minutes. Under the proposed budget cuts, SJPD's response times will only grow beyond their

already unacceptable levels. By 2014-2015, it may take over eight minutes to respond to a Priority 1 call.

For Priority 2 calls, which may involve a crime in progress, response times have increased by 42% to over sixteen minutes. With the budget cuts projected over the next few years, the Department anticipates that the response time for these calls may increase to more than half an hour. Estimated wait times for Priority 3 and 4 calls (the lowest priority calls) is currently at about 45 minutes, and is expected to exceed 105 and 130 minutes, respectively.

Due to reduced staffing levels, the Department has already stopped responding to some low-level, non-priority calls for service. With the projected budget cuts, the number of these occasions will only increase. According to anecdotal reports from officers, community members have already indicated that they may not report a crime because they expect a delayed or inadequate response. Moreover, the Department has been forced to shift from a proactive policing to a more reactive approach. Officer-initiated calls and stops have decreased in recent years, and the number of SJPD officers assigned to community policing and outreach has been significantly reduced. This diminished proactive presence is likely to lead to residents feeling less safe, a perception that the police force is less effective, and a potential increase in criminal activity.

Under the projected budget reductions, departmental reprioritization will extend to investigations, where many misdemeanor crimes and most property crimes will simply not be investigated. Finally, the SJPD is and will continue to be severely hampered in its ability to respond to multiple critical events occurring at the same time. As the largest police force in the county, SJPD cannot rely on mutual aid from neighboring jurisdictions; typically, other agencies rely on SJPD for assistance. A more in-depth discussion on service-level impacts to the Police Department can be found in Appendix A.

B. Impacts on the Fire Department

Despite ranking as the tenth largest City in the nation by population and ranking among the top fifty largest U.S. cities by land area, the San José Fire Department (SJFD) has traditionally operated with lean staffing levels. To date, SJFD has lost 13.5% of its staff since 2007-2008 due to increased operating costs with little offsetting budget augmentation. In the past two years, SJFD has closed a fire station, taken four fire engines and one fire truck out of service, and reduced daily staffing from 203 firefighters to 160 firefighters.

Without emergency measures to address the growing retirement costs, the Fire Department will be operating at levels far below all targets, including industry standards. Given these further reductions to the already skeletal operations, the Fire Department is certain that response times will continue to increase dramatically.

The projected budget cuts will require taking out of service up to nine more fire engines or trucks, eliminating SJFD's Hazardous Incident and Urban Search and Rescue teams, and closing at least one more fire station. Daily staffing could fall as low as 124 firefighters on duty in a 24-hour period. A daily staffing level of 144 firefighters per day represents the minimum staffing threshold for a City the geographic size, population, level of hazard, demographics and density of San José. Coverage under these reduced levels will be 0.52 firefighters per 1,000 people compared to the national average of more than 1 firefighter per 1,000 individuals (the metropolitan or city average is even higher).

Already, SJFD's response time to medical and fire emergencies has increased to unacceptable levels. Target response times are set based on the time during which a fire can be contained in its room of origin, and a patient can survive following a sudden heart attack. The national standard for emergency response is a maximum of six minutes for medical and fire emergencies; however, San José has adopted an eight minute threshold. Although SJFD met this goal in all but one month prior to the recent staffing cuts, it has consistently failed meet its target since staff reductions in July 2010.

If budget reductions at the level identified in the budget balancing scenario are necessary, the projected budget cuts will result in the following critical outcomes:

- Response times will deteriorate to over 10 minutes, and will likely hit 12 minutes on a fairly regular basis.
- Diminished capacity to respond to two or more sustained structure fires in single family dwellings that occur within the same time period.
- Inability to confine structure fires to the room of origin; SJFD will increasingly be working to contain fires to the *building* of origin, instead of the room of origin.
- Higher casualty rate experience in structure fires.
- SJFD will have severely diminished capacity for large or major events, such as a second alarm fire.
- The Department will have limited capacity to respond to wild land fire dangers and anticipates that wild land fires will therefore be larger. In the high fire danger season – April through October – the SJFD responds to these kinds of incidents approximately once a week.
- The SJFD will be unable to meet medical response times and will experience lower resuscitation rates and significantly worse patient outcomes.
- Greater percentage of second due (or later) companies responding to emergencies.
- Major events (two or more alarms) and longer duration emergencies will affect the Fire Department's ability to manage emergencies without significant support and assistance from outside agencies.

These impacts would represent a service-level emergency situation for the City. A detailed analysis on service-level impacts to the Fire Department can be found in Appendix A.

C. Impacts on Library Services

The San José Public Library System's (SJPL) main library is the King Library. It is located in downtown San José and was opened in 2003. The King Library is the first joint-use library in the United States, shared by a city and a major public university (San José State University). In addition to the King Library, the SJPL has 22 branch libraries. However, four of those branches – which were recently constructed following bond measures – are not operational due to budget restraints, leaving only 18 currently operational branches.

The San José Public Library System (SJPL) operates the largest public library system between San Francisco and Los Angeles. SJPL operates 18 branch libraries throughout the community and with San José State University jointly operates the system's central library, the Dr. Martin Luther King, Jr. Library (King Library). SJPL staff has been reduced by 26% since 2007-2008, and four newly built branch libraries remain shuttered because the City cannot afford to operate them. Hours at the remaining branch libraries have been reduced from six or seven days per week to only four days per week. Moreover, library services and outreach programs have been significantly reduced in the past several years.

If budget reductions at the level identified in the budget balancing scenario are necessary, SJPL will have to close almost all of its branch libraries, operating only the King Library (Main Library) and a handful of others. If the voters have not reauthorized the SJPL parcel tax before it sunsets in 2015, SJPL will be forced to close *all* of its remaining branch libraries.

The vast majority of SJPL's usage occurs at branch locations – not at the King Library. During 2010-2011, there were more than 4.3 million *branch* library visits. This means that when the branches are closed, these visitors will be without a library, unless they are able to travel to downtown San José. This geographic limitation will prohibit most residents from any public library access. Moreover, even if all of those library users could find a way to the King Library, that facility does not have the capacity to serve them.

The elimination of branch libraries and library programming will have a dramatic impact on the economic and social well-being of the community. It will mean the majority of San José's publicly-educated elementary and middle school students will have very limited or no access to a library. The SJPL libraries also offer early childhood education and literacy programs and these would also cease.

The value of the library extends beyond providing educational programming for youth. As the economic downturn persists, job seekers have turned to the SJPL in visible numbers to access library resources. Further, community rooms at the branches are utilized as gathering space for neighborhood and City-sponsored meetings. Researchers have examined the impact libraries have on

property values.[52] Their findings show living within a quarter mile of a library is associated with having a property value approximately 7.7% higher than comparable zones at greater distances.

If these budget cuts are necessary, what would residents lose?

- 2,000 story times to 81,000 children at branch libraries will no longer occur;
- 880 literacy education programs at branch library family learning centers with 20,555 attendees will be shut down;
- Over 700 school-aged children visiting branch libraries after school each day, many of which are not accompanied by a parent or caregiver will no longer have a safe, constructive and educational place to go;
- 501,243 reference questions at branch libraries will be left unanswered;
- Over 10,000 branch library programs with over 280,000 attendees, including 171,000 children and 8,664 teenagers will no longer have programming;
- 1,215 branch community room uses with 41,197 attendees will no longer be available.

These budget cuts will leave the future of SJPL on uncertain ground and will result in the loss of valuable social and economic benefits for the City of San José.

The Library may eventually be forced to close completely, wiping out a basic municipal service in the City of San José. This is a service impact that cannot be afforded. No large city in the United States is without library services for its residents. Further details on service-level impacts to the Library System can be found in Appendix A.

D. Impacts on Parks, Recreation and Neighborhood Services

The City's Department of Parks, Recreation and Neighborhood Services (PRNS) is an essential element of the fabric of San José. Nearly 40% of San José households visit PRNS parks or facilities at least once a week. PRNS, along with the libraries, have been hit hard by the budget cuts to date, as the City has prioritized preserving the public safety department budgets. PRNS staff has been cut by 47% since 2001, with 35% of that reduction occurring since 2009, from 708 to 460 FTEs. In the past several years, PRNS has had to reduce or eliminate countless programs for City residents of all ages.

The projected budget cuts will leave PRNS with only 276 FTEs by 2014-2015, and an even more limited range of services available to City residents.

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[52] Citations to all resources cited in this section are listed in the complete Library Impacts discussion contained in Appendix A.

With the budget cuts to date, PRNS has been forced to consolidate all City recreational services in to Multi-Service Hub Community Centers (large facilities ranging from approximately 13,000 to 60,000 square feet). Under this program, out of 54 community centers, the City currently operates only 10 community centers as regional hubs with reduced staffing, plus the Grace Community Center (a therapeutic recreation facility). PRNS has also had to reduce afterschool programming for children and eliminate the Citywide Sports League. The Department has had to reduce the Senior Nutrition Program, and eliminate counseling and helpline services for seniors. A number of services that were not eliminated completely have been outsourced to other agencies.

If budget reductions at the level identified in the budget balancing scenario are necessary, all remaining PRNS-run recreation programs will be eliminated, leading to an increase in the number of adolescents without after school programming. All Park Ranger positions will be eliminated, meaning that no one will be available to collect fees, coordinate special events, or provide other services to park visitors. Even revenue-generating recreational programs will be eliminated because PRNS will not have sufficient staff to run the programs. The Senior Nutrition Program, which still provides about 1,000 hot meals each day, will be at risk of severe reduction or elimination. The City will be unable to operate any of its 54 community centers unless reuse providers can cover operational overhead. Some of these very centers have been linked with reducing crime rates in the surrounding neighborhoods.[53] Programs designed to suppress gang-activity and graffiti abatement will be reduced to skeletal levels, which will be compounded by the elimination of the after-school Teen programs.

What will we lose if emergency measures are not taken to address the rising retirement costs and other cost drivers? With services provided in 2009-2010 as our benchmark:

- 54 Community Centers would be potentially vacant;
- Over 2 million recreational program user activities will be lost;
- 238,000 nutritious meals in jeopardy of loss or reduction to seniors;
- 7,000 kids will not attend San José's summer camps;
- 6,600 people with disabilities would lose access to programs;
- Over 1,000 fitness pass members would lose access to wellness equipment;
- Daily services for 80-90 adults with mental, physical and developmental disabilities will no longer be provided at the Grace Community Center;

[53] Citations to data cited in this section are listed in the complete PRNS Impacts discussion contained in Appendix A.

- 53 miles of trail will no longer be patrolled by Park Rangers;
- Emergency medical calls, fire response calls and search and rescue calls will not be answered by the Park Rangers Service;
- Over $7 million in fees and grant revenues would be lost;
- While preserved in the next fiscal year, eventually the Mayor's Gang Prevention Task Force (MGPTF) gang prevention and intervention services will be decreased; and
- Ability to coordinate and engage 500,000+ hours currently served by volunteers to improve City property would be lost.

The effect of these reductions and eliminations will be to wipe out all basic municipal recreational services in the City of San José. The City will be forced out of the business of providing recreational and neighborhood services with these budget cuts: Community Center recreational operations with services for seniors, youths, adults and therapeutic customers will all be eliminated absent a partner agency subsidy. The negative impacts to the community of San José as a result of these changes cannot be afforded.

Further details on service-level impacts to the Parks, Recreation & Neighborhood Services Department can be found in Appendix A.

E. Impacts on Other City Services

1. Capital Maintenance

The Capital Maintenance departments are responsible for developing and maintaining the physical assets of the City of San José, including City facilities and the transportation infrastructure. Deep reductions in these areas have already impacted the appearance of the City and have contributed to a significant backlog of unmet and deferred infrastructure needs. For instance, the transportation infrastructure currently has an unmet need of over $474 million on a one-time basis and $105 million ongoing. The underinvestment in these areas will continue to lead to the deterioration of the City's assets. Further, in many cases, such deterioration will require much higher long-term costs, and rebuilding and replacing assets is typically much more expensive than responsible, ongoing maintenance.

As an example, the estimated cost to eliminate the deferred maintenance backlog of the City's streets has grown from $250 to $277 million over the past year. Based upon information presented to the Transportation and Environment Committee in May 2011, approximately $100 million annually would be needed to fully eliminate the backlog and to improve overall pavement conditions of the City's street system to a rating of good. Funding levels for pavement maintenance in 2011-2012 total $20.0 million, as identified in the 2011-2012 Adopted Capital Budget. This funding is from various capital and grant funds.

At current and projected funding levels, the backlog of deferred pavement maintenance will continue to grow and the overall condition of the network will continue to decline. The current Pavement Condition Index (PCI) for all San José streets is 64 on a 100 point scale, a rating of fair, and the lowest of all cities in Santa Clara County. By the year 2020, it is estimated that 54% of all streets will be in poor condition and the backlog of deferred maintenance will approach $1 billion, as compared to the current maintenance backlog of $277 million. The recent budget cutbacks have had the following impacts on the City's infrastructure:

- Reductions in the pavement maintenance program, which have reduced the number of arterial streets sealed from 67 miles to 26 miles and residential streets sealed from 169 miles to 46 miles.
- Reductions in the traffic maintenance program, impacting traffic sign maintenance, roadway striping, and markings maintenance.
- Eliminated funding for city-wide sidewalk repairs and emergency street tree services (property owners are responsible for these costs).
- Reductions in street landscape services, significantly impacting the condition of the street landscapes.
- Reductions in City facilities maintenance and the outsourcing of custodial services, fleet maintenance, and labor compliance staffing reductions.
- Reductions in transportation operations services, impacting the installation of traffic calming devices, completion of neighborhood cut-through traffic studies and intrusion studies, and responses to speed compliance calls.

If budget reductions at the level identified in the budget balancing scenario are necessary, the following reductions to capital maintenance are anticipated:

- Traffic maintenance programs will be further reduced, impacting traffic sign maintenance, roadway striping, and marking maintenance.
- Further reductions in City facility maintenance and fleet maintenance.

2. General Government

The General Government departments support the departments that provide direct services to the community. With budget reductions over the last decade, staffing levels have been reduced to the minimal levels necessary to perform these required functions. For example, between 2002-2003 and 2011-2012, staffing for the Human Resources Department was reduced by 30% and for the Information Technology Department by 23%. Following are some of the major reductions implemented and further impacts to these areas will be required to balance budget shortfalls over the next several years:

- Reductions in staffing in financial reporting, financial management, internal controls, and compliance functions in the Finance Department.
- Reductions in employment services, safety program, workers compensation claims administration, wellness programs, and training and development in the Human Resources Department.
- Reductions in city-wide technology coordination and information technology infrastructure services in the Information Technology Department.

In the early years of the budget shortfalls, reductions were focused on lower priority services. In recent years, however, significant reductions to the City's highest priority services, including public safety, have been unavoidable. In addition, several new City facilities, including the Police sub-station, four branch libraries, and one community center, remain closed due to lack of funding to operate these facilities.[54] Based on projected General Fund shortfalls for the next four years currently estimated at $113-150 million, continued service reductions are anticipated, with limited options now available to reduce those services without jeopardizing the primary functions performed by the City.

[54] These facilities were constructed following the passage of bond measures.

V. EFFORTS TO ADDRESS THE FISCAL CRISIS AND CONSIDERATION OF ALTERNATIVES TO DECLARATION OF EMERGENCY

The City has made every reasonable effort to address its fiscal situation, and continues to do so. Most recently, the City Council adopted a comprehensive Fiscal Reform Plan to address the City's budget shortfalls and increasing retirement costs. Moreover, as discussed below, the City has considered – and continues to consider - other proposed solutions for addressing the rising retirement costs. However, it must be noted that the service-level impacts (Section IV and Appendix A) are in fact another alternative, albeit one with unacceptable consequences since the City will be rendered unable to provide basic municipal services. That dire situation will be the unacceptable outcome if the City does not declare a fiscal emergency and reduce its retirement costs.

The City has also considered and is pursuing other ways to control costs and avoid unacceptable service cuts. Some of these are discussed below. Ultimately, even if the City is successful in achieving all of the ways to control costs outside of changes to retirement benefits, they are insufficient to solve the crisis facing San José.

A. The City's Fiscal Reform Plan

Over the past decade, the City has balanced General Fund budget shortfalls of $680 million and has eliminated 28% of the workforce. A combination of strategies has been used to address these deficits, including cost reduction strategies, revenue strategies, and service reductions and eliminations. Given the severity of the budget actions already taken and the size of the General Fund shortfall projected over the next four years, it is no longer feasible to rely on these strategies alone to balance the budget without reducing services to unacceptable levels.

On May 2, 2011, the City Manager presented a comprehensive Fiscal Reform Plan[55] to the Mayor and City Council, which was adopted by the City Council on May 24, 2011. It should be noted that the City Council has subsequently provided revised and additional direction on some of the items in the Fiscal Reform Plan. The recommendations contained in that memorandum were designed to achieve $216 million in General Fund savings by Fiscal Year 2015-2016. Following is a discussion of those strategies, some of which have already been implemented.

1. Cost Reduction Strategies

The Fiscal Reform Plan identified several strategies to reduce costs, including reduced compensation for existing employees; reduced costs for sick leave payouts, vacation buybacks and overtime pay; modified healthcare plans; and cost sharing and avoiding further increases in retirement costs through retirement benefit changes. Through bargaining, the City has already achieved a 10% total

[55] The Fiscal Reform Plan is available at: http://www.sanjoseca.gov/budget/FY1112/05MBA/MBA01-FiscalReformPlan.PDF

compensation reduction for all employees (with 2009-2010 as baseline) and rolled back any general wage increases received in 2010-2011. This 10% total compensation reduction included reducing pay of employees, and increased cost sharing in healthcare. Although this reduction saved approximately a net $39.6 million, it is not enough to resolve the continuing increases in retirement costs.

This plan also identified savings that could be achieved in retiree healthcare by providing a lower cost health plan for active employees that reduces costs by 25%. Any changes made to active healthcare are then applied to retiree healthcare. Achieving this could result in savings of $17.9 million and the City is currently meeting and conferring with bargaining units on this issue.

As part of this plan, the City is also pursuing the elimination of sick leave payouts, reduction in overtime and elimination of a vacation sellback program. The elimination of sick leave payout would save approximately $7.5 million in the General Fund and this has already been achieved with four out of eleven bargaining units. The City is currently meeting and conferring with the rest of the bargaining units over this. By January 2013, vacation sellback has been phased out for all but one bargaining unit and the City will be pursuing the changes to overtime identified in the Fiscal Reform Plan in the next round of negotiations.

Although the savings above identified in the Fiscal Reform Plan are significant, the most significant changes which are the majority of the $216 million in savings identified in the Fiscal Reform Plan, are changes to retirement benefits, most of which require voter approval. Changes to the City's retirement benefits could yield the most significant amount of savings. These changes include implementing a second tier system or a hybrid system for pension benefits, temporarily suspending the cost of living adjustment built into pension benefits, and/or increasing employee cost sharing. These proposed changes may require a combination of voter approval and collective bargaining. In addition, depending on judicial determinations, one or more of these changes may require a declaration of emergency.

2. Revenue Strategies

The Fiscal Reform Plan identified the following revenue measures: (1) Sales Tax Increase; (2) Business Tax Modernization; (3) Municipal Water System Tax on Gross Receipts; and, (4) Disposal Facility Tax Increase. Each of these revenues measures, however, would require voter approval. When the Fiscal Reform Plan was published in May 2011, it was estimated that $46.5 million in additional revenue would be received collectively from the measures if passed by the voters. This figure has been revised upward to $48.25 million based on an updated Sales Tax revenue estimate.

It is important to note that the City's ability to raise revenue through taxes and fees is severely constrained by the California Constitution, as modified by several statewide ballot measures, ranging from Proposition 13 in 1978, to Proposition 218 in 1996, to 2010's Proposition 26.

Proposition 13 limited the revenue that cities may receive from property taxes by capping both the assessed value of property and the tax rate allowed. Proposition 13 also imposed a requirement that "special taxes" be approved by a two-thirds supermajority of voters. In 1984, Proposition 62 extended a voter approval requirement to "general taxes" imposed by cities. In 1996, Proposition 218 imposed further restrictions on cities' ability to impose property-related fees, reaffirmed voter approval requirements for all taxes, and granted voters the right to repeal or reduce taxes or fees through the initiative process. Although Proposition 218 continues to be interpreted through the courts, it is clear that it has created an additional significant barrier for local governments in attempting to control financial outcomes.

Proposition 26, the most recent restriction on the City's ability to raise revenue, extended voter approval requirements to "regulatory fees" by reclassifying such fees as taxes. An example of a regulatory fee is a fee imposed on manufacturers of products containing lead to fund health services and mitigation of the environmental impacts of lead. By requiring voter approval for such fees, Proposition 26 significantly restricted one of the few remaining options for cities to raise revenue.

As previously noted, the City Council has advanced four new taxes since 2008 for which voter support had been indicated through professional surveys. (See Section II, B (3)). Over this same period, the City has also evaluated voter support for the additional revenue enhancement measures addressed in the Fiscal Reform Plan; however, the results to date have not supported a decision to place those measures before the voters.

A challenge facing City Council whenever evaluating whether or not to place revenue measures before the voters is how to weigh the marginal support typically seen in pre-vote surveys. In judging whether to place a measure before the voters, the City Council must weigh the likelihood that marginal voters who are "leaning" in support of a measure will vote in favor of the measure, against the knowledge that the City generally will only get one "bite at the apple" when it comes to any particular revenue measure, and that the cost for that one "bite" is extremely high, whether it wins or loses. According to the advisory firm that conducts surveys for the City,[56] once the voters reject a measure, it is often significantly more difficult to pass in a subsequent election. In other words, the likely chance of passage is reduced once a ballot measure has been rejected. These combined concerns have prompted the City Council to take a cautious approach when considering placing revenue measures before the voters.

Following is a discussion of each of the four potential tax measures included in the Fiscal Reform Plan.

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[56] Fairbanks, Maslin, Maulin, Metz, and Associates.

a. Potential Tax Measures

(i) Sales Tax Increase

In July 2011,[57] the City surveyed voter support for several alternative forms of a sales tax increase, including a one-half percent general sales tax increase and a one-quarter percent general sales tax increase, each with different sunset provisions (15 or 9 years). Likely voters who would "definitely" or "probably" vote for the one-half percent increase measure topped out at 46%. For a one-quarter percent general sales tax, support from the same two categories of potential voters was 49%. Success in either of the two general sales tax options, which require a simple majority to pass, would require support from voters who were "leaning" in favor of the measure, and it is these voters who are most likely to be swayed by arguments against the measure.

In addition to the two general sales tax measures, the City surveyed voter support for three versions of a special sales tax to support public safety: 1) a one-quarter percent special purpose sales tax for Police services; 2) a one-quarter percent special purpose sales tax for Fire services; and, 3) a one-quarter percent special purpose sales tax for Public Safety services. As special purpose taxes, each of these would require a super majority (two-thirds) vote for approval. In each case, support for these options fell far short of the super-majority required. Of the two general tax measures, the one-quarter percent sales tax appears to be the more viable. However, it should be noted that placing a general tax measure on the ballot prior to June 2011 would require a unanimous vote of the City Council. In its August 2, 2011 meeting, the City Council voted not to pursue a sales tax increase option in a special election, but continues to discuss the possibility of placing this measure on the next General election after additional polling has been completed to test voter support. The one-quarter percent sales tax is most recently projected to generate $35.75 million annually, and is assumed as a revenue source in the Fiscal Reform Plan.

(ii) Business Tax Modernization

The City's business tax was first implemented in 1964 and was revised in 1984. The current structure is antiquated, based on an outdated business sector that has long since been replaced by the Silicon Valley economy. This tax, which is charged to business owners, currently generates approximately $12 million annually. The Administration has reviewed options to modernize the business tax. Minor changes could be implemented to adjust exemptions and ensure various types of businesses are addressed. The changes would also have to be considered in the context of the overall cost of doing business in San José and the competitiveness of San José when compared to surrounding jurisdictions. For purposes of this analysis, it is assumed that a combination of CPI

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[57] See Item No. 3.5 for City Council Meeting on August 2, 2011, "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."

adjustments as well as modernization efforts, would conservatively generate at least an additional $5 million annually.

In the past few years, the City has surveyed voters four different times on the question of support for a business tax modernization measure: January 2008, January 2009, January 2010, and January 2011. Over this time support from likely voters who would "definitely" or "probably" vote for the measure has grown from 27% to 49% in the most recent survey. On June 24, 2011, the City Council directed the Administration to reach out to the business community regarding a business tax modernization measure and that work is currently underway. If approved by voters, a potential measure is projected to generate at least $5 million.

(iii) Municipal Water System Tax on Gross Receipts

In the 2010-2011 Mayor's March Budget Message as approved by the City Council, staff was directed to "re-evaluate the feasibility of leasing Municipal Water to private companies that could generate millions of dollars of revenue for the City, as well as current alternatives to generate a rate of return on the system." In June 2010, the City Council directed staff to conduct further analysis of opportunities to generate General Fund revenue from the Municipal Water System. In response to that direction, staff presented a preliminary Work Plan and options for maximizing financial benefits from the San José Municipal Water System at the November 9, 2010, City Council meeting. At that meeting, staff was directed to evaluate the viability of a voter-approved transfer of 10% of gross revenues generated by the Municipal Water System. Because such a transfer would not be allowed under Prop 218, this would require the approval of a simple majority of voters as a new tax, and, if approved, could be expected to generate $2.5 million annually.

(iv) Disposal Facility Tax Increase

By Ordinance, the City established the Disposal Facility Tax in 1987 and revised the tax in 1992 to its current rate of $13 per ton of solid waste for disposal sites. This tax currently generates approximately $10-11 million annually. The City has twice surveyed voter support for increasing this tax. In January 2010,[58] those who said they would "strongly" or "probably" vote in favor of the increase totaled only 37% of likely voters; one year later, that level of support had grown to 49%. There are a number of options to increase and broaden this tax, and an increase of up to $5 million annually could be generated if voters approved the measure.

b. Best Cases Revenue Scenario Does Not Solve the Problem

The four measures included in the City's Fiscal Reform Plan have been considered by the City Council. The City's survey consultants warn against placing multiple revenue measures on the same

[58] See Item No. 3.5 for City Council Meeting on February 9, 2010, "Mayor's Budget Prioritization Survey Results."

ballot. They note that when you have multiple measures on a ballot, it is likely to reduce support for all of them and so they recommend a phased approach when placing multiple measures before the voters. However, it is important to note in the context of declaring a fiscal emergency, that all of these potential revenues together would only garner about $48.25 million, which would only cover approximately 60% of the 2012-2013 projected shortfall and slightly over 40% of the $116 million deficit projected over the next four years.

c. Other Revenue Alternatives Rejected

While not included in the Fiscal Reform Plan, the City has also reviewed voter support for a number of other potential revenue measures, none of which has demonstrated sufficient support to merit serious consideration. Among these are:

- General purpose taxes requiring a simple majority to pass:
    - An increase in the Transient Occupancy Tax: 38% "strongly" or "probably" support (January, 2008);
    - A tax on Parking Facilities to support "police patrols, fire protection, street repair, parks and libraries":
        - 46% "strongly" or "probably" support (January, 2009);
        - 34% "strongly" or "probably" support (January, 2010).
- Parcel taxes requiring a super-majority (two-thirds) to pass:
    - Parcel tax supporting "landscape and energy-efficient lighting": 13% "strongly" or "probably" support (January, 2008);
    - Parcel tax to support "police, fire, and other critical services": 19% "strongly" or "probably" support (January, 2008);
    - Parcel tax to help maintain City library services by continuing an existing parcel tax: 51% "strongly" or "probably" support (January, 2011);
    - Parcel tax to "protect and maintain City infrastructure services like libraries, street and park maintenance, traffic signals and roadway markings maintenance": 39% "strongly" or "probably" support (January, 2011);
    - Parcel tax to "protect and maintain public safety services like police patrols, 9-1-1 emergency response, and fire protection": 35% "strongly" or "probably" support (January, 2008).

As the data shows, voters appear to be unwilling to support any of these potential revenue measures.

B. Spending Down Reserves

In a time of fiscal crisis, the use of reserves is one of the options to consider as a short-term approach to bridge funding gaps in order to continue providing essential municipal services. In fact, the City of San José has used this strategy over the past several years as part of the budget balancing actions. In 2012-2013, the use of the $11.6 million Future Deficit Reserve is expected to be brought forward to address a portion of the projected General Fund shortfall as these funds were set aside for that purpose.

As shown in the chart below, the 2011-2012 Modified Budget includes Earmarked Reserves of $47.8 million and a Contingency Reserve of $29.3 million, for total reserves of $77.2 million. Excluding the Development Fee Program Reserves, which are restricted, General Fund reserves total $60.8 million.

Earmarked Reserves	2011-2012 Modified Budget
Workers' Compensation/General Liability Catastrophic Reserve	10,000,000
Salaries and Benefit Reserve	7,296,903
Future Deficit Reserve	11,616,917
Development Fee Program Reserves	16,387,470
Various Capital/Maintenance Reserves	250,080
Miscellaneous Other Reserves	592,414
Filled Position Elimination Expenditure Reserve	700,000
Retirement Pre-Payment Reserve	1,000,000
Total Earmarked Reserves	**47,843,784**
Contingency Reserve	**29,309,000**
Total Reserves	**77,152,784**

Earmarked Reserves are one-time monies that are set aside to address specific needs and are maintained until those funds are used for the designated purpose or it is determined that the funding is no longer needed and can be reallocated. Of the $47.8 million in Earmarked Reserves, $16.4 million was generated from the development fee programs and is restricted to that use. Excluding the development fee program reserves, the Earmarked Reserves total $31.4 million. Of this amount, $11.6 million has been set aside to address a portion of the 2012-2013 General Fund shortfall and the remaining funds of $19.8 million have been designated for other purposes, with the largest allocations for the Workers' Compensation/General Liability Catastrophic Reserve ($10 million) and the Salaries and Benefit Reserve ($7.3 million). While each of these reserves will be analyzed in the development of the 2012-2013 budget, the Administration anticipates recommending the retention or use of most of these reserves for the existing purposes.

The Contingency Reserve of $29.3 million meets the City Council policy to set aside a minimum of 3% of the operating budget. The Administration strongly believes that this reserve should remain intact to address any unforeseen circumstances as it serves as the City's safety net. Without these funds, the City would not be equipped to address significant unforeseen expenditure needs or to offset large drops in revenues. It is imperative that the City be in a position to meet its financial obligations each year and must prudently plan to do so.

There are strong budgetary and strategic reasons for the City to maintain adequate reserve levels and to avoid using these needed one-time funds to balance the budget. However, even assuming that the City could use its reserves, this would not solve the anticipated shortfall. With an $80.5 million General Fund shortfall projected in 2012-2013, if the City Council chose to deplete *all available reserves (excluding the restricted development fee reserves)* of approximately $60 million and reallocate those funds to balance the budget next year, the City still would have a remaining gap of $20 million to resolve. More importantly, because this deficit is structural in nature and because reserves by definition are one-time monies, the City would simply be shifting the budget problem out one year (to 2013-2014) by that same amount. Then, the City would be worse off in 2013-2014 (forecast shows a shortfall of $25.1 million for that year) as it would have to not only resolve that added gap, but it would also have no reserves to use to balance the budget or to address unforeseen circumstances.

At a more fundamental level, the City has drawn down its reserve levels over the last several years and this practice is unsustainable. Effectively, San José's actions have been equivalent to those of a homeowner drawing down from their savings account to pay for monthly mortgage and grocery bills that exceed their regular paycheck. So long as the savings last, such a practice can buy time to either find a better paying job, and/or to cut down on monthly expenses. If insufficient changes are made with such recurring income and spending, however, the savings will eventually be depleted.

C. Deferring the Pension Problem

Some have suggested the City should in essence "defer" its current retirement costs as a means to avert the current crisis. For a number of reasons, this is neither realistic nor prudent. It is unrealistic because the Retirement Boards that run the City's retirement plans are independent. They are comprised of employee representatives, City representatives, and independent directors, each of whom has fiduciary obligations. The determination as to whether to change the actuarial assumptions, amortization periods or smoothing periods is not in the City's hands, and therefore, cannot be assumed as a means to avert the current crisis.

The City's retirement plans utilize a five-year smoothing period in determining the actuarial value of assets, and amortization periods ranging from sixteen to thirty years. Increasing the smoothing period or extending the amortization period would have the short-term effect of reducing employer contributions to the plan. However, neither is likely to be viewed as acceptable by the plans' trustees

in light of current economic realities. Critically, lengthening the amortization or smoothing periods would fly in the face of recent actions by GASB which are intended to shift public agencies to fund pension benefits over the working life of employees, to reduce intergenerational funding [cross-funding], and to protect pension plans from potential insolvency. On July 8, 2011, GASB released an "exposure draft" of proposed accounting changes expected to be adopted in 2012. Those standards will require amortization of unfunded liabilities over the remaining average service lives of today's employees. *This will actually shorten the permitted amortization period.* GASB has also recommended smoothing periods no greater than five years – the City's current standard.

The City Council and Administration have reviewed the alternatives discussed on multiple occasions. These options show no opportunity for addressing the City's retirement problems. The Fiscal Reform Guiding Principles contained in the Mayor's March Budget Message for 2011-2012, which was adopted by the City Council, contained the following statement: "Pension costs shall not be pushed onto future generations, and we will not borrow our way out of this problem." In particular, increasing the smoothing and amortization periods, only defers and does not eliminate the current crisis. As a matter of policy and fiscal responsibility, the City must adopt changes that address the structural problems in its retirement plans. It is critical that the steps taken by the City guarantee a healthy and viable retirement for current and future generations of San José employees.

CONCLUSION

The City of San José faces a fiscal crisis of staggering proportions. The City has closed budget shortfalls every year for the past decade, largely through reductions in staffing and service level reductions. Citywide staffing levels have dropped by almost 30% (eliminating more than 2,000 funded positions) between 2001-2002 and 2011-2012.

Despite these reductions, the City's cost of providing services has continued to rise. Retirement costs are the major factor driving the increased cost of providing services. During the 2009-2010 fiscal year, the City's share of the annual required contributions for retirement (pensions and OPEB) was $133 million. Today, that number is $245 million and it is expected to rise to $431 million in 2015-2016.

Expressed as a percent of payroll, retirement contribution rates (including both pension and OPEB) have risen from 16% of pay for the Federated Retirement Plan and 15% for the Police and Fire Retirement Plan to a projected 52% of pay for Federated and more than 96% of pay for Police and Fire. In other words, for every $100 paid for police and fire payroll, the City will be required to pay an additional $96 into the retirement system, nearly doubling the cost of every hour of labor.

As a result of these increasing costs, the City projects budget shortfalls for the foreseeable future. Those shortfalls are anticipated to grow on a cumulative basis, if no corrective action is taken, from $80.5 million in 2012-2013 to over $115.7 million by 2015-2016. Absent a dramatic change to the accelerating cost of employment, the City will have to close these budget gaps by cutting and potentially eliminating already reduced services below acceptable levels.

For all of the foregoing reasons, the Administration recommends that the City Council adopt a resolution of fiscal emergency based upon the need to find and implement solutions that may require the exercise of the City Council's emergency powers.

APPENDIX A – IMPACTS ON SERVICES

As noted in the *Service Impacts Analysis* section of this report, the rise in retirement costs has forced the City to make difficult and drastic reductions in essential services. Unfortunately, those rising costs are expected to continue for the foreseeable future.

The Administration has worked with the Police, Fire, Library and Parks, Recreation & Neighborhood Services departments to assess the likely impacts of the reductions that would be required to close the shortfalls that have resulted primarily from increased retirement costs. The budgetary cuts projected for the foreseeable future will severely reduce and potentially eliminate vital City-wide services. This *Appendix A: Impacts on Services* section provides details of the four departments, and the likely impacts.

A. IMPACTS ON SAN JOSE POLICE DEPARTMENT

1. Department Overview

a. Department Organization

The SJPD currently employs 1,087 sworn officers. The Department is administered by a command staff including the Chief, Assistant Chief and four Deputy Chiefs, presiding over an Operations Command divided into four Bureaus. The Bureaus are comprised of 11 divisions with more than 61 specialized Units and assignments.[59]

The Bureau of Field Operations (BFO) includes the SJPD's Patrol, Special Operations and Airport Divisions. BFO is the primary provider of police response to calls for services from the residents of San José. The Patrol Division deploys 659 sworn staff members (compared to 729 in 2008) on a 24-hour basis. Patrol personnel respond to both emergency and non-emergency calls for service. In addition to responding to calls for service, officers provide visible patrol throughout the City, detect and apprehend persons actively involved in criminal activity, recover and return lost and stolen property, perform the initial investigation of criminal offenses, and attempt to reduce both immediate and potentially hazardous situations to the community.

BFO's Special Operations Division utilizes uniformed, highly-trained, specialized officers that enhance the Department's abilities to apprehend and investigate crimes, particularly those of a more violent nature; address critical incidents involving threats to life; coordinate tactical efforts and crisis response; and provide for the safe movement of vehicular and pedestrian traffic. The Airport Division enforces the Airport Security Plan; ensures compliance with all Transportation Security

[59] To name a few: Airport Police; Canine Unit; Drug Task Force; Gang Investigations Unit; Internal Affairs; Traffic Enforcement; Bomb Squad; Metro Unit; and the Covert Response Unit.

Administration (TSA) security directives and existing Federal Aviation Administration (FAA) regulations; and provides a safe traveling environment for the public.

The Bureau of Administration includes the personnel and permits units, oversees the police academy, the property and evidence warehouse and training, and handles recruiting and background checks for the SJPD. The Bureau of Technical Services oversees Communications and Dispatch, Operations Support Services and the Systems Development Unit. Finally, the Bureau of Investigations (BOI) investigates homicides and crime scenes; family violence and sexual assaults; accident reconstruction and auto theft; robbery and assaults; juvenile crimes; missing persons and financial crimes. BOI also oversees Gang Investigations, the Internet Crimes Against Children Task Force and the Covert Response Unit.

b. San José Statistics

San José's incorporated area covers 179.8 square miles, placing it in the top 50 largest U.S. cities by land area. And yet, San José is the largest city in the nation that operates out of one facility; most other large agencies operate out of multiple precincts or substations. To cover this large area, the Department has established four divisions (Foothill, Central, Western, and Southern) each with four districts.

With respect to population, San José is the 10th largest city in the United States, the 3rd largest city in California and the largest city in the nine-county Bay Area. The population growth trends have continued upwards for decades. In 1950, San José had only 95,280 residents; by 1980 this number had grown to 629,442. Currently, the City has nearly 1,000,000 residents (958,789). Historically, on a per capita basis, the Department has been a leanly staffed police force in comparison to the agencies of other large cities in the U.S.

Despite the comparatively low staffing levels, crime in San José has traditionally been lower than in other large American cities. In fact, it has been ranked as one of the safest cities in the country with a population over 500,000 people.[60] This is due in part to how the SJPD has managed to efficiently and effectively police the City with its staffing levels. It is also because of certain demographic features of San José.[61] However, because the SJPD has traditionally functioned with a lean, efficient staff, cuts to those staffing levels (even at percentages which may seem low) are felt more rapidly and with greater severity. All of the indirect support functions have already been reduced to the

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[60] The designation is based on crime statistics reported to the Federal Bureau of Investigation in six categories: murder, rape, robbery, aggravated assault, burglary, and auto theft.

[61] Included in these factors are the prevalence of high-tech industry jobs and the comparatively high level of educated citizens. San José ranks among the most educated metropolitan areas with the highest percentage of people 25 and older with a bachelor's degree or higher (40.5% of its population in this demographic, compared to the national average of approximately 27%).

minimum levels necessary to operate the Department. The 20% sworn staffing cuts to date and possible budget cuts of up to nearly 10% over the next several years have caused and will continue to result in deep cuts to direct services.

2. Department Budget

The current amount appropriated to the Police Department from the General Fund, based on the 2011-2012 Adopted Budget is $297,056,236 or approximately 36% of the total General Fund budget. The Police Department's adopted budget over the past few years has been fairly stable:

	2009-2010	2010-2011	2011-2012
Adopted Budget	$295,214,712	$297,353,229	$297,056,236

Sources: Adopted Budgets 2009-2010 through 2011-2012. (Rebudgets and Grant-Related Expenditures Removed).

Nonetheless, because of rising personnel costs, to simply maintain a nearly constant budget, the Police Department has had to significantly reduce staff (and services), including a reduction in sworn staff from 1,395 FTE's in 2008-2009 to 1,087 FTE's in the current fiscal year (or roughly $62 million in operating cost reductions).

The projected loss of another 9% of its General Fund budget over 3 years, would equate to over 183 additional position cuts within the Police Department by 2014-2015.

3. Consequences of Budget Reductions in Police Department

The SJPD has done an excellent job of policing the community, despite its comparatively lean staff as compared to police forces in other large cities. Consistent with the national trend, major crime has decreased in San José. Although it is difficult to directly correlate budget or staffing reductions with increases in crime, there are some identifiable trends showing spikes in crime, with potential correlations to recent reductions. Since the major budget cuts in calendar years 2009 and 2010, there have been a few noticeable indications of problematic trends. For example, in 2011, San José – historically ranked as one of the "Safest Big Cities" – experienced a significant surge in homicides. This statistic cannot be ignored. Although there had been a decrease in violent crime and gang-related violent crime between 2008 and 2010, the Department has seen an increasing trend in 2011. As of November 2011, homicides reached 37 (18 of which were gang related), far surpassing 2010's total number of homicides (20).

SJPD officers have anecdotally observed an increase in out-of-city criminals which seems to be related in time with the spread of information relating to SJPD layoffs. Moreover, what we can predict is that – with the projected department cuts – the types of crimes that SJPD can respond to will effectively be limited to violent, high priority crimes and the department's response time on all calls will increase to unacceptable levels.

Highlighted below are several primary indicators of departmental service levels impacted by recent staff reductions. With fewer staff on patrol, the BFO has already seen reductions in the number of officer-initiated calls, the number of car and pedestrian stops, and the number of arrests. The declining number of cases going to the BOI is a direct result of patrol activity. As resources decrease in Patrol, productivity decreases and the number of investigation cases declines. With fewer resources in investigations, BOI has seen a reduction in cases investigated and an increase in the number of "cases not assigned due to lack of resources" statistic, as shown below.

Activity	Target	CY2008	CY2009	CY2010	CY2011[62]
Bureau of Field Operations					
Number of officer-initiated calls		110,112	94,324	94,393	91,316 ↓
Number of car & pedestrian stops		104,010	92,499	74,101	69,068 ↓
Number of arrests (felony, misdemeanors, & status offenses)		35,001	29,716	27,792	N/A
Bureau of Investigations					
Cases received	62,500	68,172	57,601	54,065	54,416 ↑
Cases investigated	37,250	42,815	39,515	37,601	34,424 ↓
Cases not assigned due to lack of resources ("target" is a targeted maximum no. of cases)	3,000[63]	6,003	4,901	4,416	6,396 ↑
Cases resolved	39,600	45,982	40,906	33,211	34,272 ↑
Percentage of cases assigned resulting in criminal filings or otherwise successfully resolved	85%	105.75%[64]	103.40%	90.84%	84.61% ↓

Source: City of San José Police Department.

The data on traffic stops reflects an even more dramatic trend. Due to staffing reductions, the total number of traffic stops dropped by 40% in two years. This is troubling because traffic stops are an extremely effective way to prevent future crimes.

Traffic Stops Totals	
2008-2009	96,789
2009-2010	89,260
2010-2011	58,477

[62] Please note: the column contains an annual projection, calculated based on 2011 first quarter data. All other columns reflect actual annual data.

[63] In 2008, the targeted number of cases not assigned was 2,500.

[64] These percentages may exceed 100% because they include resolved cases that were assigned in previous years.

The anticipated reductions to the Department will lead to operating levels far below targets and far below community expectations. All of these factors, of course, will contribute to whether residents decide to continue living in the City of San José.[65] The major impacts of further budget cuts are described below.

In each of these sections, the data reflects where the City is now in terms of service levels in the Police Department. Although we cannot specifically predict the impact of the further proposed cuts on response times, service levels and increased crime, we can make evidence-based projections, as set forth below.

a. SJPD Staffing Reductions

(i) Reductions to Date

Since 2007-2008, Department sworn staff has been reduced by 308 positions or more than 20%, resulting in deep cuts to direct services. Moreover, civilian staff has been steadily reduced since calendar year 2001, with 81 positions cut since that time. Civilian cuts have been intensified by challenges in filling vacancies within the Department. Currently, there are 42 civilian vacancies pending.

The impact of reductions has been felt in all areas of the Police Department: Patrol, Investigations, Crime Prevention, Support Services, Records Management, and Special Operations Units. The Department has restructured various units and functions to minimize the impacts of these severe cuts. Units that support Patrol were realigned, reduced or restructured to continue to provide support to Patrol functions; and civilianization of several positions was implemented to allow remaining sworn staff to focus on peace officer functions. The Department has looked at span of control, special operations and deployment methodologies to ensure remaining resources are utilized efficiently and workload distributed equitably. A restructure of the BOI included the elimination or consolidation of investigative functions based on best practices and prioritizing certain types of crimes. Additional reductions were made to take home vehicles, travel expenditures, supplies and equipment purchases, front lobby hours to the public, the suspension of the helicopter program, contracting out prisoner transportation and police artist functions, and the number of crossing guards.

The City has deferred the opening of the Police Substation, delaying expected efficiencies in deploying the Southern Patrol Division; however, the annual operations and maintenance costs

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[65] Fear of crime impacts business and housing decisions. Crime spikes, particularly those relating to violent crimes and homicides, deter both potential business investors and existing customers. Gang activity and violence is costly to the business community as urban blight and graffiti negatively affect real estate and property values. As crime statistics become more readily available via online crime maps, these increases impact current or prospective resident's decisions about whether to live in the City. Accordingly, crime rates can ultimately impact the housing market (and consequently property values and taxes).

cannot be afforded at this time. The Department implemented improved overtime monitoring controls to reduce overtime costs. Several policy changes were implemented that limit or eliminate Patrol response to calls for service and offer the community an alternative means of reporting. The Department also reviewed all revenue resources and implemented increases in fees and fines where appropriate to increase revenue to the City.

Following are the major public safety service reductions that have taken place since 2008:

BFO Reductions (**201 total positions cut**), including:

- Reductions in Police Field Patrol (85 positions); reductions in Police Special Operations (47 positions), including Airport Operations, Metro Unit, the Horse Mounted Unit, Downtown Services Unit, the Violent Crimes Enforcement Team (VCET), and the Canine Unit. The Horse Mounted Unit was eliminated and functions as a collateral assignment only; the Canine Unit staffing was reduced and deployed within the patrol structure as a beat assignment; Metro and VCET were combined into one unit and staffing reduced; the helicopter was grounded temporarily; and Special Operations was restructured and staff was redeployed to maximize the number of staff on patrol.

- Reductions / Elimination of Community Policing Programs: Elimination of the majority of the Crime Prevention and Community Services Division staffing (20 positions), leaving four Crime Prevention Specialist positions to support the patrol divisions. Crossing guards have been reduced based on a safety index and programs, such as Challenges & Choices have been eliminated. The School Liaison Unit has been reduced to one officer per patrol division.

BOI has reduced staff by **64 total positions**, including reductions in Police investigative services (61 positions), impacting the majority of units. BOI was restructured and units were consolidated. Staffing reductions impacted almost all investigative units, including Court Liaison, High Tech, Warrants, Financial Crimes, Auto Theft, Assaults, Juvenile, Robbery, Intel, Vice, Family Violence, and Vehicular Crimes.

Reductions for Bureau of Technical Services, Bureau of Administration, and Office of the Chief have totaled **56.5 positions.** Those staff members support the following services: Police Administrative Building main lobby, public information officer, personnel, fiscal, permits, gaming, and training. The Police Officer Academy and Field Training programs have also been suspended, the performance analysis detail was eliminated, and main lobby hours available to the public have been reduced.

Service levels are already below acceptable levels for the City; and yet, continued cuts loom on the horizon.

(ii) Anticipated Future Reductions

The Department is already at a point where it cannot absorb further budget cuts without services reaching unacceptable levels for the public's welfare. SJPD has experienced a drop in community policing efforts, an increase in response times, and has stopped responding to selected low-level, non-priority calls for service. Under a potential General Fund Budget Balancing Scenario, described in Section II of this report, the Department may have the following expenditure reductions in 2013-2015 and projects the following commensurate reductions in staffing to meet the anticipated reduction targets.

Police Department Reduction Estimates			
	Reduction from 2011-2012 Adopted Budget	**Total Cuts Each Year**	**Projected Cuts Each Year[66]**
2012-2013	4%	$ (13,315,000)	74 positions eliminated
2013-2014	4%	$ (10,959,000)	86 positions eliminated
2014-2015	1%	$ (2,141,000)	17 positions eliminated

Source: City of San José Police Department.

In terms of Department staff, civilians have already been reduced far below what is needed to run the organization and to provide services to the public. Further reductions to civilian staff will be difficult because the Department must continue the basic flow and processing of paperwork to the District Attorney's Office and to the Courts. It must also maintain payroll, administrative and fiscal control functions.

Further reductions in civilian staff would impact training, fiscal controls, 911 Call Center staffing,[67] Records staffing, and other administrative support, which would slow the administration and impact all areas of police operations. Oversight of the operations will be limited as data would not be collected timely, reports not completed and analysis of police operations not conducted. The Department is currently at the lowest levels possible in the civilian support staff and further reductions would be counter-productive.

Moreover, with reduced civilian staffing, the Department will have decreased ability to apply and maintain grants, which will certainly decrease funding. Most of the police equipment and technology enhancements are made available through grant funds. Lastly, as reductions throughout the

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[66] Proposed cuts are based on average cost per sworn position, less non-personal, equipment, overtime, and vehicle expenses per position cut. Additionally, these numbers assume the continued postponement of the southern substation and the elimination of the crossing guard program.

[67] Notably, staffing in the 911 Call Center has not been reduced, because it would result in call answering times that exceed state mandated minimum call times and impact both public safety and officer safety on the street.

Department are implemented, it would become increasingly difficult to stay abreast of the latest policing strategies and integrate them into existing policies and procedures. This would weaken the Department's position when competing for federal dollars.

This means that to meet the projected budget reduction estimates noted above, cuts will need to come almost entirely from sworn staffing. And, while the Department would try to minimize reductions to Patrol, other areas of the Department have already been cut so drastically, that Patrol cannot be spared. Supplies and equipment budgets, overtime budgets, and vehicle expenses would all be reduced commensurate to staffing reductions. In addition, the City would continue to defer the opening of the Police Substation, delaying the expected efficiencies in deploying the Southern Patrol Division.

b. Investigative Service Impacts

(i) Investigation Impacts to Date

As staffing has been reduced Department-wide, BOI reports fewer cases received, fewer cases investigated, and more cases not assigned due to lack of resources. Cases to BOI are a direct result of Patrol activity. As resources decrease in Patrol, the number of cases referred for investigation declines. As response times increase and fewer resources are available on-scene, the solvability of cases also declines. As investigative staff reductions occur, fewer crimes are investigated and the number of cases not assigned due to lack of resources goes up. Notably, the Department estimates in excess of 6,000 cases will not be investigated due to lack of resources in calendar year 2011 (more than double the Department's target maximum).

The Department has already experienced a change in how cases are handled. Compared to the same time last year, the first quarter of this fiscal year (July 1, 2011 to Sept. 30, 2011), there is a 4.46% increase (593 more cases) in the number of cases received, but an 11.44% drop (1055 less cases) in the number of cases investigated. The number of cases not assigned due to lack of resources has increased by almost 80% or 901 cases for the same time period.

(ii) Anticipated Impacts on Investigations

With the anticipated reduction targets, investigative resources will diminish even more. Without being able to predict crime patterns, it is difficult to say with certainty what crimes will not be investigated, but the Department will have to prioritize cases, ensuring those cases with the most likelihood to be solved and lead to prosecution or those of the most serious nature (e.g., crimes against persons) will continue to be investigated. All homicides and sexual assaults will be assigned for investigation; however, almost all other types of crimes will be evaluated and either assigned for follow-up investigation or closed due to a lack of staffing resources. Property crimes would be at the low end of the priority and will most likely not be investigated.

A few examples of cases most likely not to get investigated are:

- Most misdemeanor cases, unless an arrest was made by patrol units and conclusive investigative action had been completed at that level;
- Cases related to stalking and terrorist threats that involve one person's word against the other (these cases involve conducting follow-up interviews, a threat assessment of the suspect, and locating independent witnesses or corroboration and are therefore time-consuming);
- Most property crimes where there is a time delay in reporting, there is no identifiable suspect, the victim is not cooperative, no viable leads, or no likelihood of charges being filed by the District Attorney's Office;
- General graffiti cases;
- Auto thefts will be referred to a regional task force and will be limited by task force resources;
- Vice crimes enforcement (prostitution, alcohol related violations, pimping, other quality of life issues) will be severely limited; and
- Internet prostitution and motel/hotel prostitution investigations, massage parlor regulation and compliance investigations, residential brothel investigations.
- As certain crimes continue to fall to the bottom of the priority and are not investigated, the likelihood of that crime increasing in the community is high. For example, if we do not investigate auto thefts, we can anticipate an increase of auto thefts to follow. Ultimately, crime will increase in San José as this cycle continues.

It is estimated the anticipated cuts, as tracked by calendar year, will impact Department performance as follows:

Activity	**Estimated CY 2012**		**Estimated CY 2013**		**Estimated CY 2014**	
Number of officer-initiated calls	↓ 35%	60,000	↓ 40%	36,000	↓ 10%	33,000
Number of car & pedestrian stops	↓ 35%	45,000	↓ 40%	27,000	↓ 10%	24,000
Cases received	↓ 10%	49,000	↓ 15%	42,000	↓ 5%	40,000
Cases investigated	↓ 20%	27,500	↓ 25%	21,000	↓ 5%	20,000
Cases not assigned due to lack of resources ("target" is a targeted maximum no. of cases)	↑ 30%	8,300	↑ 30%	11,000	↑ 10%	10,000
Cases resolved	↓ 25%	25,700	↓ 30%	18,000	↓ 10%	16,000

Source: City of San José Police Department.

c. Community Policing Impacts

(i) Impacts on Community Policing to Date

A decline in community policing efforts means that a police force shifts from a balance of proactive and reactive policing to a more exclusively reactive style of policing. Proactive community policing efforts are documented in the number of officer-initiated calls, pedestrian stops, car stops, special event activity, and community meetings attended. As shown above, those efforts have been reduced. Furthermore, staffing in the community services division has been reduced to one crime prevention specialist for each of the four divisions. The bulk of community policing efforts now rests on the members assigned specifically to Patrol. Staff will continue to attend community meetings and events to provide critical outreach to include information on crime trends, updates on significant crimes in specific neighborhoods, and education as possible. Although community policing efforts have diminished, the Department recognizes that good community relationships are critical to effective policing. As such, the Department is actively working with community members to improve its community policing plan.

(ii) Anticipated Impacts on Community Policing

If the anticipated level of reductions is realized, the Department will continue to move towards a reactive policing model and focus efforts on core services. Outreach to the community will be limited and community policing services would be eliminated or severely reduced, such as truancy abatement, burglary suppression, community education, attendance at community meetings and special events, the crossing guard program, and the Neighborhood Watch program.. Patrol officers will no longer have time to conduct proactive police work or community policing. The elimination of community policing efforts will diminish the effectiveness of the remaining patrol officers and (as noted in the studies above) further impact the residents' perceptions of the police force.[68] Good community relationships lead to cooperation and participation in successfully solving and preventing crime. As resources diminish within the police department there is less positive interaction with the community. As a direct result, community members may decide not to report crime or participate in helping solve investigations.

Cutting another 183 positions will dramatically impact all sworn functions. The number of officer initiated calls and car stops is anticipated to drop by approximately 35% in the first year, 40% in the second year and another 10% in the third year. Participation in special events will be reduced by 50% in the first year and eliminated in the second year. All special events will need to be paid for by the event promoter on overtime or through the secondary employment unit. Participation in community meetings will be limited and attended by the division captain as time allows. Activity

[68] Increased online reporting may offset community frustration; however these reports still require staff time to document and process.

reports will be available to the community through the current web-based crime reports but specialty reports will not be available. The decrease in community policing efforts may impact the availability of federal funds through the COPS Office that focuses support to those agencies with a strong community policing plan. School resource officers will not be deployed. Schools will continue to have police response, but it will be through Patrol. As a result, we lose the relationships developed between school principals and police officers, between students and officers.

The relationship between the community and the police department ultimately impacts how the community feels about policing efforts, as well as its willingness to report crime and assist the department during an investigation. As community policing efforts decline, it is expected that the solvability of crimes will diminish over time.

d. Public Knowledge of Layoffs and Crime Spikes

Another trend that the SJPD has been following is the correlation between the timing of when information about SJPD layoffs becomes publicly known and crime spikes. Just prior to a recent crime spike, information became publicly available regarding upcoming police department layoffs. Although it may not always hold true that fewer police officers equals more crime, what SJPD has recently observed is that the *announcement* of fewer patrol officers has been associated with increases in certain types of criminal activity.

In March of 2011, information concerning the SJPD's reduction in force – which involved a loss of positions, reorganization of the department and elimination of certain units (which were absorbed into other units) – became publicly known. Following this dissemination of information regarding the reductions in force, San José experienced a significant increase in certain types of crime in May and June of 2011. The Department has evidence that this spike is due, at least in part, to the spread of information related to police layoffs. Through conversations with arrestees and prostitutes and through communications observed on gang-related social media, police officers have learned that out-of-city criminals seek out information suggesting that SJPD no longer investigates street crimes or suggesting there are fewer patrol officers on the street. During the recent crime spike, investigative units monitored gang-related social media activity. These officers began seeing messages to the effect of "the streets are ours now" after reports of the layoffs became publicly known. Moreover, officers in the Metro unit observed an increase in the number of prostitutes, followed by explanations that the prostitutes had come to San José after hearing that the City was no longer policing prostitution.

It is unclear whether the recent spike would have occurred had information of the reduction in force not been so publicly known. In any event, there seems to be a correlation between the crime spike and the recent layoffs. The Department anticipates that the impact of further cuts and reductions will likely follow this trend.

As of 2009, the City had the second lowest violent crime rate of any city with 500,000 or more residents. By October 2011, however, the number of homicides in San José has already surpassed the City's total number of homicides in 2010 by a significant amount. The SJPD has observed, over the past few months, increases in violent crime, 911 calls, and response times. As noted above, it is difficult to directly correlate budget or staffing reductions with increases in crime. Nevertheless, there do appear to be identifiable trends showing a correlation between the recent spike in crime and recent staffing reductions. The police department is focusing current resources in an effort to stop this trend. However, future reductions will impede these efforts.

e. Response Time Increases

(i) Response Time Increases to Date

Over the past few years, the Department has experienced an increase in the number of calls it receives and increased average response times to emergency calls for service.[69] Faster response times increase the likelihood of apprehending the offender at or near the crime scene. This is vital for catching suspects and collecting evidence necessary for a good prosecution.

Furthermore, faster response times to calls can prevent injury to victims. A faster response to a domestic violence call could mean the difference between life and death. Police are often the first responders to medical emergencies. In some instances, fire or medical response personnel will not enter a scene until it has been secured by the police. With a trend that has steadily increased to, and is now above, an average of 6 minutes for top priority calls, there is cause for concern. Moreover, with continued cuts, these trends will continue as described in detail below.

The Department uses a call prioritization method to direct limited resources according to event severity. All calls for help are categorized by the call prioritization method to differentiate between urgent calls for help and less urgent calls.

Priority 1	• There is a present or imminent danger to life • There is major damage to or loss of property • The incident may have an immediate impact on and need for Citywide police resources
Priority 2	• District-wide response when a crime is in progress or has just occurred • There are injuries or there is the potential for injury • The suspect is still present or in the area

[69] Trends in call volume are fairly unpredictable and do not necessarily relate to volume of crimes or resources on the street. Although logic indicates that as crime goes up, call volume goes up, this is not always the case. Call volume is impacted by public awareness, as well as the relationship between the police and the community.

	• All missing person reports where persons are at-risk or are children under the age of 12
Priority 3	• District-wide response when a crime has just occurred; there is property damage or the potential for it to occur; the suspect has most likely left the area
Priority 4	• District-wide response to a non-violent crime when there is no present or potential danger to life or property

Source: City of San José Police Department.

The Department's target for Priority 1 Average Response Time is 6 minutes;[70] the Average Priority 2 target is 11 minutes. As shown below, the SJPD is not meeting either of those targets at this time.

Police Response Data: Priority 1 and Priority 2 Events
By Fiscal Year (July-June)

Response Time Average in Minutes

Priority 1	Minutes
Target	**6.00**
2007-2008	5.91
2008-2009	6.02
2009-2010	5.97
2010-2011	6.11

Priority 2	Minutes
Target	**11.00**
2007-2008	11.38
2008-2009	11.87
2009-2010	12.11
2010-2011	13.67

Source: City of San José Police Department.

In July 2007, the City implemented a comprehensive GPS automated dispatching system. This system tracks the locations of all patrol cars and automatically dispatches the closest vehicle to the incident.[71] By reducing Priority 1 response times (by roughly a minute), the GPS system has minimized the net impact of the increases caused by reductions in staffing. This is important because, had staffing and budget remained equal, a reduction in response time would have been expected since the implementation of this new system. Instead, the impact of this use of technology has been to minimize the impact of the staffing reductions on response times.

In addition to this GPS technology, the Department underwent consolidation and restructuring of Special Operations in order to maximize the number of patrol officers and minimize the impact on response to calls for service. In 2011-2012, direct cuts to Patrol could not be avoided and as a result, response times are on the rise.

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[70] On most calls, especially high priority events, a two-officer response is required and action is not taken until the second unit arrives.

[71] Under the previous system, the dispatch would go to the officers assigned to that area (who may or may not be the closest patrol car to the site of the incident at a given point in time).

(ii) Anticipated Response Time Increases

The SJPD will continue to prioritize and respond to calls where there is an imminent danger to life or major damage or loss of property. However, response times for all calls, including violent crimes, will continue to rise. Lower priority calls will hold for available units and have longer wait times or canceled due to lack of resources. The Department may increase the types of low priority calls for which there will be no response and an alternative for reporting such activity may need to be addressed.

Response to Priority 1 and Priority 2 calls will remain the focus for the Department. In the first quarter of 2011-2012, we have seen an increase in average response times and expect that further reductions in staff will lead to longer delays; Priority 1 average response times increased by almost 7% and Priority 2 average response times increased by almost 42%.[72]

The following are the estimated average response times in minutes.[73] These estimates are based on the increase in average response times in the first quarter of fiscal year 2011-2012 (after recent reductions were implemented) compared to the first quarter of fiscal year 2010-2011.

Average Response Times in Minutes		
	Priority 1	Priority 2
Actual: First Quarter 2010-2011	6.04	11.57
Actual: First Quarter 2011-2012	6.46	16.40
Estimated: 2012-2013	7.24	22.14
Estimated: 2013-2014	8.33	36.53
Estimated: 2014-2015	8.75	40.18

Source: City of San José Police Department.

Response to Priority 3 and Priority 4 calls will also be severely diminished. These calls will wait until units are available able to respond. Sergeants will be required to monitor these calls and direct officers to respond as the situation warrants. There will be no response to these calls during major events. Severely delayed responses or no responses may drive an increase in victimization. Community members may be less likely to report crimes as they observe a reduction in the Police Department's ability to respond to calls for help. Community members have communicated to Department staff that this is already happening due to the current increase in response times. An increase in crime may also occur as criminals become aware of the lack of response by police.

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[72] July 1, 2010 through September 30, 2010 compared to July 1, 2011 through September 30, 2011.

[73] Based on an increase of 7% in First Quarter Priority 1 average response times, estimated 2012, 2013 and 2014 Priority 1 was based on a 12%, 15% and 5% increase, respectively. Based on an increase of 42% in First Quarter Priority 2 average response times, estimated 2012, 2013 and 2014 was based on a 35%, 65% and 10% increase, respectively.

In the first quarter of fiscal year 2011-2012, average response times for Priority 3 and Priority 4 calls have increased; further reductions in staff will lead to even longer delays. As noted above, Priority 3 average response times increased by 20% and Priority 4 average response times increased by 24.5%.

Estimated average response times in minutes:[74]

Average Response Times in Minutes		
	Priority 3	Priority 4
Actual: First Quarter 2010-2011	37.25	41.81
Actual: First Quarter 2011-2012	44.84	52.05
Estimated: 2012-2013	65.02	78.08
Estimated: 2013-2014	97.53	121.01
Estimated: 2014-2015	107.28	133.12

Source: City of San José Police Department.

Response times are a primary indicator of patrol service levels. As patrol resources diminish, response times get longer because officers are more reactive and go from one call to another. The Department will always respond to Priority calls and as resources are pulled to these priority calls, lower priority calls will pend longer. Additionally, there will be little time between calls to do follow-up investigations, interviews or evidence collection. As response times increase, there is the possibility of increased victimization, injury or property damage. Slower response times decreases the likelihood of apprehending the offender at or near the crime scene or finding witnesses to an event, which impacts investigative abilities and leads to less solvable cases.

(iii) Capacity Diminishment

The SJPD has already experienced difficulty in responding to multiple critical events at one time due to the limited resources in Patrol. During a critical incident,[75] there is significant call saturation in the 911 Call Center, and response times to other priority calls increase dramatically. Further reductions will exacerbate this condition and make it increasingly difficult for police to respond to multiple major events. For example, during a recent officer involved shooting there were only 73 total units on duty. Because a number of units were actively involved in the event, responses to other calls were significantly delayed. On average, Priority 1 calls had a response time of more than 10

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[74] Based on an increase of 20% in First Quarter Priority 3 response times, estimated 2012, 2013 and 2014 Priority 3 was based on a 45%, 50% and 10% increase, respectively. Based on an increase of 24.5% in First Quarter Priority 4 response times, estimated 2012, 2013 and 2014 was based on a 50%, 55% and 10% increase, respectively.

[75] For example, a homicide, an officer involved shooting, or a major violent crime.

minutes and average response times for Priority 2 calls exceeded 27 minutes that day. These types of resource driven events occur regularly in San José.

Further reductions in sworn staff would limit the Department's capacity to respond to a critical event. Response to multiple events at one time will be severely impacted. As the largest law enforcement agency in the county, SJPD cannot rely on mutual aid for these types of events. Typically, surrounding agencies rely on SJPD to assist on their major events. Multiple critical events will utilize all available resources leaving the City unprotected and could lead to increased violence and victimization.

Finally, another important consideration is the impact these decisions will have on the staff. We cannot overlook the impact of what these cuts mean to department members. It is not only the level of staff resources that impacts the success of the police department. The morale of officers is critical in building relationships with the community and ensuring we meet the goals and expectations of that community. We cannot ignore the impact these decisions will have on our dedicated police force that has worked so hard to reduce crime in the City, protect our neighborhoods and keep our community safe.

B. IMPACTS ON SAN JOSE FIRE DEPARTMENT

1. Department Overview

a. Current Capacity

The San José Fire Department (SJFD) currently employs 650 authorized sworn personnel and 101 non-sworn staff including Fire Communication Dispatchers and civilian personnel.

SJFD provides the following core services: Emergency Response, Prevention Code Compliance, Fire Cause Investigation, Emergency Management, and Community Outreach and Education.[76] The Fire Department provides emergency response services through its established resource deployment system. The system consists of trained firefighters, fire engineers and fire captains assigned to engines and truck companies strategically distributed in fire stations throughout the community. The primary goal of the SJFD deployment system is to arrive at the scene of a structure fire so that it can be contained within the room of origin; and to arrive at a medical emergency prior to the point of a patient's irreversible brain damage.

The emergency deployment system consists of:

- 30 Engine Companies – staffed with one Captain, one Engineer, one Firefighter and one Firefighter/Paramedic;
- 10 Truck Companies (including one Search and Rescue company) – staffed with one Captain, two Engineers and one Firefighter/Paramedic; and,
- A Paramedic Supervisor and five on-duty Battalion Chiefs.

Included in this total is an air rescue company at San José International Airport and a Hazardous Incident Team. Staffing at least one paramedic to all SJFD in-service engine and truck companies allows the Department to provide advanced life support and pre-hospital care services throughout the community.

- The basic fire department unit is a small unit called a **Company.** San José has two main types of companies: **Engine Companies** and **Truck Companies.**
- A **Fire Station** is a structure or other area set aside for storage of firefighting apparatus. It may contain multiple companies.
- **Fire Engine** refers to fire suppression apparatus (also known as a pumper) that carries a fire hose, has a large capacity water tank and is equipped with a fire pump. Primary firefighting duties include the application of water and rescue.
- **Fire Truck** refers to fire suppression apparatus equipped with an aerial ladder and carries a large inventory of tools such as extrication, ventilation and forcible entry equipment and rescue systems. Primary firefighting duties include forcible entry, access, ventilation, salvage, overhaul and rescue.
- A **Structure Fire** is a fire in or adjacent to any structure. The initial response, or first alarm, includes 3 engine companies, 2 truck companies, 1 Paramedic Supervisor and 2 battalion chiefs.
- A **Second Alarm Fire** exists when additional units are requested to assist with a structure fire; SJFD requires 2 engines, 1 truck and 1 battalion chief.

[76] The Public Education/Community Outreach Office was eliminated due to the budget deficit. SJFD accommodates requests for Station Tours, Fire Safety Presentations, Juvenile Fire Setter Intervention, and Fire Prevention Activities on a very limited basis.

The current daily staffing level is, at a minimum, 160 sworn personnel on duty during a 24 hour period.[77] Following the closure of one station in 2009-2010 due to budget cuts, the City now has 33 fire stations located throughout the community. In the past, 11 SJFD stations had two assigned and staffed in-service companies. However, currently, only 7 fire stations have two in-service fire companies (one engine and one truck) with two stations each day subject to a temporary company closure. The remaining 26 fire stations have one assigned emergency response company (a fire engine or truck).

To put the work of the Fire Department into perspective, in 2009-2010 SJFD received 51,349 emergency requests. During this time, San José experienced fire loss damage in the amount of $29 million, and the department was able to prevent an estimated $542.7 million in property damage. Four lives were lost to fire over that period of time.

- **Response time** refers to the time from receipt of alarm, answering the 911 call at the dispatch center, to on scene arrival by the first fire department unit.
- **USAR** refers to San José's Urban Search and Rescue Company, which is staffed with four personnel including one paramedic.
- **Hazardous Incident Team** refers to a unit trained as Hazardous Materials Technicians or Specialists.
- **Flexible Brown Out** occurs when a fire station temporarily reduces its number of assigned on-duty companies (apparatus and crew), when a daily staffing vacancy occurs. In the event of a vacancy, personnel would be moved from station to station leaving one engine or truck company without personnel to operate it.
- **Room of origin** refers to the room or area where a fire starts. The goal is to keep 90% of all structure fires within the room of origin. (Compare to **Building of Origin**, referring to containment to the building where the fire was ignited).
- **Flashover** refers to a fire condition inside a structure where all combustibles in the room reach their ignition temperature and ignite simultaneously. This is usually the point where the fire extends beyond the room of origin.

b. Department Organization

The SJFD senior command structure consists of a Fire Chief, an Assistant Fire Chief, three Deputy Chiefs, and two Deputy Directors. A Fire Captain works for the Fire Chief as the Department Public Information Officer and the Department staffs its own Fire Communications Center. There are six Bureaus in the San José Fire Department: The Bureau of Field Operations, Bureau of Emergency Medical Services (EMS) and Training, Bureau of Fire Prevention, Bureau of Administrative Services, Bureau of Support Services, and Office of Emergency Services.

The Bureau of Field Operations is the largest Bureau in the Department. Under this Bureau, fire companies are dispatched and respond to emergencies through a series of planned and scripted activities. The Bureau's mission is to ensure that properly trained and equipped personnel arrive at the scene of an emergency and initiate the appropriate actions to reduce the loss of life and property.

[77] This figure assumes two companies are temporarily closed, subject to the flexible brown out plan (discussed below), due to low daily attendance.

c. Pre-hospital Emergency Medical Care

Pre-hospital emergency medical care is authorized and regulated by statute through the State of California Emergency Medical Services Authority, a department of the State Health and Human Services Agency. The County of Santa Clara Health Department provides oversight for the State system which includes all cities and fire districts within the County. The City of San José Fire Department provides first responder Advanced Life Support (paramedic) services primarily within the incorporated City limits through a direct contract with the County of Santa Clara Emergency Medical Services (EMS) Agency. The County also contracts with a private company to provide emergency ambulance transportation services exclusively to all County areas (except to the City of Palo Alto).

The term of the contract is five years, July 1, 2011 through June 30, 2016. It requires the Fire Department to respond to requests for emergency medical services within San José and specifies response time requirements, as well as certification levels for responding personnel.

The City is partially reimbursed (approximately 61%) for the total cost of the program which supports the County-wide response system and enhances the services provided to the community. The decision to enter into the agreement was approved by the City Council based upon the recommendation of City and Fire Department Staff. The contract may be extended by mutual agreement of the City and County of Santa Clara and there is a "no-fault" 180 day termination clause that can be initiated independently by either party.

The Fire Department has provided pre-hospital emergency medical services for many years. However, SJFD formally began delivering paramedic level services through engine companies in 1995. Formerly, the City was a contractor of first responder paramedic level services and had an agreement with the exclusive ambulance provider (as did all County fire agencies). County fire agencies and the EMS Agency subsequently agreed that a direct relationship between first responder fire agencies and the County was more appropriate and this change in the relationship occurred with the approval of the current agreement.

d. San José Statistics

San José is the 10th largest city in the United States and population growth trends for the City have continued upward for decades. It also ranks in the top 50 largest U.S. cities by land area and is listed by the California Department of Forestry and Fire Protection as a city that contains "Very High Fire Hazard Severity Zones."

The San José Fire Department protects 206 square miles and approximately 1.2 million residents (City and county areas) and has traditionally operated with a leanly staffed firefighting force in comparison to other large cities in the U.S. The table below compares the SJFD to the staffing and resources of neighboring communities, as well as of the County of Santa Clara.

Agency	Service Pop.	No. of stations	No. of sworn fire personnel	Daily staffing
Gilroy	49,800	3	36	9
Milpitas	69,000	4	63	15
Mountain View	72,100	5	70	20
Palo Alto	77,779	8	105	30
City of Santa Clara	114,700	10	148	39
Santa Clara County Fire Department	240,789	17	247	68
South County Fire District	24,533	4	29	12
Sunnyvale	135,200	6	82	24
Neighboring Communities TOTAL	783,901	57	780	217
City of San José	**1,037,567**	**33**	**650**	**168**
Santa Clara County TOTAL	**1,821,468**	**90**	**1,430**	**385**

Source: City of San José Fire Department.

Per capita, SJFD has the lowest total number of firefighters of the top 25 U.S. cities based on population, despite being the 10th largest city. In addition, given the populations served, the SJFD has the fewest stations, the lowest number of sworn fire personnel, and the lowest daily staffing levels. As a comparison, each of San José's five battalions, which have a maximum of **8 fire stations**, covers an average area of 41 square miles with a population of 200,000 residents. Comparatively, this area is about the same size as the cities of Milpitas, Mountain View and Santa Clara combined, which are served by a total of **19 fire stations**.

Although the SJFD continues to be a highly effective firefighting force and emergency services provider despite its limited resources, services are a challenge to maintain. Further projected reductions, however small, will have a dire impact on SJFD's overall effectiveness. Appropriate and sufficient geographic coverage is critical to meeting response time targets. Those targets are based on the time it takes to confine a fire to the room of origin prior to flashover and the time needed to get to a medical emergency prior to the point of the patient's irreversible brain damage. As resources (companies and fire stations) are eliminated due to the anticipated budgetary reductions, response times will increase and likely exceed response time compliance standards. Moreover, as the largest firefighting force in the County, the Department cannot rely on mutual or automatic aid from neighboring jurisdictions to provide basic levels of fire and emergency medical services; typically, other agencies rely on SJFD for assistance. It is not an overstatement to say that longer response times will result in more lives lost and much greater property damage and loss.

2. Department Budget

In 2006-2007 and 2007-2008, following voter-approved general obligation bonds to construct three new fire stations, 41 positions were added to the Fire Department in order to staff those stations. However, in 2009-2010, budget cuts began to affect the SJFD.

The current amount appropriated to the Fire Department from the General Fund budget, based on the 2011-2012 Adopted Budget, adjusted for rebudgets and grant-related expenditures, is $158,611,097 or approximately 18% of the total adjusted General Fund. The Fire Department has had a fairly stable adopted budget in terms of actual dollars over the past few years:

	2009-2010	2010-2011	2011-2012
Adopted Budget*	$154,457,416	$153,081,702	$151,663,759

*Source: Adopted Budgets 2009-2010 through 2011-2012; *Rebudgets and Grant-related Expenditures Removed.*

However, to meet its budget targets, the Fire Department has had to significantly reduce staff and services over the three year period of time; including a reduction in sworn staff from 753 FTE's in 2008-2009 to 650 FTE's[78] in the current fiscal year (an operating budget reduction of $30 million).

From 2012-2013 through 2014-2015, as set forth in the potential General Fund Budget Balancing Scenario described in Section II of this report, the Fire Department is anticipating expenditure reductions totaling about 9% of the 2011-2012 Adopted Budget.

3. Consequences of Budget Reductions in Fire Department

SJFD has sought ways to reduce service impacts of the budget cuts to date, including implementing the Dynamic Deployment system discussed below. Several internal actions have been proposed, initiated, or implemented to ensure the highest possible utilization of existing emergency response resources. These include reduced company response to unconfirmed emergencies, fewer responders dispatched to lower priority incidents, transferring patient care when appropriate, automatic and mutual aid and increased opportunities to share resources across jurisdictional boundaries.

Yet, even with these efforts, the Department projects that additional reductions will negatively impact response time performance (compliance) and the Fire Department's capacity to respond to two or more sustained structure fires in single family dwellings that occur within the same time period. Additionally, major events (two or more alarms) and longer duration emergencies will affect the Fire Department's ability to manage emergencies without significant support and assistance from outside agencies.

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[78] It is important to note of those reductions, 49 FTEs were reinstated as a direct result of a federal grant.

a. Staffing and Capacity Reductions

(i) Reductions to Date

The Fire Department has experienced a 13.5% reduction in staff since 2007-2008 and is at a point where further budget cuts cannot be absorbed as services will be at unacceptable levels for the public's welfare. Service levels are already below acceptable levels for the Department. And yet, without emergency measures, continued cuts loom on the horizon. As projected in Section II, the Fire Department may face the following expenditure reductions in 2011-2013 through 2014-2015.

Fire Department Reduction Estimates			
	Reduction from 2011-2012 Adopted Budget	**Total Cuts**	**Projected Cuts**
2012-2013	3.5%	$ (5,500,000)	44 positions, 3 companies
2013-2014	4.7%	$ (7,406,000)	60 positions, 4 companies, Close at least one fire station
2014-2015	1%	$ (1,140,000)	14 positions

** Based on $125K/position, excluding retirement costs*

A fire station was closed in August 2010, dropping the total number of stations from 34 to 33. Moreover, four fire engine companies were eliminated – reducing the number of engine companies to 30; one truck company was eliminated – reducing number of truck companies to 9. In an effort to lessen response time impacts of these cuts in 2009-2010, the Fire Department implemented Dynamic Deployment dispatching,[79] an automated resource management system.

Other reductions included:

- Staffing on fire apparatus was reduced, including the reduction of staffing on most fire truck companies from 5 to 4 per day and the elimination of a Hose Wagon (net reduction of 31 positions and redeployment of 1 position to the relief pool).
- The number of fire apparatus at the airport was reduced from three to two (7 positions eliminated).
- Elimination of a dedicated Hazardous Incident Team (HIT); HIT-trained staff were reorganized into a two-company task force that will provide this service.

[79] Dynamic Deployment is an automated method of evaluating the overall deployment system's ability to provide consistent emergency response coverage to the community with available resources. It suggests, when indicated, the temporary re-assignment of remaining resources to reduce coverage gaps that may exist due to incident activity. The Department formerly used a similar practice primarily as a response to large scale or multiple emergencies. The major difference between Dynamic Deployment and the former practice is that Dynamic Deployment re-assesses the City's coverage on a continuous basis.

- Reductions in fire management and administrative staffing (19 positions).

In 2010-2011, and to date, the cuts have continued. SJFD laid off 49 firefighters and reduced daily staffing levels from 203 firefighters per day to 179 in 2010-2011.

In July 2011, the Fire Department implemented a Flexible Brown-out Plan as a cost saving measure. Under the Plan, no fire stations are closed, but the seven fire stations with two assigned emergency response companies will no longer have both companies staffed, in-service, and available to respond to emergencies at all times. When a vacancy occurs, firefighters from a browned-out fire company will be deployed to work elsewhere in the City in place of absent personnel or to fill other Department needs. It is anticipated in this scenario that up to two fire companies (i.e., two of the seven stations noted above) will be subject to a brown-out each day based upon available on-duty staffing. This was a departure from the standard operating practice of filling a vacancy with relief personnel or overtime personnel.

Summary of Staffing Changes To Date			
	2009-2010	**2010-2011**	**2011-2012**
Fire Stations	34	33	33
Total Companies	45	40	40*
Engine Companies	*34*	*30*	*30**
Truck Companies	*10*	*9*	*9**
Urban Search and Rescue	1	1	1
Hazardous Incident Team	2 person	2 person	Eliminated[80]
Airport Rescue Team	6 person	4 person	4 person
Battalion Chiefs	5	5	5
Total Sworn FTE's	851	751	650
Total daily FF Staffing	**203**	**179**	**168***
Total staffing with brown-outs			***160***
**Subject to daily brown-outs, implemented effective July 2011*			

Source: City of San José Fire Department.

One impact of the brown-out plan is to reduce the daily staffing level to a minimum of 160 Firefighters on duty during a 24 hour period (if 2 companies are temporarily closed due to low daily attendance). The Fire Department anticipates that this measure will save over $3.5 million dollars. However, a browned-out company will increase response times to the area with the closed fire company. The remaining companies will have to go further from their respective areas to provide service to a larger geographical footprint. Extended periods could result when other companies are already responding to emergencies in different areas.

(ii) Anticipated Staffing and Capacity Reductions

In finding ways to address and absorb the current and anticipated budget cuts, SJFD is doing its best to keep stations open, opting instead for reductions in staffing dollars (overtime and consequently companies). This is because the loss of a station has the greatest impact on increasing response time and will leave some first due areas with response time performance dropping to below 15%, and

[80] See footnote in chart below for further explanation of changes to Hazardous Incident Team.

potentially 0% compliance with targeted response times. And yet, if the anticipated budget reductions are realized, at least one station, and potentially three others, will be closed over the next 3 budget years. As long as reductions continue, response time performance will increase (which is already much higher than the nationally recognized standard and higher than targets), as will the property loss experience and deaths from cardiac arrest.

In 2012-2013, without cost containment measures, the budget reductions are estimated at $5.5 million. If those budget projections are realized, two additional engine companies and a truck company, potentially including the Hazardous Incident Team and the Urban Search and Rescue Team will be eliminated. Only two stations with more than one full time company will remain, with two additional two-company stations subject to daily brown outs. And, the anticipated budget cuts would result in total daily staffing being reduced to 148 firefighters on duty (translating to one firefighter on duty for every 7,300 residents).

In 2013-2014, the budget reduction is estimated at $7.4 million. Should this anticipated budget reduction occur, the SJFD will face a critical staffing emergency, with staffing levels below even the minimum acceptable threshold. The Fire Department will be down to 31 full time companies and at least one, but possibly as many as four, fire stations will be closed. (SJFD has not yet determined what the appropriate distribution of engine companies and truck companies would be at this level). The total daily staffing would be reduced to approximately 124 firefighters on duty (translating into one firefighter on duty for every 9,100 people). Another 1% (or $1.1 million) budget reduction would be applied in 2014-2015, meaning further company reductions.

The chart below depicts the summary of staffing reductions to date on the left side of the chart. The right side shows possible staffing scenarios that SJFD has developed based on the projected budget impacts from 2012-2013 through 2014-2015.

Staffing Changes To Date				Possible Reduction Scenarios		
	2009-2010	**2010-2011**	**2011-2012**	**2012-2013**	**2013-2014**	**2014-2015**
Fire Stations	34	33	33	33	32 or less	31 or less
Total Companies	46	41	40*	37*	32 or less	31 or less
Engine Companies	34	30	30*	29*		
Truck Companies	11	10	9*	8*		
Urban Search and Rescue	1	1	1	1	Eliminated**	Eliminated**
Hazardous Incident Team[81]	2 person	2 person	Eliminated	Eliminated	Eliminated**	Eliminated**
Airport Rescue Team	6 person	4 person	4 person	4 person	Eliminated	Eliminated
Battalion Chiefs	5	5	5	5	4	4
Total Sworn FTE's	851	751	650[82]	609	541	528
Total daily FF Staffing	**203**	**179**	**168***	**156***	**136**	**132**
Total staffing with brown-outs			***160***	**148**	***128***	***124***
*Subject to daily brown-outs, implemented effective July 2011 ** SJFD will no longer be able to provide this function.						

Source: City of San José Fire Department.

The Fire Department's analysis shows that daily staffing below 144 firefighters per day is below even a minimally acceptable level to provide fire and emergency services to the City of San José. The analysis has shown that given the City's demographics, density, hazards and occupancy inventory, on-duty staffing cannot be reduced below this level without extremely endangering the effectiveness of fire suppression efforts and emergency medical responses and the ability to bring emergencies under control. At these levels, the system will be unable to respond to the anticipated emergencies both in terms of maintaining an acceptable response time performance and having the resources to respond to multiple emergencies of any significance.

b. Response Time Impacts

(i) Response Time Impacts to Date

Although SJFD has had a call volume increase of 5% over the past year, this measure is unpredictable. A more useful performance measure is response time because it is reasonably

[81] In 2008-2009, the Hazardous Incident Team (HIT) was a stand-alone, specialized 4-person company. In 2009-2010, it was reduced to a 2-person team and was attached to a truck company. Members of the truck company also have HIT training, but it no longer operates as a stand-alone HIT unit. Therefore, if the 2 person specialized team is eliminated in 2011-2012, then the truck company could continue to provide HIT services. In 2013-2014, under the projected cuts, SJFD will no longer be able to provide HIT services. The only service provided will be to deny entry into the hazardous area and to isolate the area until another service provider arrives.

[82] As previously noted, this number would have been 601 FTE, had it not been for the need for the City to maintain certain staffing levels in order to continue receiving the federal SAFR grant.

predictable insofar as it correlates with available Fire Department resources. Clearly the most disturbing result of the recent budget cuts is the upward trend in response times.

To put response time into context, a few examples are useful:

1. Sudden cardiac arrest calls are often used as the key measure of emergency medical performance: How long after the 9-1-1 call is received does it take for help to reach the patient and deliver lifesaving care? Recent research from the Mayo Clinic indicates that this type of patient has 6 minutes to live. A shock with a defibrillator within that time usually will restore the heart's rhythm. Even if the victim goes an additional minute without a normal heartbeat, the patient can still survive if paramedics restore breathing and administer key drugs, such as adrenaline.

2. Response time must be under 8 minutes in order to contain a fire to room of origin. Notably, with the vast increased use of synthetic materials in furnishing, window and wall coverings, this number has been steadily decreasing and, in some instances, flashovers occur within 2 minutes of the start of the fire according to the National Fire Protection Association (NFPA).

The NFPA has established a 6 minute minimum response time as a best practice for first responders to medical emergencies and fires. San José has identified that this is not a realistic target, given its geographic and staffing constraints. Accordingly, the City has adopted an 8 minute standard that must be achieved 80% of the time. Prior to July 2010, there was only one month in recent history where the City had not met this target. Since August 2010, however, SJFD has consistently fallen below its medical response time target on a monthly basis. Additional loss of resources will further deteriorate response performance, resulting in lives lost.

(ii) Anticipated Response Time Impacts

Should the Fire Department be required to reduce resources to the levels projected for 2013-2014, projected station closures in any of the districts will result in an impact in the overall response time performance for the City and/or an unacceptable response time performance within the first due area (well over 10 minutes or more). In all cases, the on-duty staffing will be below a level that will support the system capacity needed to serve the community in an acceptable or recommended way.

The reductions projected through 2014-2015 will result in a total of 30 remaining full-time fire companies. As such, it will be necessary to close additional fire stations and will result in significantly longer response time performance. The Department staffed 34 full time fire stations in 2008-2009 which could potentially fall to as few as 30 one-company fire stations in 2014-2015.

Analysis based on stations that would be most likely closed as a result of the cuts, and the accompanying impact of any single station would have on response time compliance in the areas

where the stations will be closed. As multiple stations are closed, these numbers would likely be worse than projected here, given the interconnectedness of the Fire Department's system. The modeling predicts response time performance experience to fall to the following levels:

Potentially Closed Stations	Response Time Compliance Within First Due Area	First Due Avg. Response Time (minutes : seconds)
Station 7, 800 Emory Street	65%	7 minutes: 17 seconds
Station 11, 2840 The Villages Parkway	13%	10 minutes: 32 seconds
Station 20 (San José Mineta Airport)	0%	unknown
Station 25, 5125 Wilson Way (Alviso)	0%	12 minutes: 49 seconds
Station 27, 6027 San Ignacio Avenue	2%	12 minutes: 04 seconds
Station 28, 19911 McKean Road	28%	10 minutes: 32 seconds
Station 30, 454 Auzerais Avenue	81%	6 minutes: 23 seconds

Source: City of San José Fire Department.

Under these projections, in some areas, the SJFD will have no ability to meet the 8 minute target response time. SJFD concludes that the projected on-duty staffing level that will result from closing nine additional fire companies from 2011-2012 levels (that is to say lowering on-duty staffing consistently below 144 Firefighters on-duty), would represent an unacceptable staffing level of fire and emergency medical response service for a City the geographic size, population, level of hazard, demographics and density of San José. Under the current budget projections, the Fire Department will reach these levels in 2013-2014. This would represent a service level emergency situation for the City.

c. Alternative Service Provision Models

As previously noted, truck company staffing has recently been reduced from 5-person companies to 4-person companies. This was done to retain the number of companies available at any time and to avoid station closures. The City will consider alternative service provision models to in an effort to reduce costs and / or to minimize the number of company and station closures. One example of this is the potential elimination of SJFD's provision of paramedic services (discussed below).

(i) Eliminate SJFD Provision of Paramedic Services

The Department will need to consider whether to continue to provide advanced life support services from fire companies. As noted above, the City is contracted with the County through June 2016 to provide Emergency Medical Services within City-limits. Under the agreement, SJFD provides first responder advanced life support services within the County pre-hospital care system, arriving at the scene of reported medical emergency within 7 minutes: 59 seconds at least 90 percent of the time.

Because SJFD arrives in time to provide early treatment and therapies, the County's contracted ambulance provider may arrive later, within 11 minutes: 59 seconds.

If staffing levels drop to the forecasted levels, the Department's response time performance on medical emergencies may increase to the point that it will not be possible to meet the response time requirements of the County First Responder contract. Already, the Department's performance has fallen to the point (performance below 95 percent compliance) that fines are levied monthly. The Fire Department will be in breach of the contract requirements if response time performance falls below 90 percent compliance. If SJFD's performance drops to the point where it is in breach of the contract, a decision will have to be made as to whether the Department can continue to support the First Responder Advanced Life support Program. If SJFD stops providing this service, the ambulance company would need to add several resources, ambulance units and staff, to arrive within 7 minutes: 59 seconds at a greater expense or continue to arrive at 11 minutes: 59 seconds providing a lower level of medical services. As a result, if SJFD discontinues this service, patients will suffer either: (1) because, under the more likely scenario, they will bear the expense of the added staffing and resources the County's contracted ambulance company would need to arrive within 7 minutes: 59 seconds; or (2) because they will not receive treatment within the clinically recommended time.

The first potential outcome is that the contracted ambulance company will need significantly increase staffing and resources to meet first responder advanced life support standards. This would likely require a dramatic increase in user fees. The increase in costs may be so great that it may not be feasible for the company to recover those costs from users, with the end result being a lower level of pre-hospital emergency medical services.

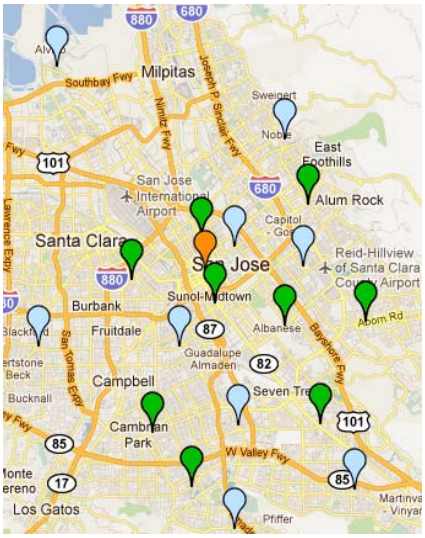
This leads to the second possibility, which is that that patients will have to wait longer for advanced life support services. This is particularly concerning for seriously ill or injured patients, and will lower the potential to resuscitate pulseless, non-breathing patients. In this scenario, the County might be forced to increase the response time performance requirements for the privately ambulance companies as a result of the severe decrease in resources to the overall system resulting from the City no longer providing paramedic services. Requiring ambulance companies to meet the current standards without the support of SJFD may prove to be cost prohibitive for private companies.

In conclusion, as the Department struggles to provide services in the face of continued budget reductions and fewer resources, SJFD staff will continue to evaluate methods and alternatives to service delivery to attempt to keep critical firefighting resources available for large emergencies to the extent possible. It should be noted that response time performance may be maintained through other types of response system strategies yet to be developed, however the capacity of the system to respond to fire emergencies within the City of San José cannot be maintained through these actions. Reductions in staffing and resources will have the greatest impact on the SJFD's ability to respond to multiple incidents and 2 or more structure fires that occur during the same time period.

C. IMPACTS ON SAN JOSE PUBLIC LIBRARY SYSTEM

1. Overview of the San José Public Library System (SJPL)

The San José Public Library System (SJPL) is the largest public library system between San Francisco and Los Angeles, serving approximately 958,789 residents, and providing access to all of Santa Clara County's 1,781,642 residents under the State of California universal borrowing program. The SJPL's main library is the Dr. Martin Luther King Jr. Library (King Library), located in downtown San José. King Library opened in 2003 and is the first joint-use library in the United States shared by a city and a major public university (San José State University). In addition to the King Library, the SJPL has 22 other branches, only 18 of which are currently operational. Those four non-operational branches were constructed following the passage of bond measures. At the time of this report, three of these newly constructed branches are closed due to budget cuts and one branch – still under construction – will not be opened due to budget constraints.



The SJPL provides one of the City's most popular services. Each year, the SJPL branches have more visitors than attendees at home games of the San Francisco Giants, 49ers, Oakland As, and San José Sharks *combined*. The average San José resident checks out approximately 15 books each year – more than double the Bay Area average. Further, recent survey results indicate that for the better part of this decade, at least four out of five San José residents have taken advantage of the SJPL services at least once per year. Of those households with children, 37% have used library services 12 or more times per year.

San José Branch Libraries				
1	Almaden Branch		10	Hillview Branch
2	Alum Rock Branch (Dr. Roberto Cruz)		11	Joyce Ellington Branch
3	Alviso Branch		12	Pearl Avenue Branch
4	Berryessa Branch		13	Rose Garden Branch
5	Biblioteca Latinoamericana Branch		14	Santa Teresa Branch
6	Cambrian Branch		15	Tully Community Branch
7	East San José Carnegie Branch		16	Vineland Branch
8	Edenvale Branch		17	West Valley Branch
9	Evergreen Branch		18	Willow Glen Branch
Currently Non-Operational Branches				
	Bascom Branch			Calabazas Branch
	Educational Park Branch			Seventrees Branch

2. Budget Impacts Past, Present and Future

a. Budget Cuts to Date

The City's financial difficulties have had a devastating impact on the economic resources of the City and its residents. The SJPL has been hit particularly hard. The following are some of the most detrimental library service reductions that have occurred in the last decade:

- Staff: Since 2007-2008, library staff has been reduced by 26% (currently at 271 FTE, down from approximately 366 FTE).
- Branch Locations: As noted above, in addition to the King Library, the SJPL has 22 branch locations. However, presently, only 18 of those locations are currently operational. The remaining four branch locations – which were recently built with bond funds – are sitting closed due to the lack of funds to render them operational.
- Library Hours: Branch Library hours and days of service have been reduced from 47-51 hours per week in 2007-2008 (six to seven days per week) to 33-34 hours per week (four days per week). Reductions have also been imposed in the hours of operation and library services at the King Library, including the Children's Room hours, the California Room hours, and Access Services and Periodicals support.
- Library Programming: There have also been significant reductions to services provided at branch libraries (story-time, children's educational programs, homework assistance to students, literacy programs, adult programming, Summer Reading Celebration, and school class visits) and elimination of the Library Homework Center program. Branches provide materials for curriculum support for K-12 (250,000 print items, many online databases, and Internet research materials) that would not be available if branches closed.
- Other Impacts: Elimination of reserves on DVDs and CDs, reductions in King Library service desk hours over the past two years, and elimination of the bookmobile, disability outreach, and the Library Outreach Services Unit over the past several years.

While the SJPL has worked hard to absorb these budget impacts and to continue providing library services to the residents of San José, the anticipated budget cuts will result in further reductions and eliminations, rendering continued City-wide library services next to impossible.

b. Current Funding Levels/Projected Budget Cuts

The current amount of General Fund dollars appropriated for the SJPL services is $22,642,000. With a projected loss of $13,585,000 under the budget balancing outlined in Section II of this report, that amount could be lowered to $9,057,000 by next year. As the following chart shows, at that level of

funding SJPL would have to devote all of its General Fund appropriation to keeping the King Library open and operational. [83]

General Fund (GF) Positions at King Library (61.26 FTE)	$	5,713,000
King Library Operating Costs:	$	2,531,000
Reduced Fine Revenue:	$	1,000,000
GF Cost to Maintain Closed Branches ($25,900 x 22):	$	570,000
Potential 2012-2013 General Fund Expenses	**$**	**9,814,000**

In addition to support from the City's General Fund, SJPL operations are currently funded by a ten-year Library Parcel Tax, authorized when voters passed Measure S in 2004. The Library Parcel Tax generates nearly $7.2 million in revenue and interest annually, which currently funds 43.8 full-time equivalent employees, the purchase approximately 131,000 new library materials, and some system-wide automation and technology projects.

Funding Source	FTE in 2011-2012	FTE in 2012-2013 (Projected)	Note
General Fund	225.21	61.26	A reduction of 162.65 Full Time Equivalent Positions (FTE)
Library Parcel Tax Fund	41.50	43.80	May not be renewed beyond 2014-2015
Community Development Block Grant (CDBG)/Capital Funds	4.65	N/A	May not be renewed as part of the CDBG Budget Process
Total	**271.36**	**105.06**	

Assuming that parcel tax revenue is used entirely to fund branch library operations at four days per week, the SJPL will be able to keep 6 to 8 branch libraries open three to four days per week (along with the King Library) until 2015. However, the parcel tax sunsets at the end of fiscal year 2014-2015 and would require a two-thirds vote to continue. Renewal is unlikely if the majority of San José residents no longer have branch libraries operating in their neighborhoods, especially since the original measure passed with only 700 votes to spare.

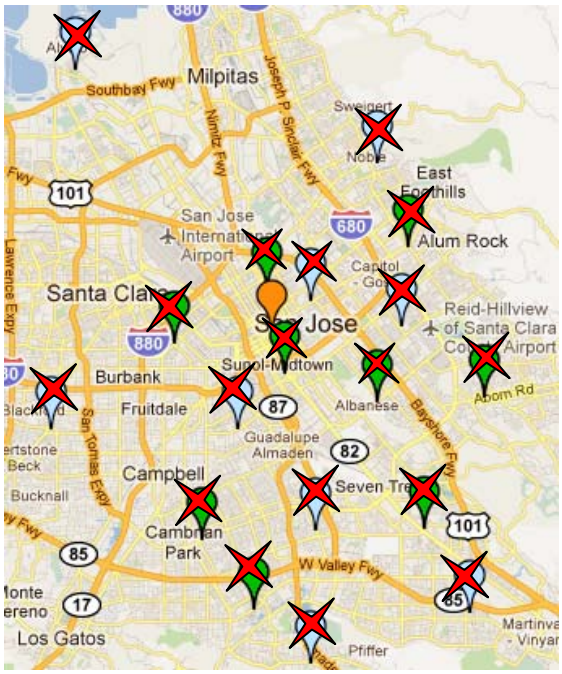
[83] The Operating Agreement between CSJ and the CSU Board of Trustees regarding the King Library, supplemented by specific cost-sharing agreements, includes a formula for sharing the costs of facility maintenance and utilities as well as the number of hours open per week, subject to change only by mutual agreement.

Thus, after 2014-2015, it is very likely that SJPL will only be able to operate the King Library and will be forced to close all remaining branch libraries.

3. Consequences of Proposed Budget Cuts

a. Branch Library Closures

If the parcel tax sunsets in 2015, all branch locations will close.[84] Branch closings following the proposed budget reduction are reflected below. Consolidating all library resources into one location effectively decimates library usage in the areas beyond downtown. As noted in the chart below, the mileages from the other locations to the King Library would be prohibitive for most residents, especially for school children who rely on the resources provided at their local branches to complete school assignments.



Distance in Miles to King Library	
Almaden Branch	10.5
Santa Teresa Branch	10.5
Calabazas Branch (CLOSED)	9.9
Vineland Branch	9.0
Alum Rock Branch	8.6
Cambrian Branch	8.1
West Valley Branch	7.8
Berryessa Branch	7.5
Evergreen Branch	7.1
Edenvale Branch	6.6
Pearl Avenue Branch	6.4
Seventrees Branch (CLOSED)	5.6
Alviso Branch	5.3
Tully Community Branch	5.3
Hillview Branch	4.8
Educational Park Branch (CLOSED)	3.6
Willow Glen Branch	3.5
Rose Garden Branch	2.8
East San José Carnegie Branch	1.3
Joyce Ellington Branch	1.3
Biblioteca Latinoamericana Branch	1.2

According to the latest census information, the City of San José has 75,515 children under five years old, 169,610 school-aged children, and 94,864 senior citizens that would no longer have service unless they could travel to King Library; yet the King Library resources would not be sufficient to meet the needs of nearly 1 million people. King Library has 350 computers (compared to 690 branch

[84] In our branch libraries, we have invested over $30,000,000 in computers, library materials, furniture, fixtures and equipment. If all branches are closed, these investments would lose nearly $5,000,000 per year in depreciation – a significant loss of value in resources that are not being utilized and which could not be properly recouped by selling these assets.

computers); 13,000 picture books (compared to 166,000 picture books at branches); 1,000 résumé books (compared to 8,000 résumé books at branches); and 21,000 curriculum-related materials (compared to branches with 250,000 curriculum support materials). King Library is also shared with San José State University and will continue to be heavily used by SJSU students and faculty.

Most library usage occurs at branch locations. Each year roughly 13 million items are checked out or renewed through the SJPL, with 80% of those transactions occurring at branches, not at King Library. Moreover, even if we assume that the residents of San José could all make their way to the King Library, the King Library does not have the capacity to serve those individuals or to house the resources necessary to accommodate that number of residents. Because of the King Library's unique relationship with San José State University (a school with 30,000 students) during peak times of the school year, the King Library will have 10,000-12,000 patrons visiting the library during the course of a single day. King Library has seating for 3,300 people. There is simply not enough capacity to accommodate a large increase in resident use during these times.

In 2010-2011 there were 4,345,389 branch library visitors checking out 11,975,557 materials and reserving computers and study rooms 1,162,345 and 16,571 times, respectively. With parcel tax funding, only a handful of branches will remain open. The rest of these visitors will not have a place to go for library resources. Unless the voters renew the parcel tax, all of these visitors will be without libraries in 2015.

b. Alternatives to SJPL Are Insufficient/Not Feasible

Facing the devastating impacts of the potential budget cuts, the SJPL has looked into alternatives for providing library services to the public. However, the feasibility of these options – let alone the impact they would have on providing library services to the residents of San José – is presently unknown.

(i) Use by San José Residents of other Public Libraries in Santa Clara County

For example, when the SJPL began reducing branch hours, many residents began using the Santa Clara County Libraries as their primary library rather than as a supplement to their local branch under the universal borrowing rules. However, with increased reductions in library staff and hours, San José residents began to overuse the universal borrowing system. Accordingly, the Santa Clara County Library began charging non-residents $80 annually for a County library card. With a significant reduction of service, it is likely that other local libraries would do the same.

(ii) Creation of a Regional Library System or Joining the Santa Clara County Library District

The difficulty that San José would have in being a part of a regional library system is that these entities would be likely unwilling to partner with San José. This is in large part because the huge differences in annual operating funds per capita would be difficult for another entity to absorb. They would expect San José to bring adequate funding. The Santa Clara County Library District, for example, operates at nearly $80 per capita while the City of San José is currently operating at around $34 per capita. Other municipal libraries in the County range from $50 to $99 per capita in annual operating funds.

(iii) Support from Library "Friends" Groups is Helpful, but Insufficient

Through fundraising via donations, book sales, etc. the library "Friends" groups and the San José Public Library Foundation provide additional funding for library programs and materials in the range of $500,000 to $850,000 annually. Without branch libraries in the community, it would be very difficult for this level of support to continue, much less expand.

4. SJPL's Economic and Social Benefits That Will Be Lost

Recent studies show a strong link between public libraries and a community's economic health. As one study notes, "[a]n increasing number of economic research tools are now being used to explore the public value of libraries, including the cost-benefit impacts and return on investment that public libraries generate. These studies consistently identify positive economic impacts made by libraries[.]"[85] Other studies have similarly affirmed the long-term community and quality of life impacts that libraries bring to a community.[86]

Libraries are especially important in a city as diverse as San José, where the SJPL provides many services and benefits, both direct and indirect, to a wide range of residents. For example, in addition to the specific services outlined below, librarians often provide important information regarding many non-library issues such as voter registration forms and election information, social services information, and tax forms and information. Loss of the branch libraries and SJPL programs would have a drastic impact on the economic and social well-being of the San José community.

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[85] Urban Libraries Council, "Making Cities Stronger: Public Library Contributions to Local Economic Development" (January 2007).

[86] See Fels Research & Consulting (University of Pennsylvania, Fels Institute of Government), "The Economic Value of The Free Library in Philadelphia" (October 2010); Fight Crime: Invest in Kids (California), "High-Quality Education: Cutting Crime and Saving Up to $300 Million a Year in Bay Area" (Sept. 2010).

Libraries located in neighborhoods of varying economic and educational characteristics, with library materials, computers and professional librarians and other staff to assist users, provide every resident with an equal opportunity to participate fully in a democratic society and to learn about matters of importance to them.

a. SJPL and Schools

Because of the unique relationship between the SJPL and San José State University, it is easy to see the importance King Library has on the education of the University's students. But what is less obvious is the impact the SJPL services have on students throughout the San José community. Nineteen school districts serve children who live in San José and most schools – especially elementary and middle schools – do not have libraries staffed by a teacher-librarian. The SJPL's 18 branch locations fill that void; the SJPL staff has worked hard to ensure that – despite recent cutbacks – these branches are open when students need them the most.

The SJPL libraries also offer a host of educational and instructional programs for children and youth. For example, the SJPL has incorporated early literacy (pre-reading) skills into regular "story time" programs for attending preschoolers and their respective caregivers. Summer Reading programs have traditionally been one of the SJPL's most popular programs, with over 100,000 participants over the last four years (the program runs for six to eight weeks during the summer).[87]

Studies also show a correlation between the amount of words a child is exposed to and their success at language and information acquisition. Students entering kindergarten following participation in the Smart Start San José programs have a better foundation for academic and social success due to participation in those programs. With the elimination of staff development and training for parents and child care providers through Smart Start, Books for Little Hands, and other childcare related programs, we can assume that these numbers will drop off. [88]

b. SJPL and Public Safety

SJPL services help to make San José a safer city both now and in the future. In addition to providing access to materials and information, the SJPL libraries also provide youth with a safe place to go after school. Library branches currently serve nearly 700 youths each afternoon, most of whom are not accompanied by a parent or caregiver.

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[87] Participants in these programs engage in a fun and developmentally appropriate activity that more than 90 percent of caregivers report causes them to read more often to their child. Of those that used the Summer Reading programs, 94 percent of parents, caregivers, educators, and students surveyed agreed or strongly agreed that participation in library programs contribute to improved school performance.

[88] One national study concluded that "public libraries contribute to long-term economic productivity primarily through literacy programs." Urban Libraries Council (2007).

The educational programs offered by libraries also help to reduce crime down the road. The High/Scope Foundation released the most recent findings of lifetime effects of participation in the Perry Preschool Program in Ypsilanti, Michigan (a model of early childhood education programs).[89] By age 27, those randomly assigned at-risk, low-income three and four year-olds who did not attend the program as children were *five times* more likely to become chronic offenders with five or more arrests compared to those who did attend. By age 40, those who did not attend the program were more than twice as likely to become career offenders with more than 10 arrests and twice as likely to be arrested for violent crimes.

c. Community Gathering Spaces

Community rooms at the SJPL branches are a valued resource. The branches were built intentionally so the "zone" of the library that includes the community room could be used separately from the rest of the building and could be used when the library branches are closed. There are a wide variety of users, from community associations, neighborhood groups, to information providers (usually sponsored and arranged by the Library). Some examples:

- The City often uses the facilities for "meetings in the neighborhood" to gather input and share information (e.g., five branches were used to host Community Budget Meetings for this last budget year);
- Some City Council members hold regular hours to meet with constituents;
- Neighborhood associations meet to discuss projects, issues, and to inform constituents;
- Library programs are held to inform, educate and entertain patrons (e.g., Health organizations and non-profits hold events co-sponsored by the Library to share their expertise and information with the public);

d. Adult Literacy Programs and English as a Second Language Collection

The SJPL also runs literacy programs for adults and families.[90] Of the 26,171 participants in SJPL's Family Learning Centers, 93% reported improvement in their reading, writing or speech skills. In a recent study of the Philadelphia Free Library – which is structured similarly to the SJPL – 10% of survey respondents reported "I couldn't have learned to read without the library," meaning an

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[89] Lawrence J. Schweinhart, Jeanne Montie, Zongping Xiang, William S. Barnett, Clive R. Belfield, and Milagros Nores. *Lifetime Effects: The High/Scope Perry Preschool study through age 40*. Ypsilanti: High/Scope Press, 2005.

[90] Approximately 16% of American adults function at the lowest level of literacy. In San José, that means over 153,000 adults lack the basic skills to read the directions on a medicine bottle, find an intersection on a map, or fill out a job application.

estimated 10,788 people attribute their ability to read to the Philadelphia Free Library.[91] Moreover, that study found an economic benefit of adult literacy programs totaling $21.8 million for 2009-2010.[92]

Language collections have been the pride of the SJPL, and making them available in the neighborhoods where the patrons live goes a long way toward making them accessible and visible. Branches house about 150,000 books in the major languages (circulating 2 million times per year), while King Library has about 70,000. Similarly, the materials many non-English speakers use to learn and practice their English are almost exclusively at the branches. There isn't room to house the materials at King Library, and it isn't clear that customers would or could travel to access them.

Many San José residents are working to gain U.S. citizenship. SJPL provides study materials to them and also partners with volunteers and organizations such as SIREN (Service, Immigrants, Rights and Education Network) to provide citizenship classes and practice exams.

e. Libraries and Home Values

A recent study of the Philadelphia Free Library system examined the economic impact that libraries have on home values.[93] The study concluded that homes within a quarter mile of a library were worth, on average, $9,630 more than homes outside that vicinity.

In reaching this conclusion, researchers looked at a regression of home sale prices over a ten-year period. The regression removed from the analysis other amenities that may account for the higher values, such as proximity to city hall (being close to downtown typically adds value to homes), parks, and retail shops. All in all, researchers found that being within a quarter mile of a library is associated with having a property value approximately 7.7% higher than comparable homes at greater distances.[94] Notably, the study concluded that libraries were responsible for $698 million in home values and generated an additional $18.5 million in property taxes for the city.

As the Philadelphia study shows, there is a strong correlation between libraries and home values. Being within easy, regular walking distance to a library adds significant value to a home. Consistent with these results, the loss of the SJPL branch libraries under the City's projected budget cuts may have a significant negative impact on home values in the San José community.

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[91] Fels Research and Consulting (October 2010).

[92] *Id.*

[93] *Id.*

[94] *Id.*

f. Job/Career Training and Other Educational Resources

In the last several years of severe economic downturn, job seekers have turned to the SJPL branches in very visible numbers to utilize library resources. Each year, the SJPL provides computer access to residents at a rate of two million computer sessions per year. Many of these sessions are for unemployed members of the community looking for work.

The State Unemployment Insurance Offices send many people to the library to fill out their unemployment insurance claim forms. The computer instruction services offered at the SJPL branches are one of the most valuable tools for this purpose. Many of our visitors report using job search sites, and ask for help with resumes, filling out online applications, and locating job postings. We estimate that 20% of adults using the SJPL computers are using them for job and career resources. Programming has focused on training in these areas to provide individual support and guidance.

Philadelphia researchers estimated that 979 Philadelphians found jobs directly as a result of the resources provided by the Library in 2009-2010.[95] Those entry-level jobs translate into $30.4 million in earned income in one year (at an average entry-level salary for Philadelphia), generating $1.2 million annually in wage tax revenue. Under the scenario described in Section II of this report, the majority of SJPL branch libraries will be shuttered next year, in addition to the four branches that were recently constructed following bond measures but are not operational. If the library parcel tax is not extended by 2015, all of the SJPL's branch libraries will close, with only the King Library remaining open. Many of SJPL's essential community services are provided through its branch libraries and the King Library simply cannot fill this void. The impacts of library closures will be felt throughout the San José community both immediately and well into the future.

[95] *Id.*

D. IMPACTS ON PARKS, RECREATION AND NEIGHBORHOOD SERVICES

1. Overview of Parks, Recreation and Neighborhood Services

The Department of Parks, Recreation and Neighborhood Services (PRNS) oversees the City's various parks, recreational programs, and neighborhood services. PRNS has one of the most diverse service models of any agency of its type, servicing not just San José's residents but individuals from surrounding cities and communities as well.

City-owned inventory overseen by PRNS

- Nearly 3,500 acres of Parkland
- 9 Regional Parks
- 3 Golf Courses
- 180 Neighborhood Parks
- 6 Skate Parks
- 1 Roller Hockey Rink
- 1 BMX Park
- 57 Basketball Courts
- 9 Dog Parks
- 54 Community Centers
- Over 53 miles of urban trails
- 20 Community Gardens
- 6 Pools
- 1Wilderness/Family Camp
- 1 Zoo & Amusement Park
- 250 Playgrounds
- 75 Tennis Courts at 22 locations

Residents of San José are active users of their Parks and Recreation system. Based on a resident survey, approximately 85% of households in San José had visited a park or outdoor recreational area within the City in the prior 12 months.[96] Moreover, 38% of households were classified as "frequent users," meaning that they visited PRNS parks or facilities at least once a week. Further, approximately 70% of households in San José reported having used one of the City's trails or walkways in the prior 12 months, typically for exercise. Finally, 40% of the households in San José participated in indoor recreational activities (e.g., exercising in a gym or playing indoor basketball) in the prior 12 months.

b. Parks

PRNS provides a wide variety of parks landscaping services throughout the City's 180 neighborhood parks, nine regional parks, and 39 civic ground sites. As a whole, PRNS maintains an estimated 3,436 acres of parkland citywide (2,002 developed and 1,434 undeveloped), providing services such

[96] 2009 Greenprint Update.

as turf, landscape, equipment, custodial maintenance, and playground safety checks that keep the City's parks clean, green, and safe for the community. In addition, PRNS oversees the City's park ranger services.

Realizing the positive effect of outdoor space on the community and the rapidly rising cost of land, PRNS devised the City of San José Greenprint – a comprehensive master plan for interweaving parks into the future growth of the City. It incorporates parks into all parts of the City ensuring equal access to green space for all San José residents.

The Park Ranger Program has been an important part of maintaining the safety and security of the parks for the enjoyment of the San José's residents. Park Rangers provide a variety of services: they provide emergency medical care, prevent and suppress wild fires and search for lost children. Park Rangers educate the public on nature, provide park maintenance services, and protect the natural resources and wildlife found in San José's parks. Rangers also serve as public safety officers in the parks, suppressing gang-activity, graffiti and vandalism. Park Rangers have contributed to decreasing response times for San José's Police and Fire Departments, a critical service for the City.

c. Recreational Programs

PRNS also oversees a variety of recreational programs at 54 Community Centers designed to stimulate children, engage youth, provide exercise for adults, and keep our seniors physically and socially active. PRNS offers hundreds of classes and activities each year on a variety of subjects crafted to appeal to San José's diverse community. The curriculum offers everything from pre-school cooking classes to ballroom dancing for seniors. Community Centers provide a fundamental safety net for youth, seniors, adults and person with disabilities. PRNS recreation programs provide affordable programs for all residents of San José. If City recreation services are eliminated, as anticipated by the prospective budget cuts set out in Section II of this report, there would be very few, if any, affordable programs to refer to participants. In 2009-2010, Community Center programs had an estimated total of 2 million attendees. In 2010-2011, Community Center programs generated $5.6 million in revenues for the City.

Community Center Reuse Program: In November of 2000, the voters of San José approved a $228 million General Obligation Bond issuance known as "Measure P" to acquire property and construct improvements for parks, trails and recreation facilities in San José. Consequently, the San José City Council approved a Community Center Reuse Plan that allows PRNS to vacate older, less-used community center facilities and centralize services, programs and staff at the newer, larger and more efficient centers, most of which were built and/or renovated with Measure P funds, while maintaining community service priorities in vacated facilities. This Community Center Reuse Policy allows Santa Clara County-based nonprofit, neighborhood associations, school districts, and other government agencies or community service providers to use PRNS recreation facilities designated as Community Center Reuse sites at no cost in exchange for services that primarily benefit San José

residents. Currently, 43 of the City's 54 community centers are part of the Reuse program, most of which are receiving free utilities and maintenance costs in addition to free lease of the facilities.

***Children and Youth*:** The PRNS summer camp program offered over 500 day camps, enrolling more than 7,000 participants in 2010. PRNS also provides after-school programming through a partnership with the schools. Teen Centers, administered by PRNS at Community Centers, provide a safe place for youth to engage in structured recreation programs that teach leadership and promote good decision-making and constructive use of time through sports, creative arts and other organized activities.

***Seniors*:** The Senior Program provides daily nutritious meals to seniors and free or reduced cost recreation opportunities. With funding from the County, the City's Senior Nutrition program feeds 1,000 people daily at 13 sites throughout San José, totaling over 238,000 meals annually.[97]

***Adults*:** PRNS provides a multitude of Health and Wellness Programs for adults at Community Centers. Many participants would not have the opportunity to utilize higher cost fitness centers or exercise programs, thus eliminating access to these kinds of programs for many adults.

***Therapeutic Programs*:** The PRNS Therapeutics Program offers recreation programs and services for youth and adults with physical, mental or developmental disabilities. Persons who utilize these programs would be left with few, if any, alternative options for recreation programs. Included in this programming is the Grace Community Center. Grace is a therapeutic recreation center serving the social, recreational, and therapeutic needs of adults with mental illness. Staffed by mental health professionals, Grace is the only center providing medically-based social recreation programs to serve these needs in Santa Clara County. All of Grace Community Center's programs are designed specifically for adults with mental disabilities, primarily adults with symptoms of mental illness.

d. Neighborhood Services

PRNS added "Neighborhood Services" to its name in 1993, creating programs to combine the positive influences of recreational and community services with the neighborhood revitalization effects of code enforcement, graffiti abatement and community development block grants. Since the 1990s, PRNS has been involved in a variety of programs including the Special Olympics and has received numerous awards for its anti-graffiti and anti-litter campaigns.

Included within the Neighborhood Services Division are the Mayor's Gang Prevention Task Force (MGPTF) and Youth Intervention programs. The MGPTF is made up of a Policy Team and a Technical Team. The Policy Team, chaired by the Mayor, provides direction and focus to the City's

[97] In a survey of County-funded nutrition sites, 70% of seniors reported that lunch served during the nutrition programs was their primary meal of the day. The Nutrition Program also serves the dual purpose of providing seniors the opportunity to socialize, which reduces depression and isolation seniors feel in home-bound settings.

gang prevention and intervention efforts. The task force is comprised of the city, county and state; community based organizations; the San José Police Department; faith community; schools; and other community stakeholders. By bringing together these partners, the Task Force has been able to leverage a variety of available "pro-social" community resources to combat the anti-social influences that youth receive from gangs. These programs work to eliminate the involvement of youth ages 6-24 in gangs, to reduce crime, and to make neighborhoods safer. The Safe School Campus Initiative – a crisis response and communication protocol team covering 72 middle and high school campuses – provided services to administrators and over 100,000 students in 2010. In 2010, the Mayor's Gang Prevention Task Force served more than 5,500 youth. The 2010-2011 BEST Evaluation Report surveyed 1,293 program participants who reported the following outcomes as a result of participation in the MGPTF BEST program:[98]

- 81% Improvement in school from no attendance to enrollment this year
- 66% Improvement in arrest rate from arrested before services to no arrests during services
- 81% Of youth indicated they are not using drugs
- 71% Of youth indicated their ability to stay safe is better.

Through the Parks Volunteer Management Unit, PRNS coordinated the efforts of over 20,000 volunteers to beautify the parks. Moreover, volunteers picked up over 36,000 pounds of garbage in 2010. Under the City's graffiti abatement program, volunteers and staff cleaned and painted over 1.5 million square feet of graffiti in 2010.

2. Budget Impacts – Past, Present and Future

a. Budget Cuts to Date

PRNS has been hit particularly hard by the recent decline in the City's finances. The following are some of the more detrimental service reductions/cutbacks that have taken place in recent years:

2008-2009
• Elimination of Summer Work Experience Program
• One time funding shift for San José After School (SJAS) Level 2 programming and elimination of Level 1 programming for various sites
• Elimination of Community Based Organizations funding for youth employment and elimination of City staff support for San José All-Stars

[98] City of San José BEST Evaluation Report and Summary of Mayor's Gang Prevention Task Force 2010-2011. http://www.sanjoseca.gov/prns/mgptf/best.asp

2009-2010
• Closure of regional parks on Mondays
• Staffing reductions at Grace Community Center
• Further administrative reductions in San José After School Program
• Elimination of telephone helpline and walk-in counseling/referral service for seniors
• Elimination of grant funding for San Juan Bautista Child Development Center
• Elimination of one PRNS Division which oversaw revenue generation, aquatics, sports, marketing, communications, events and Family Camp, including the associated Deputy Director position, with remaining PRNS divisions absorbing the work from that division

2010-2011
• 50% staffing reduction for Striving Toward Achievement with New Direction (STAND) Program, a citywide program that provides gang intervention programs for youth, ages 13 to 18, who are marginally involved in gangs or have the potential to become involved in gangs
• Suspension of San José Family Camp for Summer 2010
• Reduction in Park Ranger Program at Overfelt, Emma Prusch and trails (saved for one year)
• Reduction in Aquatics Program – City operations for two pools, outside operators for remaining (except Almaden Lake)
• Reduction of Community Centers (CC) operated by PRNS to 10 Hubs and 1 Satellite Center, effective July 2011, with remainder being placed on reuse
• Reduction in afterschool programming and senior nutrition services
• 15% reduction in Civic Grounds maintenance
• Elimination of Lake Cunningham Marina budget (saved for one year)
• Elimination of Citywide Sports League programming

2011-2012
• Further reduction in Park Ranger Program and elimination of all fixed post staffing
• Staffing reduction for Grace Community Center
• Reduction in Youth Intervention services
• Reduction in Multi-Service "Hub" Community Center staffing and hours
• Outsourcing of park restroom, small park maintenance and Graffiti Abatement services
• Elimination funding for Children's Carousel
• Elimination of funding for Edenvale Community Center and shift to reuse

As the foregoing demonstrates, these cutbacks have reduced most of PRNS's major services, while a number of services have been completely eliminated. PRNS is already operating on a shoestring budget.

b. Current Funding Levels/Projected Budget Cuts

PRNS's General Fund 2011-2012 Adopted Budget is $45,560,206 (a 21.1% drop from fiscal year 2010-2011 adopted General Fund budget). Across all funds, PRNS is staffed at 459.65 positions, (a

35% drop from 2009-2010 adopted budget, when PRNS was staffed with 707.61 FTE). It is projected that the City may need to cut another $11.4 million from the PRNS General Fund Budget for 2012-2013, with an additional $2.275 million in cuts for each of the following two consecutive years. These projected cuts would have a devastating impact on PRNS's ability to provide essential services to the community. From a staffing perspective, PRNS projects that an additional 40% reduction will result from the projected cuts. This would mean only 276 FTE for all of PRNS in July of 2015.

Critically, many of these budgetary and staffing reductions have occurred while park acreage and Community Centers were increased (as a result of bond measures). Following the passage of bond measures, one community center was recently constructed for the City but has remained closed due to lack of funding to operate the facility. Further, while capital funding for new parks is available, a hold on new park construction is in place due to a lack of funding for the operating and maintenance expenses those new facilities would create. This has resulted in some San José residents living near vacant lots planned for park development.

3. Consequences of Proposed Budget Cuts

Under the proposed budget cuts, the following services would most likely have to be severely reduced or eliminated completely:

- Recreational Services: The City would have to discontinue all City recreational programs, with possible closure of all 54 Community Centers, including removing non-profit partners from existing reuse facilities, unless partners could pay for facility overhead.

- Senior and Therapeutic Services: The City would also have to severely reduce or discontinue senior services, including its Senior Nutrition Program, which provides approximately 1,000 hot meals each day. In addition, the City would have to close the Grace Community Center, which serves as the primary location for the City's Therapeutic Services, providing programs designed specifically for adults with mental, physical and developmental disabilities. This center presently serves approximately 80-90 clients per day.

- Park Ranger Program: The City would have to eliminate park ranger services. Rangers currently supervise most on-site fee collection and revenue processing at regional parks. They also provide special event coordination support, public safety and fire suppression services, and traffic and crowd control at regional parks during high season activities.

- Park Maintenance Services: The City would have to outsource all park neighborhood maintenance services. This may raise some challenges in the larger parks, as the staff development of extensive relationships with the local community, park volunteers and sports field users is a critical component of the current service delivery, which require more sustained services than contractors often provide.

In addition to eliminating these programs, the City would have to impose additional cuts to its MGPTF/Youth Intervention Programs and reduce support to the Santa Clara County Children's

Health Initiative. The impacts of the reduction or elimination of the Gang-Intervention programs would be compounded by the closure of the Teen Programs at Community Centers.

The public does not support such cutbacks in PRNS services. The City of San José's 2011 Budget Priorities Survey Report of Finding indicates while some reductions in recreational program and neighborhood services may be acceptable, closing all Community Centers, closing restrooms in parks and reducing gang and youth intervention programs is unacceptable to the majority of the San José community.[99] Also, in a recent survey, 85% of residents felt that "maintaining the City's parks and recreation facilities" was either "extremely important" or important to them personally, while 79% felt that "providing adequate funding for parks and recreation opportunities throughout the City" was "important."[100]

4. PRNS Economic and Social Benefits That Will Be Lost

PRNS provides services that help maintain our physical health, strengthen our communities, and make San José and our individual neighborhoods more attractive places to live and work. A further reduction in these services would have dramatic repercussions on the economic and social benefits that San José residents currently enjoy.

a. Impact of Recreation/Neighborhood Services

A recent academic study examined all existing evidence-based research on the economic and social impacts of recreational services on youths and adolescents.[101] The report identified a number of positive impacts that recreational services have on a given community, including crime reduction, improving academic performance, and preventing childhood obesity.

(i) Crime Reduction

According to the study, children ages 12 to 17 who are left unsupervised three or more days per week are twice as likely to hang out with gang members, three times as likely to be engaged in criminal behavior, and more than three times as likely to use illegal drugs.[102] Moreover, children who are unengaged, bored, or uninvolved have a higher risk of undertaking negative behaviors such as delinquency.

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[99] http://www.sanjoseca.gov/mayor/goals.budget.BudgetSurvey.asp

[100] http://www.sjparks.org/greenprint/gp2009/docs/Appenix%20A%20-%Community%20Assessemt.pdf

[101] Peter A. Witt & Linda L. Caldwell, "The Rationale for Recreation Services for Youth: An Evidenced Based Approach," National Recreation and Parks Association, Research Series (2010) ("Witt & Caldwell (2010)"). http://nrpa.org/uploadedFiles/Explore_Parks_and_Recreation/Research/Witt-Caldwell-Research%20Paper-Final-lores.pdf

[102] *Id.*

The availability of recreational programs helps address these issues. Studies have found that community violence occurs less frequently among youth who live in neighborhoods that offer a variety of recreational-based afterschool programs.[103] These programs – which involve not only the youth participants, but also parents, volunteers, and program employees – generate both a greater sense of trust and solidarity in a community as well as promote a willingness of residents to intervene in potentially violent or harmful situations for the sake of public order. In other words, the very existence of recreational programs, such as ones organized by PRNS, may help keep crime levels down.

There are economic benefits to these programs as well. A 2007 study found that students who participated in a recreational afterschool program based in Los Angeles had significantly lower incidences of juvenile crime.[104] That study reported that every dollar invested in the program resulted in an estimated savings in juvenile crime costs of approximately $2.50. Youth violence costs the United States more than $158 billion each year.[105]

San José has experienced directly the positive impact that Community Centers can have on crime reduction. PRNS tracked the impact of the opening of three Community Centers in the Roosevelt, Seven Trees and Mayfair neighborhoods. That tracking showed marked declines in certain criminal activities in those neighborhoods following the opening of those centers. Decreases were noted in the number of reports or arrests for vandalism, auto theft and disorderly conduct.[106]

(ii) Improving Academic Performance for Youth

In addition to helping reduce crime, participation in afterschool recreational programs has been linked to improving academic performance. Studies show that students who participate in afterschool recreational programs experience greater engagement in learning and have higher homework completion and quality.[107] Participation in these programs has also been linked to reductions in grade retention and dropout rates. When young people have access to quality recreational programs, they have increased opportunities to succeed academically and are better prepared to enter post-secondary school and the workplace, where they will contribute to the growth

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[103] Witt & Caldwell (2010) at pg. 39 (citing for example, Gardner, G., and Brooks-Gunn, J (2009) Adolescents' exposure to community violence: are neighborhood youth organizations protective? *Journal of Community Psychology, 37*(4), 505-525.)

[104] Witt & Caldwell (2010) at pgs. 36-37 (citing Goldschmidt, P., Huang, D., and Chinen, M, (2007) The long-term effects of after-school programming on educational adjustment and juvenile crime: A study of the LA's Best After-School Program. Los Angeles, CA: CRESST/University of California. Retrieved March 15, 2010, from http://www.uwex.edu/ces/4h/afterschool/partnerships/documents/ LASBEST_DOJ_Study_Brief.pdf.)

[105] *Id.* at pgs. 36-37.

[106] Annual Report (2010) at pg. 7 (based on crime analysis data compiled by Police Department).

[107] *Id.*

of the economy.[108] As noted in the MGPTF Strategic Workplan Update,[109] the following population results indicate that San José residents working together were successful in favorably impacting juvenile crime and school success outcomes. This conclusion is based on the fact that:

- The rate of violent crime per 100,000 population has decreased by 38% since 2000;
- There has been a 27% decrease in juvenile violent crime rate since 2000;
- The number of violent gang related crimes is down 20% from 2009 to 2010;
- There has been a 37% increase in the number of high school graduates that meet the University of California/California State University admissions requirements since 2001; and
- The Academic Performance Index for San José school districts has increased by 12% since 1999.

The high school graduation rate has improved as measured by the Cumulative Promotion Index by 19% since 1999.[110]

(iii) Health Benefits for Youth and Adults

Recreational programs promote an active and healthy lifestyle and reduce the risk of childhood obesity, which, in recent years, has become a serious problem in American society. Total health care costs attributable to obesity are projected to double every decade to approximately $861 to $960 billion by 2030, accounting for up to 18% of total U.S. health care costs.[111] Studies have found that children and adolescents who do not have access to afterschool recreational programs are more likely to be overweight, with increased risk of adult metabolic syndrome and obesity. Youth who engage in adequate amounts of physical active recreation are more likely to be at an appropriate weight and a reduced risk of later weight-related problems.[112]

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[108] Indeed, based on 2006 statistics, an individual with less than a high school education will have average earnings of less than $22,000 per year, while a high school graduate will earn $29,000 per year, someone with a bachelor's degree $43,500, and a person with at least a master's degree $50,000. Witt & Caldwell (2010) at pgs. 39-41.

[109] MGPTF Strategic Workplan Update (2011-2013) at pg. 10 (http://www.sanjoseca.gov/prns/mgptf/docs/MGPTFSWP-Draft%202711.pdf).

[110] *Id.*

[111] Witt & Caldwell (2010) at pgs. 39-40 (citing Wang, Y., Beydoun, M.A., et al. (2008) Will all Americans become overweight or obese? Estimating the progression and cost of the US obesity epidemic. Obesity, 16(10): 2323–2330.)

[112] Witt & Caldwell (2010) at pgs. 39-40 (citing Department of Parks and Recreation (2003) *Business leader's opinions of parks and recreation: A survey of California chambers of commerce–2002*. Sacramento, CA: California State Parks.)

The benefits of these activities are not only realized by youth. PRNS provides Health and Wellness services for residents of San José. Such services have now been recognized in academic studies to provide direct physical benefits for adults, by promoting physical activities.[113] This data clearly supports the cost effectiveness of efforts to reduce obesity, for adults and youth, through the availability of public recreational programs.

Given these findings, it is perhaps not surprising that in a recent Budget Priorities Survey of San José residents, only 35% of respondents indicated acceptability for closing nearly all Community Centers.[114]

b. Impact of Parks on Property Values and Economic Development

It goes without saying that the City's parks and green spaces significantly contribute to what makes San José a desirable place to live. A recent study by the Knight Foundation found that "aesthetics, particularly the parks, playgrounds and trails, is perceived as a community strength."[115] Residents in San José have given the City high marks for the availability of outdoor parks, playgrounds, and trails. Because aesthetics are a key driver of attachment to a community, reducing the investment in these areas will decrease residents' attachment and will ultimately influence locational decisions.

Studies have also examined the relationship between parks and property values. For example, researchers in Texas concluded that parks and open spaces have a positive impact on property values – noting that in some cases, having a park in the vicinity can increase property values by as much as 20%, significantly increasing sale prices, not to mention property tax revenues.[116] A West Virginia study determined that two park systems enhanced property values by approximately $280 million, which in turn generated approximately $980,000 annually in property tax revenues despite West Virginia's very low property tax rate. [117]

A study examining the importance the municipal parks in Denver, Colorado found that "Denver's parks deliver annual revenue of $7.1 million for the city, municipal savings of $3.6 million, resident

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[113] The Benefits of Physical Activity Provided by Parks and Recreation Services: The Scientific Evidence; (http://www.nrpa.org/uploadedFiles/Explore_Parks_and_Recreation/Research/Godbey-Mowen%20Paper-Final-Web.pdf)

[114] This 2011 survey was compared to the 2010 response to a similar question regarding the acceptability of closing *some* Community Centers, which was deemed acceptable by 46% of respondents.

[115] See Knight Foundation Soul of the Community Project, http://soulofthecommunity.org.

[116] Sarah Nicholls & John L. Crompton, "Impacts of Regional Parks on Property Values in Texas," Journal of Park and Recreation Administration, Vol. 23, No. 72 (Summer 2005).

[117] Mark L. Burton & Michael J. Hicks, "Tax Increment Financing Implications of Municipal Parks in West Virginia: Spatial and Semi-Parametric Estimates," Journal of Park and Recreation Administration, Vo. 25, No. 2 (Summer 2007).

savings of $517 million and a collective increase of resident wealth of $78.7 million."[118] A study of the economic benefits of municipal parks in Seattle reached similar conclusions finding that "Seattle's parks deliver annual municipal revenue of $19.2 million for the city, municipal savings of $12.4 million, resident savings of $511.6 million and a collective increase of resident wealth of $110.8 million."[119]

In addition, an article by the American Planning Association[120] provides five key points regarding how cities use parks for economic development:

1. Real property values are positively affected
2. Municipal revenues are increased
3. Affluent retirees are attracted and retained
4. Knowledge workers and talent are attracted to live and work
5. Homebuyers are attracted to purchase homes

As these studies indicate, parks and similar types of recreational facilities are not only aesthetically pleasing, but also significantly contribute to a community's economy.

The services provided by PRNS are vital to the present and future health of San José's community and economy. PRNS facilities and programs feed San José seniors, make San José a safer city, help San José youth succeed in school, and help San José residents stay healthy and active. All of these benefits reduce costs to the City in other areas. Moreover, San José's various outdoor resources increase the city's property tax base and are a major part of what makes San José an attractive place to live. Especially in the face of a financial crisis, the City cannot afford to lose the benefits provided by PRNS services.

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[118] http://www.tpl.org/publications/books-reports/ccpe-publications/denver-park-value-report.html

[119] http://www.tpl.org/publications/books-reports/ccpe-publications/seattle-park-value-report.html

[120] http://www.planning.org/cityparks/briefingpapers/pdf/communityrevitalization.pdf

APPENDIX B – FACTORS CONTRIBUTING TO THE STRUCTURAL DEFICIT

A. The Great Recession Has Taken a Toll on the San José Economy

San José, along with many other cities, has been heavily affected by the current economic downturn. The financial impact from the economic downturn has been severe, and continues to linger. However, as discussed below, the City's current crisis has been driven primarily by *increases* in employee-related costs, especially pension and retiree healthcare costs.

The City faces a structural budget gap: the growth in the cost of the City's recurring expenditures – most significantly, for employee retirement benefits – outpaces the growth in City revenues. This unsustainable imbalance preceded the decline in City revenues and will continue to imperil City services for years to come if no corrective action is taken. While the City has taken extraordinary steps to address and control these costs, shrinking its workforce, decreasing total compensation by 10% across the board, and increasing fees and other revenues; the City's ability to fund its remaining services continues to deteriorate dramatically and solutions are becoming more and more elusive. The budget pressures faced by the San José municipal government reflect the broader economic problems faced by San José's residents. By almost any measure, the Great Recession continues to have a devastating effect on San José's residents, and their economic resources:

- The unemployment rate for the San José metropolitan area was 9.6% as of September 2011, and has doubled since the onset of the recession. Since March 2009, the region has experienced double-digit unemployment in all but two months.[121]
- Median single family home sales prices have fallen sharply, and are 38% below peak 2007 annual levels as of September 2011.[122]
- As of September 2011,[123] San José foreclosure rates are nearly twice as high as the national average.

In turn, as further detailed in the analysis to follow, these economic factors have weakened the City's tax base and revenue streams, while adding to community service demands. As in communities around the nation, the downturn has created severe pressures on the City of San José budget.

While the recession that began nationally in December 2007 may have ended in June 2009, the economy has yet to generate the strong levels of growth required for full recovery. Moreover, even

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[121] Employment Development Department, Labor Market Information Division, San José-Sunnyvale-Santa Clara MSA, October 21, 2011.

[122] Santa Clara County Association of Realtors, September 2011 median home sales prices (single family) in San José of $481,500, down from $510,000 in September 2010 and $772,050 in June 2007..

[123] RealtyTrac reports 1 in 337 San José homes received a foreclosure filing in September 2011, in comparison to 1 in 605 nationally.

"normal growth" is insufficient to achieve true recovery from the recent recession.[124] Real recovery requires a return to trend – in other words, where the economy would have had normal growth continued without the contraction of a recession. Accordingly, economist Edward Leamer, Director of the well-regarded UCLA Anderson Forecast, has stated that true recovery would equate to "5-6% growth with payrolls growing at 250,000-300,000 per month and unemployment falling noticeably."[125] According to revised estimates published by the Bureau of Economic Analysis,[126] growth in real GDP has remained below 3% for the past five quarters.

Of further concern, recent projections show economic growth continuing below normal levels through calendar year 2012. In the September 2011 OMB Mid-Session Review, the 2011 Q4 forecast was reduced to 2.4% based on data through June. Using the most recent economic data available through August 2011, OMB has further reduced the forecast to just 1.6%, with growth expected to remain below 3.0% through 2012.[127] Similarly, relative to projections previously published in the second quarter of the calendar year, the more recent fourth quarter Survey of Professional Forecasters compiled by the Federal Reserve Bank of Philadelphia released in November 2011 reduced projected real GDP growth from 2.7% to 1.8% for the full calendar year 2011, and from 3.0% to 2.4% for calendar 2012.[128]

The forecasters also project prolonged weakness in the labor market, including continued high unemployment rates.[129] In the Fourth Quarter Survey of Professional Forecasters, unemployment nationally is projected to stand at an annual average rate of 9.0% in 2011 and to remain high at 8.8% in 2012, 8.4% in 2013, and 7.8% in 2014. In contrast, the national average in 2007, before the full onset of the recession, was just 4.6%. In its Mid-Session Review, OMB also revised its forecast for the national unemployment rate upward from 8.3% to 9.0% for 2011-2012, reflecting the impact of the continued turbulence in the US economy.[130]

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[124] "Normal" growth is defined as "3% GDP growth with payrolls growing at 150,000-200,000 per month and unemployment stuck at high levels." UCLA Anderson Forecast, 2011 Second Quarterly Report "U.S. Economy Growing But 'No Recovery in Sight'" (June 15, 2011).

[125] UCLA Anderson Forecast, 2011 Second Quarterly Report "U.S. Economy Growing But 'No Recovery in Sight'" (June 15, 2011).

[126] US Department of Commerce, Bureau of Economic Analysis, Gross Domestic Product Third Quarter 2011 (Advance Estimate), October 27, 2011.

[127] Executive Office of the President, US Office of Management and Budget, Mid-Session Review, Fiscal Year 2012, September 1, 2011.

[128] Survey of Professional Forecasters, Federal Reserve Bank of Philadelphia, Fourth Quarter, November 14, 2011.

[129] *Id.*

[130] Executive Office of the President, US Office of Management and Budget, Mid-Session Review, Fiscal Year 2012, September 1, 2011.

The California economy is also expected to remain sluggish. The September 2011 UCLA Anderson Forecast projects a continuing period of slow growth across the state with ongoing stress in the labor markets. Statewide, the forecast projects double-digit unemployment rates continuing through calendar 2013.[131]

Along with heightened overall economic uncertainty that may impact City revenues, planned federal budget reductions will likely also affect intergovernmental funding. As part of the Budget Control Act of 2011, Congress has agreed to cut spending by $2.4 trillion over the next decade, eliminating an estimated $917 billion in domestic discretionary spending. While specific reductions have not yet been determined, such cuts will likely reduce aid to state and local governments overall for transportation, education, and environmental programs.[132] In the shorter-term, President Obama's proposed American Jobs Act does include increased funding for public infrastructure and first responder hiring. As of November 2011, however, the President's proposals have not been adopted by Congress -- while the Budget Control Act of 2011 is current law.

B. San José Revenues Have Decreased, With Only Moderate Growth Forecast Going Forward

The City of San José's primary revenue streams are highly sensitive to the overall economy, and have been eroded by the economic downturn. The City's two largest revenue sources, property taxes and sales taxes alone comprise nearly half of overall General Fund revenues,[133] and have both experienced recession-driven declines. At the same time, multiple other significant City revenue streams, including business taxes and many of the City's licenses and permits, have also fallen.

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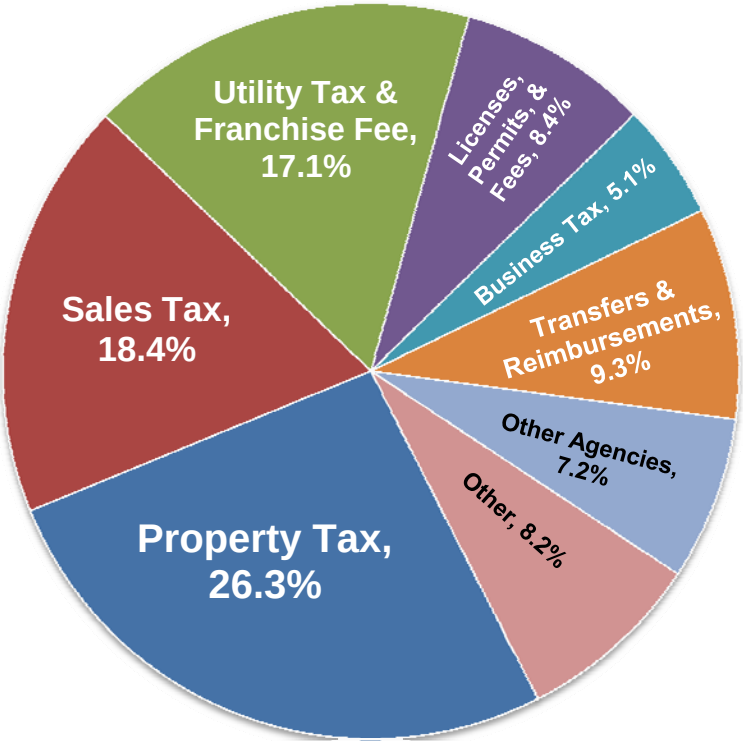
[131] September 2011 UCLA Anderson Forecast.

[132] A Growing Gloom for States and Cities, The New York Times, August 13, 2011.

[133] Excluding use of Fund Balance.

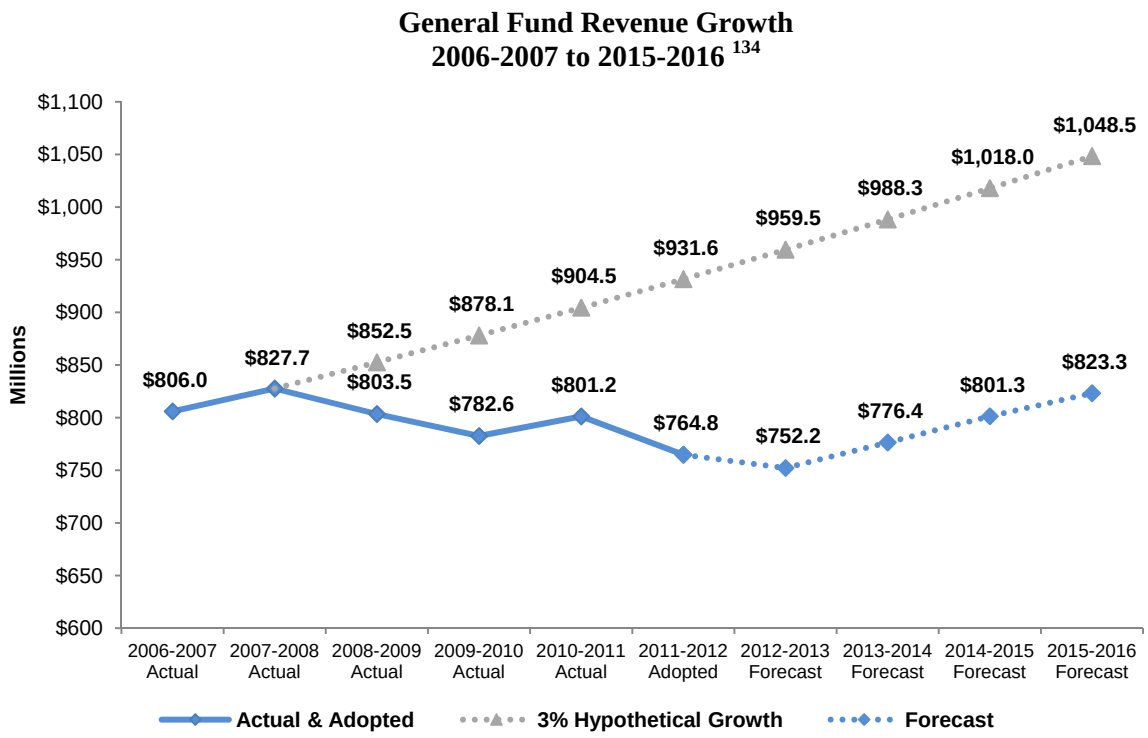
Fiscal Year 2011-2012 Adopted Budget
General Fund Revenues (Excluding Fund Balance)



Source: City of San José 2011-2012 Adopted Budget.

1. Overall Revenue Performance and Projections

Overall, the adopted 2011-2012 General Fund revenue estimates remain 7.6% lower than peak 2007-2008 General Fund revenues of $827.7 million. Based on the 2012-2013 Preliminary General Fund Forecast, which excludes one-time revenues and grants, and aggregate General Fund revenue growth rates in the 2012-2016 Forecast for 2013-2014 through 2015-2016, General Fund revenues are not expected to return to 2007-2008 levels until 2015-2016.



Sources: San José Adopted Budgets 2006-2007 through 2011-2012, Five Year Forecast (February 2011), 2012-2013 Preliminary General Fund Forecast (November 2011).

At no point during the forecast period are General Fund revenues projected to approach what they would have been had growth continued at 3% per year since 2007-2008. Adopted 2011-2012 General Fund revenues are $166.8 million lower than hypothetical General Fund revenues of $931.6 million, assuming General Fund revenues had grown at 3% per year from peak levels in 2007-2008.

2. Property Taxes

Property taxes account for more than a quarter (26.3%) of projected General Fund revenues in 2011-2012. In San José, as in communities across California and the nation, the collapse of the U.S. housing bubble in 2007-2008 led to sharp declines in home values and significant increases in the number of foreclosures. In turn, as these economic factors have worked their way through the property assessment and taxation process, property tax revenues have experienced decline – both nationally and in San José. Given continued housing market weakness and the legal constraints on property tax increases in place under the California constitution, property tax revenues will be dampened for years to come.

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[134] Note, the actual and adopted revenue figures include one-time revenues and grants; the 2012-2013 Forecast figure is based on the 2012-2013 Preliminary Forecast and is likely understated as it does not include one-time revenues and grants.

In addition to housing market factors, San José's ability to raise property tax revenue to keep pace with rising expenditures is severely constrained from a structural viewpoint by Proposition 13 and subsequent related amendments to the California constitution. Proposition 13 limited the ad valorem tax rates to 1% of a home's assessed value absent approval of two-thirds of the city's voters for a higher rate. The proposition also limited any increase in the assessed value of real property to the California Consumer Price Index up to a maximum of 2% per year, the result of which effectively locked in the total property taxes paid by many California residents to their 1978-1979 levels, adjusted by a maximum increase of 2% annually. Property that changes ownership or has major alterations may be assessed at current fair market value, and thereafter is limited to the 2% increase in assessed value per year.

As shown in the graph below, San José's property tax revenue collections peaked at approximately $215.7 million in 2008-2009 (figures include the Aircraft Property Tax), falling sharply for the next two, consecutive fiscal years to $197.2 million in 2010-2011. While the 2011-2012 Adopted Budget forecasts some recovery in this largest City revenue source, the projected $201.5 million would still be approximately 6.6% below the levels reached three years earlier. In the 2012-2013 Preliminary Forecast, property tax revenues are projected to experience continued slow growth and generate $205.7 million. If the growth rates assumed in the 2012-2016 Five-Year Forecast issued in February 2011 are applied to the 2012-2013 Property Tax estimate,[135] Property Tax revenues would not be expected to return to pre-recession levels until 2014-2015 under the City's base case scenario.[136] Further, at no point during the forecast period do projected revenues come close to the levels that would have been reached had property taxes continued to grow an annual rate of 3.0% since 2008-2009, shown in the chart below as the top dotted line.

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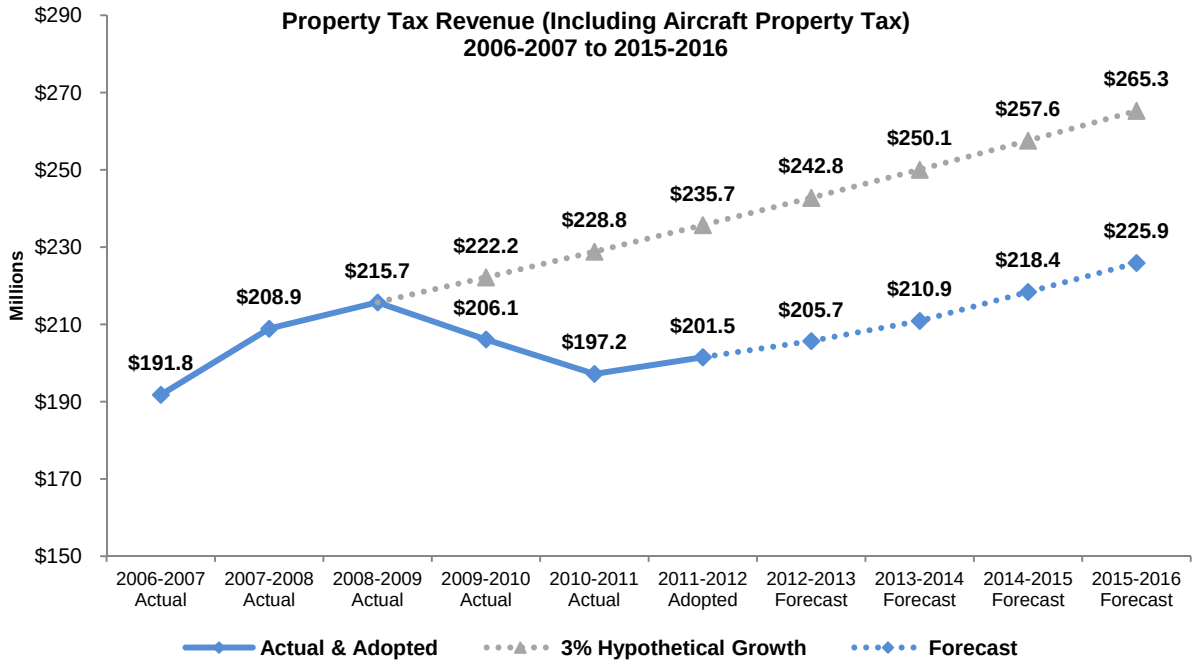
[135] Adjusted to reflect the February 2011 Forecast annual growth rates based on 2012-2013 Preliminary Forecast

[136] The base case scenario in the 2012-2016 Five-Year Forecast assumes a moderate economic recovery marked by slow improvement in employment levels and home values, and relatively low inflation 2012-2016 Five-Year Forecast & Revenue Projections, Office of the City Manager, February 2011 (base case scenario).

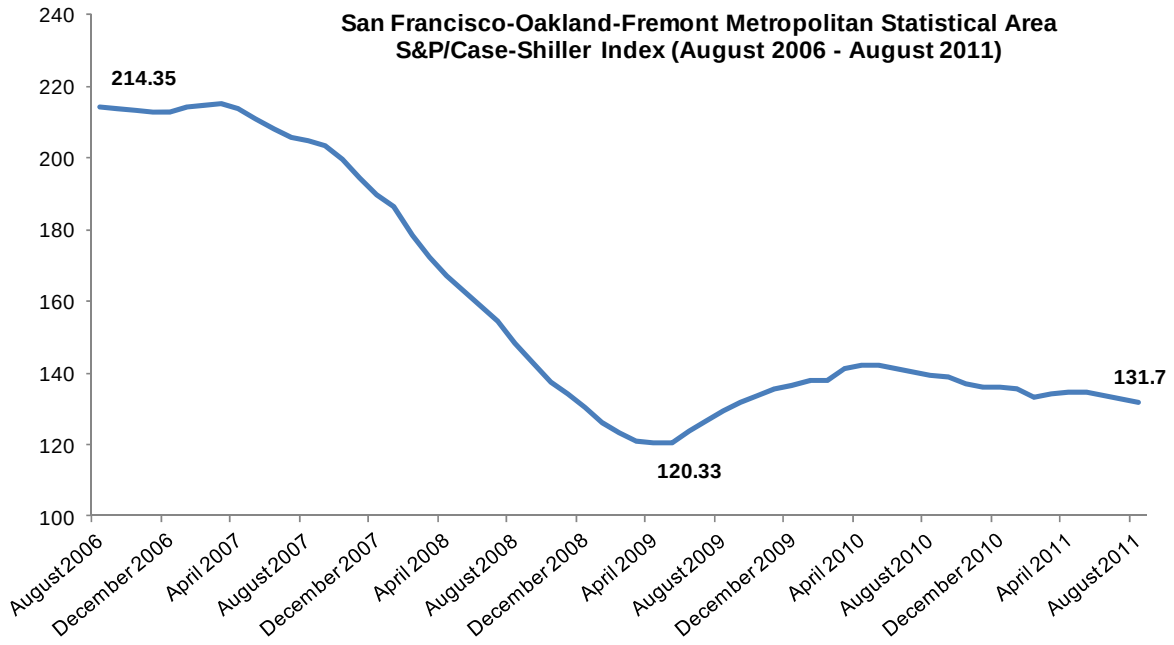


Sources: San José Adopted Budgets 2006-2007 through 2011-2012, 2012-2013 Preliminary General Fund Forecast (November 2011) and Five-Year Forecast (February 2011).

As outlined above, overall economic recovery remains weak and uncertain, and the housing market continues to be similarly challenged. Home prices as of August 2011 were still at summer 2003 levels on a national basis – down 31.2% from five years previously (seasonally adjusted; based on a composite of 20 metropolitan areas).[137]

While the San José-Sunnyvale-Santa Clara Metropolitan Statistical Area (MSA) is not among those tracked by Case-Shiller, data is available for the neighboring San Francisco-Oakland-Fremont MSA that is also part of the broader regional San José-San Francisco-Oakland Combined Statistical Area (CSA). Despite some modest recovery from a low point in 2009, the San Francisco-Oakland-Fremont MSA remains 38.6% below the levels reached five years earlier in August 2006, a more severe decline than experienced nationally. Also of concern, comparing year over year data (to minimize seasonal influences), August 2011 prices in the San Francisco index are back down 5.3% from their prior year, August 2010 levels.

[137] S&P/Case-Shiller Home Price Index, October 25, 2011.



Source: S&P/Case-Shiller Home Price Index, October 25, 2011.

Looking at data specific to San José, median home sale prices for single-family residences within the City paralleled the broader national and Bay Area trends. As noted previously, San José median home sales prices remain 38% below peak 2007 annual levels as of September 2011. Similarly, while there has been some modest recovery from post-collapse lows, September 2011 levels are down over 5% from September 2010 levels.[138]

As property values drop, so does property tax revenue. Under Proposition 8, temporary reductions in assessments are applied when the current market value of a property is less than the current assessed value. As a result of the housing market downturn, the number of revaluations has increased, contributing to reduced property tax revenue for many municipalities, including San José.[139] San José's non-residential sector is even weaker, with anticipated softness in commercial property values throughout the City's 2012-2016 Five-Year Forecast period.

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[138] Santa Clara County Association of Realtors, September 2011 median home sales prices (single family) in San José of $481,500, down from $510,000 in September 2010 and $772,050 in June 2007. Note: median sales price data can be influenced by the number and type of homes on the market, whereas the Case-Shiller index indexes prices based on "sales pairs" based on prices for the same properties, weighted to reflect quality change in the homes being compared.

[139] As property values begin to rise again, Proposition 8 will not limit assessed value increases to 2% per year until the assessed value regains its base value.

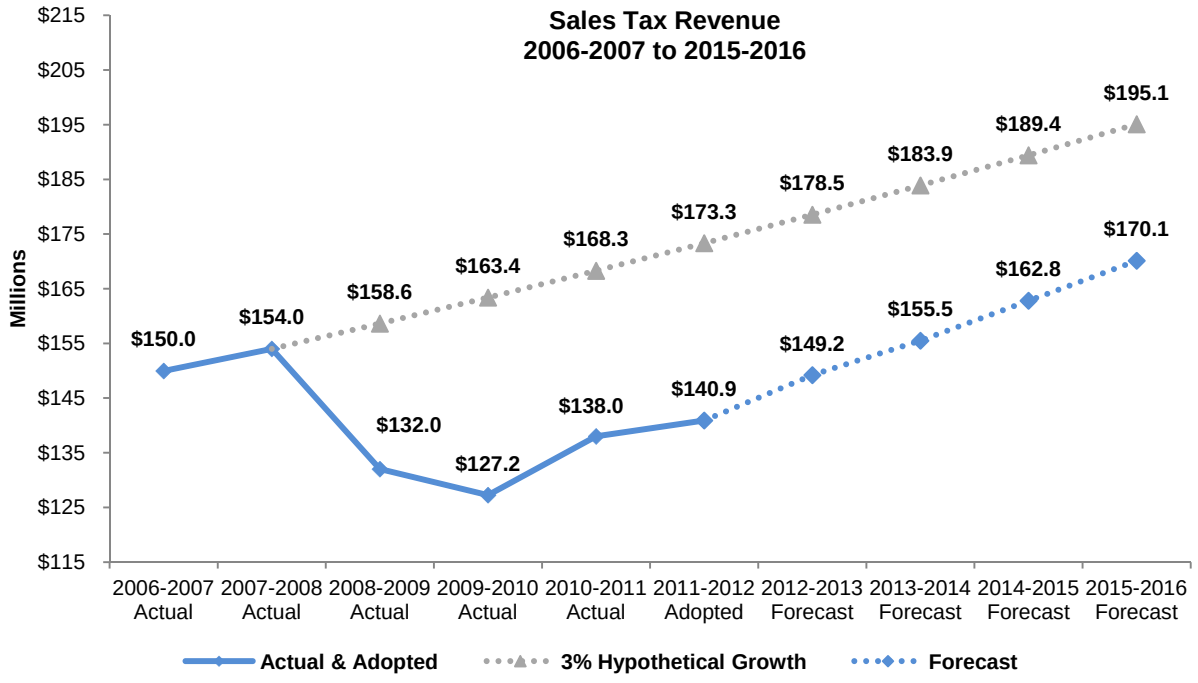
Overall, the 2012-2013 Preliminary Forecast (November 2011) projects growth of 2.8% in Property Tax receipts for 2012-2013. In the City's 2012-2016 Five-Year Forecast (February 2011), growth in fiscal years 2013-2014 through 2015-2016 is projected to range from 2.5% to 3.6% annually – considered to be moderate annual growth. These forecasts are based on the assumption that moderate economic recovery will continue, marked by slow improvement in employment levels and home values, and relatively low inflation.

3. Sales Taxes

Sales tax revenues are another important revenue stream for San José, and account for 18.4% of General Fund revenues in the 2011-2012 Adopted Operating Budget. Sales and property taxes combined account for nearly half of San José's revenues. Like property taxes, sales tax receipts have been dampened by the general economic downturn. The City estimates sales tax revenues to be $140.9 million in the Adopted 2011-2012 Operating Budget, an increase of 2.1% over actual 2010-2011 sales tax revenues of $138.0 million, incorporating some one-time accounting adjustments to reflect prior-year collections and the impact of State revenue exchanges. As part of the 2010-2011 Annual Report budget actions, an upward adjustment of $6.2 million to the 2011-2012 Sales Tax revenue estimate was approved, increasing the projection to $147.1 million based on higher actual 2010-2011 performance and one-time adjustments. With this increase, the 2012 Sales Tax estimate reflects growth of 6.6% from the 2010-2011 actual collection level.

Overall, projected 2011-2012 sales tax revenues remain 4.5% lower than peak 2007-2008 sales tax revenues of $154.0 million. In the 2012-2013 Preliminary General Fund Forecast, Sales Tax receipts are projected to reach $149.2 million in 2012-2013. This figure factors out a sizeable amount of one-time prior year adjustments and applies a 3% economic growth factor. If the growth rates assumed in the 2012-2016 Five-Year Forecast issued in February 2011 are applied to the 2012-2013 Sales Tax estimate,[140] City sales tax revenues would not be expected to return to 2007-2008 levels until 2013-2014. Further, much as with property tax receipts, at no point during the forecast period are sales tax revenues projected to come close to what they would have been had growth continued at 3.0% per year since 2007-2008.

[140] Adjusted to reflect the February 2011 Forecast annual growth rates based on 2012-2013 Preliminary General Fund Forecast.



Sources: San José Adopted Budgets 2006-2007 through 2011-2012, 2012-2013 Preliminary General Fund Forecast (November 2011) and Five-Year Forecast (February 2011) (forecast growth rates).

Overall, the 2012-2013 Preliminary General Fund Forecast and the 2012-2016 Five-Year Forecast (February 2011) project a return to moderate growth in Sales Tax receipts – with 3% underlying economic growth in 2012-2013 and growth ranging from 4.25% to 4.7% annually in the out years of the forecast period.

4. Other Revenue Sources

In the aggregate, the City's other revenue sources are projected to generate steady, but not high, rates of overall growth across the City's 2012-2016 Five-Year Forecast period. Major categories for these other sources are outlined below.

Utility Tax & Franchise Fees account for approximately 17.1% of San José's General Fund revenues in the 2011-2012 Adopted Budget. The City collects franchise fees from companies using public property in the distribution of natural gas, electricity, and water. The City also collects franchise fees from companies performing commercial solid waste collection and cable television providers. Utility taxes are charged to the users of any given utility (electricity, gas, water, telephone). Utility and franchise fees are less sensitive to the economy than sales and property taxes, and historically have been consistent sources of revenue for San José in general. At the same time, these revenues are not considered high growth.

Transfers and Reimbursements account for 9.3% of the City's General Fund revenues in the 2011-2012 Adopted Budget. This revenue category is used to account for funds received by the General Fund from other City funds through a combination of means, including operating and capital fund overhead charges, transfers, and reimbursements for services rendered. The revenues in this category can vary significantly each year and are influenced by the following: changes in staffing costs, staffing levels, and the relative proportion of services delivered to other funds; the availability of funding in other funds that are appropriate to transfer to the General Fund; and the performance of Gas Tax revenues, which are transferred to the General Fund to reimburse the City for eligible expenditures.

Business Taxes were established as a separate revenue category in February 2011. In prior years, this revenue source was included in the Licenses & Permits category. The Business Tax category includes taxes from businesses based on their number of employees, as well as revenues generated from the Cardroom Business Tax, the Disposal Facility Tax, and the Marijuana Business Tax (effective March 2011). As a new tax, there is minimal collection data on the Marijuana Business Tax revenues. While the 2011-2012 Adopted Budget includes a revenue estimate for this category, there is some upside potential if actual performance exceeds expectations and downside risk associated with regulations and implementation of this program.

Licenses & Permit Revenues are generated from payments for the issuance of Building Permits, Fire Permits, and miscellaneous health and safety-related licenses and permits. For most licenses and permits, the fees charged by a given department are based on full recovery of the estimated costs for providing each service. The demand for these licenses and permits, particularly development-related building and fire permits, are sensitive to economic downturns.

Other Agencies include revenues from local agencies, revenues from the State of California, and revenues from the federal government. This category represents 7.2% of the General Fund revenues in the 2011-2012 Adopted Budget. San José receives payments from local government agencies for providing a variety of services, such as fire and emergency medical services in unincorporated areas of the County, paramedic services, fingerprint identification services, and reimbursement from the San José Redevelopment Agency.[141] The City receives revenues from the State of California in a number of different forms, the largest of which are the Tobacco Settlement payments and various

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[141] Declining tax increment revenues are impacting the financial condition of the Redevelopment Agency (Agency). The 2011-2012 Adopted General Fund Budget includes a $10 million reduction in the reimbursement from the Agency for the $15.4 million in debt service payment on the City of San José Financing Authority Lease Revenue Bonds, Series 2001F, Convention Center Refunding Project, as well as a loss of reimbursement for other General Fund supported redevelopment activities. Impacts in 2012-2013 are dependent on the future of redevelopment agencies in California (Supreme Court ruling is expected by January 15, 2012) and tax increment revenue growth. Based on the City's initial analysis, the 2012-2013 Preliminary General Fund Forecast is anticipating another $10 million impact, for a total General Fund impact of $20 million.

grants to deliver services. The federal government also provides grant funding to support a variety of programs and services.

Other Revenues in the General Fund account for 8.2% of the General Fund revenues in the 2011-2012 Adopted Budget and include the following categories: Telephone Line Tax ($20.5 million), Fines, Forfeitures, and Penalties ($17.5 million); Other Revenue ($14.9 million); Transient Occupancy Tax ($7.2 million); and Use of Money and Property ($2.4 million). While some of these revenue sources are highly dependent upon market performance, such as Transient Occupancy Tax and interest earnings, the majority of these revenues are not driven primarily by economic conditions.

Based on detailed City analysis of each of these revenue streams in the 2012-2016 Five-Year Forecast, aggregate growth for all sources other than sales and property taxes is projected to range from 3.2% in 2013-2014 to 1.8% in 2015-2016.

Much as with Proposition 13 and property taxes, Propositions 62, 218 and 26, discussed above, have greatly limited the ability of the City and other local governments to control or affect revenue growth in many of the categories outlined in this section.

C. General Fund Expenditures

The City's Budget is heavily focused on public services. In turn, governmental service delivery is labor-intensive – relying on the City workforce to patrol the streets, respond to emergencies, provide services at libraries and community services, and deliver the other direct and supporting services of San José. As a result, and as noted elsewhere in this report, employee wages and benefits account for two-thirds of the 2011-2012 Adopted Budget for the General Fund.[142]

Summary descriptions for the major categories of General Fund expenditures[143] are as follows:

Public Safety: This category represents 50% of the 2011-2012 Adopted Budget and reflects the public safety services provided by the Police and Fire Departments. The major services include emergency response to calls for service, fire suppression, emergency medical services, and Police patrol and investigations.

Non-Departmental: The Non-Departmental category represents 25% of the 2011-2012 Adopted Budget and includes city-wide expenses (12.5% of budget), capital contributions (1.1% of budget),

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[142] City of San José, 2011-2012 Proposed Budget, General Fund Balancing Strategy Detail. This total would be even higher, but for approximately $58.5 million in assumed savings from the continuation of 10% employee compensation reductions and a roll back of any general wage increases in 2010-2011 for all City employees.

[143] For detailed analysis of assumptions for expenditure increases, please refer to the 2012-2013 Preliminary General Fund Forecast and the February 2011 Five Year Forecast, both available on the City's website at www.sanjoseca.gov/budget/

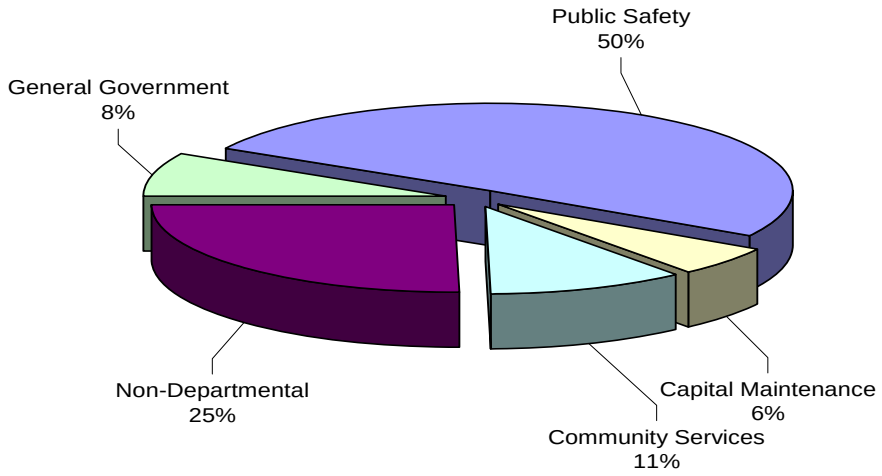
transfers to other funds (2.8% of budget), and reserves (8.9% of budget). The largest components of city-wide expenses include workers' compensation payments, Convention Center lease payments, sick leave cashout upon retirement, and various revenue-supported grants. Transfers to other funds cover City obligations, such as City Hall debt service payments and costs associated with the Hayes Mansion operation. Capital contributions cover fire apparatus replacement costs, closed landfill compliance, unanticipated emergency maintenance and costs associated with the completion of a minimal number of capital projects. The reserves category includes the Contingency Reserve, other earmarked reserves, and the encumbrance reserve.

Community Services: This category represents 11% of the 2011-2012 Adopted Budget. It covers programs such as parks, libraries, recreation centers, planning and building development services, and code enforcement.

General Government: This category represents 8% of the 2011-2012 Adopted Budget and reflects the cost for all management and administrative functions of the City and independent officials, including Human Resources, Economic Development, Information Technology, Finance, City Manager, Mayor, City Council, City Attorney, City Auditor, City Clerk, and Independent Police Auditor.

Capital Maintenance: This category represents 6% of the 2011-2012 Adopted Budget and reflects General Fund costs associated with the construction and maintenance of the City's infrastructure by the Public Works and Transportation Department.

2011-2012 Adopted Operating Budget General Fund Uses



Source: City of San José 2011-2012 Adopted Budget.

While City revenues have paralleled the weakness in the overall economy, key spending categories have grown much more rapidly than revenues have fallen. Revenue (excluding beginning fund

balance) is expected to decline by 2.3% from 2009-2010 actual collections to the 2011-2012 Adopted Budget, yet the average total *cost* per full-time equivalent position rose by 18% in this time period – from $120,418 to $141,918. To partially offset this growth in costs per employee, the City cut total headcount by nearly 18.5% -- a reduction of 1,223 FTEs. Despite these measures, relative to revenue declines of 2.3% from 2009-2010 to 2011-2012, overall personnel costs rose by 4.7%.

City retirement contributions were by far the primary drivers of the City's personnel cost growth across this period, nearly doubling, while all other cost drivers and revenues decreased during 2009-2010 through 2011-2012. Such benefit cost growth in excess of revenues has severely eroded the City's fiscal resources for maintaining staffing, service, and wage levels, and will continue to do so unless steps are taken.

The critical takeaway here is that for the City, the cost per employee has been increasing at an unsustainable rate, as retirement costs have continued to increase. This is most apparent when looking at the budget information as compared to decreasing positions throughout the City. For the past ten years, the City eliminated over 2,000 positions (28%) from 7,453 positions in 2001-2002 to 5,400 positions in 2011-2012 (all funds). Meanwhile, the General Fund departmental budgets increased by 26% from $538.9 million in 2001-2002 to $678.2 million in 2011-2012. Because the cost of each employee has risen, the City and its departments have been forced to reduce staff and services in order to keep the budget in balance.

	2001-2002 Adopted Budget	**2011-2012 Adopted Budget**	**Change**	**Percent Change**
Public Safety				
Budget	$292.8 million	$457.0 million	$164.2 million	**56.1%**
Positions	2,734	2,263	-471	**-17.2%**
Other Departments				
Budget	$246.1 million	$221.2 million	-$24.9 million	**-10.1%**
Positions	4,719	3,137	-1,582	**-33.5%**

**Other includes: Parks, Recreation & Neighborhood Services; Library; Information Technology; Transportation; Public Works; Environmental Services; Airport; Finance; Human Resources; Planning, Building & Code Enforcement; Economic Development; Mayor; City Council; Council Appointees; etc.*

BASELINE SERVICES AS OF JANUARY 1, 2011

In May 2011, the City's Fiscal Reform Plan determined that the City's acceptable baseline for providing services would be measured by the level of services being provided by the City as of January 1, 2011.[144] Service level metrics were determined by using either actual data or the level approved in the 2010-2011 Adopted Budget. For example, response times for Fire and Police services are based on performance data whereas hours of operation for the Library or Neighborhood Services are based on the service levels approved as part of the 2010-2011 Adopted Budget. Additionally, in order for the City to support these baseline service levels, strategic support services will need to be funded at an adequate level.

FIRE DEPARTMENT

- 33 Fire Stations open;
- On average, City-wide, 82.6% of time, the initial responding fire unit arrives within 8 minutes after an emergency 9-1-1 call is received;
- On average, City-wide, 85.2% of time, the second response fire unit arrives within 10 minutes after an emergency 9-1-1 call is received.

POLICE

- On average, City-wide, average response time for Priority One police calls for service (present or imminent danger to life or major damage/loss of property) is 6.04 minutes;
- On average, City-wide, average response time for Priority Two police calls for service (injury or property damage or potential for either to occur) is 12.74 minutes;
- On average, overall, the clearance rate (number cleared / total cases) for Part 1 crimes is as follows: Homicide (65.00%), Rape (19.37%), Robbery (26.54%), Aggravated Assault (39.93%), Burglary (5.58%), Larceny (18.90%), and Vehicle Theft (8.85%).

[144] Depending on the service provided, the metrics reflect actual 2010 Calendar Year-End performance data (e.g., Fire and Police response times) or the service level as approved as part of the 2010-2011 Adopted Budget (e.g., Library Hours).

LIBRARY

- On average, 18 library branches are open 39 hours per week;
- On average, King Library (subject to future contractual arrangements with San José State University):
  - Hours open: 72 hours per week per academic semester; 58 hours per week otherwise;
  - Children's Room: 50 hours per week;
  - Third Floor General Collection and Reference Desks: 64 hours per week;
  - California Room: 20 hours per week;
  - Access Services: 72 hours per week;
  - Periodicals: 72 hours per week;
  - Second Floor Reference Desk: 72 hours per week.

PARK, RECREATION, AND NEIGHBORHOOD SERVICES

- On average, 10 Hub Community Centers are open 63 hours per week;
- On average, 9 Satellite Community Centers are open 40 hours per week;
- On average, 8 Neighborhood Centers are open for 15 hours of programming per week.

STREET MAINTENANCE

72 miles of residential and arterial streets resealed and 6 miles of residential and arterial streets resurfaced with various Capital and Grant funds (no General Fund allocation). Maintaining this street maintenance level will be contingent upon receiving commensurate levels of regional, state, and federal funds annually.

FACILITIES BUILT OR UNDER CONSTRUCTION / OPENING DEFERRED

- South San José Police Substation
- Bascom Community Center and Branch Library
- Calabazas Branch Library
- Educational Park Branch Library
- Seven Trees Branch Library