

City of Palo Alto  
Office of the Mayor and City Council

**FILED**

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Chief Executive Officer/Clerk,  
Superior Court of CA County of Santa Clara  
BY D. ADYCKI

August 4, 2010

Honorable Jamie Jacobs-May  
Presiding Judge  
Santa Clara County Superior Court  
191 North First Street  
San Jose, CA 95113

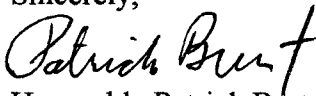
Re: Response to the 2009-10 Santa Clara County Civil Grand Jury Final Report "Cities Must Rein in Unsustainable Employee Costs"

Honorable Judge Jamie Jacobs May,

Attached (Attachment A) is the City of Palo Alto's response to the Grand Jury's Final Report on public employee costs. Palo Alto's City Council approved the response on August 2, 2010. In addition to responding to the Grand Jury request, the City would appreciate clarifying or correcting Palo Alto information in the report (Attachment B).

The City wants to thank the Grand Jury for its conscientious work and important findings. The report is invaluable as the City strives to align its costs with its resources. We will share the contents of the report with our employee groups as we mutually endeavor to maintain a sustainable budget.

Sincerely,



Honorable Patrick Burt  
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City of Palo Alto  
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Palo Alto, CA 94301

Cc: Angie M. Cardoza  
Foreperson  
2009-10 Civil Grand Jury

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## ATTACHMENT A

### **Response to the 2009-2010 Civil Grand Jury of Santa Clara County Final Report “Cities Must Rein in Unsustainable Employee Costs”**

#### **SUMMARY**

The City of Palo Alto agrees with the primary thrust of the Grand Jury’s Report that unsustainable employee costs must be aligned with available resources. Moreover, those costs must be considered in light of significant infrastructure needs and the public’s expectation of services. As demonstrated by its balanced budgets, minimal use of reserves, Triple A credit rating, and stellar annual outside audits, the City prides itself on responsible financial stewardship and management. It fully intends to maintain these best practices and adjust costs and revenues as needed.

The City agrees with many of the Grand Jury’s findings and recommendations and had taken clear concrete steps to address them even prior to the issuance of the Grand Jury’s report. In addition, the City intends to pursue medical and pension changes, already achieved with non-public safety employee groups (management, professionals, and SEIU workers), in current and future negotiations with its public safety unions.

The City does, however, want to state that progress on some recommendations must be viewed within the context of processes that are to a large extent beyond the City’s control. For example, the City must abide by contractual obligations of its labor contracts as well as legal requirements to meet and confer and bargain in good faith over matters within the scope of representation. This places real and practical constraints on the City’s ability to move forward with changes it may believe necessary, but which are subject to negotiation. The City genuinely strives to work in a collaborative manner with its employee groups to reach agreements that ensure a sustainable financial future and excellent services to the community.

The Grand Jury’s findings are valuable and provide confirmation of the direction that the City of Palo Alto and other cities are following to deal with the severe impacts of the recession and the wage and benefit liabilities that have emerged. As evidenced below, a good faith effort to address the Grand Jury’s issues was initiated prior to the Grand Jury report and will continue to be followed in the future. It is important to note that many of the Grand Jury’s recommendations that would remove benefits were benefits negotiated and granted over an extended period of time. It would be challenging, at best, to expect negotiations to address all of them in a short period of time.

#### **FINDINGS AND RECOMMENDATIONS**

##### **Finding 1**

The costs of total compensation for employees have grown substantially in the past decade and now threaten the cities’ fiscal stability.

**RESPONSE:** The City agrees with this finding. The City of Palo Alto's compensation costs, particularly in the area of pension and medical expense, have grown substantially in the past decade. Through its annual Long Range Financial Forecast (LRFF), the City identifies the "drivers" of future surpluses and deficits. In the most recent 10 year forecast, deficits were projected from FY 2011 through FY 2020. They were driven primarily by falling revenues due to the recession; significantly rising medical premium and retiree medical liability expenses; and pension costs resulting from expensive plans and weak portfolio performance by CalPERS. Using the Forecast, the City is proactive in developing budget strategies and seeking structural expense changes to erase those deficits

### **Recommendation 1**

All of the cities in the County need to implement measures that will control employee costs. As a starting point, each city should determine the percentage of savings required from the total compensation package to reach budget stability for the unions to choose to achieve that percentage goal.

**RESPONSE:** The recommendation had already been implemented. During each budget process for the following fiscal year, the City determines the savings needed to balance its budget and to position itself for future budget stability. Those savings have incorporated reductions to employee compensation. In the 2009-10 Budget, for example, the City:

- froze pay for non-public safety employees for fiscal years 2010 and 2011. Police officers voluntarily deferred a contractual pay increase for FY 2010 until FY 2011
- eliminated management employee's Variable Management Compensation plan (a bonus based on work quality and achievement of stated goals)
- eliminated tuition or professional training reimbursement for SEIU members
- increased PERS employee contribution rates for SEIU members from 2% to 5.75%
- eliminated 2 float days off for SEIU members

It is important to note that the City seeks equity among groups in wage and benefit concessions. For example, for management and SEIU employees in FY 2010, the reductions equated to nearly 4% of salaries and benefits. While one group may show reductions in a number of areas, the ultimate goal is to cut expenses equitably among groups. Similar reduction percentages will be sought from public safety employees as their contracts expire.

In addition to the above changes, in wages and benefits, the City implemented a two tier retirement plan (2% at 60) as well as a medical premium cost sharing plan for new non-public safety employees. The City is currently in negotiations with its fire personnel for similar structural changes in benefits and will pursue this with its police personnel when contract negotiations begin for FY 2011-12.

### **Finding 2**

Salary and wage increases do not reflect changes in economic conditions; e.g. even with minimal inflation, yearly COLAs are granted with little bearing on the actual increase in cost of living or market conditions.

**RESPONSE:** The City respectfully partially agrees and disagrees with the finding

### **Recommendation 2**

Cities should not increase salaries and wages that are not supported by planned revenue increases. Cities should tie COLA increases to clear indicators and retain the ability to adjust or withhold based on current economic data.

**RESPONSE:** The City has not had a COLA in its contracts in many years and agrees that it should not increase salaries and wages that are not supported by planned revenue increases. Staff has received direction from Council to tie salary increases to revenue performance and each fiscal year, the City determines what it can and cannot afford in its forthcoming budget. This financial view (derived from the LRFF) is incorporated in all labor negotiations. Recent minimal inflation impacts were a factor in freezing non-public safety employee pay along with the need to balance the budget.

It is important to note that in multi-year labor contracts (which bond rating agencies look upon favorably and thereby reduce debt expense), the City cannot adjust pay increases based on inflation or market conditions. In addition, there can be job classifications or skills where demand exceeds supply and cities need discretion to provide competitive wages e.g., electric linepersons, which may not correlate with inflation changes. Flexibility in the area of wages is important to maintain operations. To the extent implementing this finding would limit its flexibility to consider such operational factors, the City disagrees.

### **Finding 3**

Step increases are arbitrary and do not adequately represent an employee's added value to a city. Combined with COLAs, new employees' wages increase quickly and are not necessarily reflective of improved knowledge and skills.

### **Recommendation 3**

Cities should negotiate step progressions from the current three and a half years to seven years. Employees should not receive COLA increases while in step progression.

**RESPONSE:** The City has not had a COLA in its contracts in many years and agrees with the tenor of the recommendation in that excessive pay increases should be eliminated. It respectfully disagrees, however, with a seven year step progression. The concept of steps is that an employee's skill level and value in the job increases as they are in the position, but that learning and value reach a plateau after a number of years. Palo Alto has a five step progression for SEIU, fire and police personnel. The step system allows the City to maintain equitable pay scales within its employee groups for comparable work and performance. The current 4.5 year progression from step 1 to step 5 appears reasonable in that it offers incentives to progress over an extended period of time. The City will, however, carefully monitor overall pay increases to make sure they can be supported by available resources.

The City takes its fiduciary responsibility most seriously and has demonstrated this by balancing its budget each year, minimizing use of its General Fund reserve, and earning a Triple A credit

rating. At the same time, to provide the best services to its citizens it seeks highly qualified and capable public servants. Attracting and maintaining such staff requires a careful balance between prudent financial practices and maintaining a capable and dedicated work force. Having step increases allows the City to: hire people at pay rates based on their level of experience; provide incentives for development; and to recognize employee performance that meets work standards.

#### **Finding 4**

Medical insurance costs for active employees are growing year after year at rates that exceed most cities' revenue growth, while the employee contribution to medical care is minimal.

**RESPONSE:** The City agrees with this finding. The City views Findings 4 and 5 as the most serious issues it must address in order to achieve long-term financial stability. By calculating the present value of current retirement and retiree medical commitments the City can gauge the magnitude of its liabilities and the structural changes necessary to align costs with available resources.

Medical premium costs have accelerated at a pace that significantly exceeded revenue growth and inflation. In addition, the implementation of GASB 45 has made public agencies acutely aware of the post retirement medical liabilities. As background to the City's effort to control medical expenses, several years ago it eliminated the availability of PERS highest cost plan, PERS Care, to employees. In addition, it increased the vesting period required to earn full medical coverage for retirement. These were the first steps taken to decrease this benefit cost.

#### **Recommendation 4**

Cities should negotiate with employees to assume some of these increased costs for their medical benefits. To contain medical costs cities should consider the following:

A. Split monthly premiums between the city and the employee and increase the employee's share, if already cost splitting, and remove any employee caps.

**RESPONSE:** The City agrees with employees sharing medical premium costs and has implemented this recommendation with some of its labor groups. In FY 2010, the City created and included in management and general classified employee agreements a plan for sharing medical premium costs. The City could not reach agreement and had to impose the medical cost-share program with the general classified employee unit. This plan is to take effect in January 2011 unless a different cost sharing plan can be negotiated with City bargaining groups prior to that date. The plan is for employees to share 50% of cost premium increases up to a maximum of 5% in any single year. The cost sharing will continue until such time as the employee share represents 10% of total premium costs. The City is committed to pursuing a similar plan with its public safety unions as well.

Although the City is still discussing medical cost sharing options, removal of the cap must be negotiated. Making changes in a unionized environment is subject to the meet and confer process based on bargaining in good faith. This means that incremental change is a reality. Should

pressures on the City budget increase or increase dramatically, the City can and will revisit additional cost sharing arrangements. The City of Palo Alto has removed the most expensive health care provider for current and future retirees (2007). By increasing the vesting period from 5 to 20 years for retiree medical benefits (2004), future retirees must contribute towards the health premium cost unless they meet the 20 year requirement.

B. Establish reasonable co-pays for doctors' visits, prescription drugs, and in-patient and out-patient hospital care.

**RESPONSE:** Not implemented or applicable. Palo Alto is part of the CALPERS Public Employees Medical and Health Care Act (PEHMCA) medical insurance program. It cannot unilaterally determine co-pay, deductibles or other plan benefits as those are established by the CALPERS Board.

C. Prohibit an employee from being covered by both city-provided medical benefits and as a dependent of another city employee.

**RESPONSE:** The City has a financial incentive program in place to promote this goal and it has been successful in curbing medical costs. The City would have to negotiate changes to this program and cannot unilaterally prohibit an employee from dual coverage.

D. Reduce cash-in-lieu payments.

**RESPONSE:** The City has not implemented to date. Assuming the cash-in-lieu payments are for incenting staff to not have dual coverage, the City has found the incentive program successful in reducing costs. While the City considered and evaluated a change to this program in FY 2010 SEIU negotiations, the current program produces effective cost savings. Because the incentive is part of labor agreements, the City is not in a position, at this time, to change the current program. If long-term financial pressures continue, however, this is an area where cost reductions could be considered after additional analysis.

E. Introduce a new lower premium, high-deductible medical plan.

**RESPONSE:** The City has partially implemented this recommendation over time, but is limited as a PERS plan member in the plan changes it can make. Palo Alto moved in 1992 from being self-insured to PEHMCA to lower its medical costs. As part of PERS, the City cannot unilaterally determine co-pay, deductibles or other plan benefits. At this time, the City is not researching other medical plans since it is concentrating its efforts on having employees share in medical costs. The City is concerned by the recent, overall 11% cost increase in a preliminary PERs rate sheet for 2011 and will make its views known to PERS. Over time, the City may pursue other health options.

## **Finding 5**

Pension formula changes instituted in the past decade, stock market losses, the aging "baby boomer" work force, and the growing unfunded pension and OPEB liability all contribute to

making retiree pension and health care costs the most problematic and unsustainable expense the cities are facing. The city contribution to pension plans and OPEBs far exceeds the employee contribution.

**RESPONSE:** Agree.

## **Recommendation 5a**

Cities should:

1. Renegotiate and make provisions for increasing the employees' contribution for current pension plans.

**RESPONSE:** As stated under Recommendation 1, the City has implemented and negotiated a higher contribution from SEIU members to the employee's share of pension plan costs. The share of the 8% employee contribution has risen from 2% to 5.75%. This increase began in FY 2010. Managers currently pay 2%; Fire employees pay 9% (firefighters were recently given a 9% salary increase, however, which they use to pay the 9% employee contribution. In effect, the City is paying the full employee share); and Police employees do not pay any contribution toward their 9% employee share. Again, to achieve this goal, the City must engage in the process of good faith negotiations with its labor unions. During upcoming negotiations with public safety, contributions to pension plans will be negotiated.

2. Renegotiate to stop paying the employees' contribution amount to pension plans.

**RESPONSE:** The City has taken steps to increase employee's contributions (recent negotiation with SEIU raised contribution as cited above) and will continue to take such steps as financial conditions warrant. Progress toward this goal must be viewed in the context of the good faith negotiations process required by law.

3. Renegotiate to implement a contribution amount for employees to OPEB; this contribution should provide for a reasonable split of costs between a city and the employee for retiree medical and dental benefits.

**RESPONSE:** Please see response to Finding 4, Recommendation 4A. In implementing a medical cost sharing plan for management and SEIU, the City included current employees and those employees retiring after January 1, 2011 (This plan would not affect current retirees). As a part of the cost share program, the City will be contributing an amount equal to the employee portion of cost-share to the retiree medical trust. Through informal discussions, Public Safety employees are aware of the City's desire to negotiate a similar plan for their union agreements. We are currently negotiating with the fire units and will begin negotiations with the police union and sworn police management prior to the beginning of FY 2012. The City does not provide dental or vision benefits to retirees.

## **Recommendation 5b**

Cities should thoroughly investigate reverting to prior pension formulas that were less costly.

## **Recommendation 5c**

**RESPONSE:** Partially agree and disagree

To provide a meaningful, long-term solution, the cities should negotiate agreements to:



1. Institute a two-tier system for pension and retiree health care for new hires.

**RESPONSE:** The City has instituted a two-tier retirement system for non-safety employees hired after July 17, 2010. The retirement plan for these new employees is 2% at 60. For non-safety employees hired before July 17, the retirement plan is 2.7% at 55. The City will negotiate in current and upcoming negotiations for a two-tier plan for new public safety personnel. This proposal will save the City money and promote equity among the different employee groups. The existing plan for public safety personnel is 3% at 50.

2. Increase the retirement age for 50 to 55 to 60 or 65.

**RESPONSE:** For new non-safety employees the retirement age has moved from 55 to 60 and the City will negotiate for higher retirement ages for new public safety employees.

3. Calculate pensions on the last three to five years of salary.

**RESPONSE:** The City's current retirement plans are based on the single highest year of pay during the last three years. This practice was maintained in the new two-tier retirement plan for miscellaneous employees. The City has proposed a three year formula to calculate pensions to the fire union during current negotiations, but this is subject to further discussion. While the City agrees with methodologies to curb retirement costs, there are a variety of ways to achieve this goal and it is carefully weighing each option.

4. Replace current post-employment health care plans with health savings plans.

**RESPONSE:** Not considering implementation at this time. The City has moved in 2010 to have employees share in the cost of OPEB costs and does not believe further change is necessary at this time. Current efforts represent an important first step that could lead to further savings and sharing of cost in the future. With few details on the current health care legislation, it is believed premature to consider health savings plans. Once the new federal legislation is understood, the City can investigate health savings plans within its broader effort to contain post-employment health costs. Parenthetically, the City of Palo Alto is one of the few cities nationwide to have partially funded its retiree health care liability. It deposited approximately \$32 million in a PERS trust to fund the liability.

## **Finding 6**

Public sector employees are granted a generous number of holidays, personal days, vacation days and sick leave annually. Rules and limits on accrual vary by city and union, but vacation days and sick leave can be accumulated and converted to cash or calculated into the pension benefit within those limits.

**RESPONSE:** The City agrees with this finding.

### **Recommendation 6a**

Cities should renegotiate with the bargaining units to 1) reduce vacation time; 2) reduce the number of holidays and/or personal days; 3) cap sick leave and eliminate the practice of converting accumulated sick leave to cash or adding into their years of service for inclusion in their retirement benefit.

**RESPONSE:** The City has implemented steps to contain fiscal impacts from non-productive days. In terms imposed on SEIU in FY 2010, 2 floating holidays were eliminated. SEIU has agreed to extend this reduction into FY 2011.

Since 1983, Palo Alto has implemented caps on sick and vacation leave accruals. Also, it does not allow for sick leave to be cashed out or to be part of the years of service in pension calculations. Further limitations on the total number of days off will need to be part of the good faith negotiation process going forward.

### **Recommendation 6b**

Cities should negotiate to substitute paid days off for unpaid days instead of imposing furloughs. For example, reduce paid holidays to major holidays only, consistent with private industry; and convert minor holidays to unpaid. Therefore, the public is not impacted by fewer services caused by furloughs, and the city saves the employee cost.

**RESPONSE:** Palo Alto has not used furloughs as part of its budget balancing solutions in the past five years. Instead, the City has changed the way it delivers services by contracting out and reducing administrative support. Since 2009 the City has reduced 60.5 full-time equivalent fully benefited positions rather than using furloughs as a solution to reduce employee costs. If the City considers furloughs, it will negotiate for converting paid holidays to unpaid.

### **Finding 7**

Cities traditionally determine their compensation packages by surveying the wages and benefits of other public sector employees in the same geographic area. There is major resistance to comparing themselves or mirroring trends with the private sector. This has allowed wages and benefits to become artificially high and out of sync with market trends.

**RESPONSE:** The City respectfully partially agrees and disagrees with the finding. Within the City's labor agreements there are specific jurisdictions within the region to which both parties (City and union) have agreed to compare wages. These benchmarks are important in that they compare like positions in terms of skills and compensation. There are some City positions such as those in public safety that are not comparable to the private sector. Comparison with other employers, public or private, is used in unique circumstances or where specific job classification comparisons are not available such as in the case of the City's Utilities Department positions in which we attempt to use P.G.&E. benchmark data. These comparisons are reviewed from time to time in negotiations and could be changed as part of the negotiation process. For example, in the Fire Memorandum of Agreement, the City is obligated to benchmark specific cities

determined through arbitration to be appropriate matches to the City of Palo Alto Fire Department.

#### **Recommendation 7a**

Cities should research competitive hiring practices and alter the approach to determine fair wages and benefits for each city by using public and private sector data.

**RESPONSE:** The City partially agrees. Palo Alto does a salary survey of specific jurisdiction before each labor negotiation to determine fair compensation and potential “market” adjustments. It has not utilized private sector wage data to date and may consider doing so in the future. Using such data would be helpful and would need to be discussed within the context of the bargaining process.

#### **Recommendation 7b**

Cities should renegotiate salaries and wages using valid market comparisons and not only the current wage index. Cities should utilize more market-oriented compensation practices so that salaries can adjust as competition for labor changes. Cities should reduce entry-level compensation for positions for which there are many qualified applicants.

**RESPONSE:** For each negotiation the City makes market comparisons with the cities that are delineated in the labor contracts. Palo Alto does not use any specific wage index to determine salary increases nor is one specified in labor contracts. It is assumed that the supply and demand for labor in the market does affect each cities compensation results. The recent scarcity of applicants for police officer positions, for example, unfortunately drove wages higher, but this was in response to the market. The recommendation, however, is understood and the City will study and consider it prior to bargaining processes.

#### **Finding 8**

All cities perform certain core functions to run smoothly and provide services to their residents. To reduce employee costs and streamline operations, the cities are in various stages of contracting services to private industry or partnering with other cities, special districts or the County to deliver services.

**RESPONSE:** The City agrees with this finding

#### **Recommendation 8a**

Cities should explore outsourcing some functions and services to private industry. Cities should discuss the prospect with cities that are successfully doing this to determine best practices and areas for success. Cities should develop contracts with measurable objectives, performance goals, and timelines.

**RESPONSE:** The City has already implemented contracting out services in many areas. The following functions have been contracted out to the private sector to save costs: These include,

for example: landscaping of parks and City facilities; tree trimming and line clearing; and street and sidewalk repair. In July 2010, Utility bill processing and janitorial services were contracted out. In the Fall of 2010, the City will likely contract out the maintenance of its golf course. The City does, however, want to maintain a high level of service to its customers so it considers each contracting out opportunity carefully in terms of the balance between cost savings and service.

### **Recommendation 8b**

Cities should create partnerships with other cities, special districts and/or the County for services, such as payroll, human resources, animal control, police and fire. Cities should investigate sharing the cost of new information technology systems.

**RESPONSE:** Over the years, the City has established partnerships with other cities for the provision of wastewater treatment and animal services. Palo Alto provides dispatching and fire services to Stanford University. It has a collaborative and cost sharing relationship with the Palo Alto Unified School District for the maintenance of school athletic playing fields that both the schools and general community use for sporting activities.

The City operates a Regional Water Quality Control Plant whose members include Mountain View, Los Altos, East Palo Alto, and Stanford University. It operates an animal shelter that serves Mountain View, Los Altos, and Los Altos Hills. The City has a joint partnership with the cities of Sunnyvale and Mountain View for the provision of solid waste and recycling. Finally, the City provides fire and dispatching services to Stanford University. In all of these instances cost savings are realized by participating entities as fixed costs are shared and reduced and resources are optimized for the benefit of all.

The City Managers from Palo Alto, Mountain View, and Los Altos have agreed to meet to discuss further opportunities for sharing public safety equipment and services, such as consolidated dispatch. This discussion is in the early stages, but there is growing awareness of the need to reduce costs through regional cooperation.

Opportunities for partnerships that can reduce the number of employees and costs are approached on a case by case basis and are subject to the meet and confer process with affected employee groups.

### **Finding 9**

Cities can gain operational efficiencies and effectiveness with lower employee costs by making sure they are staffed with the correct numbers of people in the appropriate job classification in all departments and work groups.

**RESPONSE:** Agree. For the past several years and always during economic downturns, the City has evaluated each vacant position to determine whether it is absolutely necessary and whether its functions can be redistributed to other employees or contracted out. Cross training is a top priority of City departments so that key functions are backed up during illness or vacation.

## **Recommendation 9**

Cities should analyze the functions performed by all job classifications and make adjustments in the work force. Consolidate functions within the same group or a similar group. Reassign appropriate work to lower paid job classifications. Eliminate unnecessary functions.

**RESPONSE:** Agree. The City has been conducting a management classification study with the objective of reducing the large number of job classifications. By collapsing these classifications, additional flexibility for covering employee work functions will be realized. The City is close to completion of the study and then will perform an economic analysis and presentation to council in 2011. Implementation may take 3 years or longer depending on the results of the analysis.

In addition, during the last fiscal year, the City “froze” positions as they became vacant and executive staff used this opportunity to evaluate which positions could be proposed for elimination during the FY 2011 budget process. Between the management study and restructuring around vacancies, the City is eliminating unnecessary functions and finding opportunities to cover essential functions.

Reassigning work to lower paid job classifications is a valuable idea, but it is subject to union agreements and the “meet and confer” process. Since the City of Palo Alto owns seven different types of Utilities, it will continue to have unique classifications that usually don’t exist in other agencies. This will require further analysis.

## **Finding 10**

The San Jose City Auditor identified 88 positions currently being performed by public safety employees that can be performed by civilian employees at lower costs. The safety employees could be moved to positions that require their expertise and training. The auditor estimated this could be accomplished in less than 90 days and save approximately \$5 million annually.

**RESPONSE:** This finding pertains to the City of San Jose, but the City of Palo Alto does explore similar opportunities.

## **Recommendation 10**

San Jose should negotiate this suggested transfer with the San Jose Police Officers’ Association and set realistic timeframes to move these safety positions to civilian positions.

**RESPONSE:** This recommendation is specific to San Jose. The City, however, does explore opportunities in this area.

## **Finding 11**

In many cities, the contract negotiation process is completed by placing the negotiated collective bargaining agreements on the consent calendar for approval, which is acted on quickly at the start of council meetings by a single motion and vote of the council.

The City of Palo Alto agrees with this finding.

## **Recommendation 11**

Cities should consider holding well-publicized public hearings about the cities' goals of negotiations before negotiations begin, and again at the end of negotiations to report to citizens clearly what changes have been made in contracts.

**RESPONSE:** The City has held numerous information meetings with the public, Council and employees about the financial stresses it faces and the upcoming budget process. Solutions to solving budget deficits are proposed and discussed at these meetings. Embedded in the proposals are targets for labor cost reductions which are shared publicly. As an example, in FY 2010, a target of around \$3 million in labor cost reductions was proposed to Council and the public to balance the budget. It is the City Manager's responsibility to then propose a strategy for obtaining those reductions in closed sessions with Council. Naturally, that strategy changes with Council input and as negotiations evolve. Council is kept informed on every major point or change in negotiations.

During the City's negotiations with SEIU in FY 2010, the City established a public Web site that explained the City's proposals.

The results of negotiations are sent to Council in a City Manager Report and in public session, the Council must approve of a final contract. For example, on August 2, 2010, a Memorandum of Agreement with SEIU will be presented at a public hearing. Council Members, as well as the public, have the opportunity to make comments on the negotiated terms.

## **Finding 12**

Current contracts were negotiated in good faith by representatives of the cities and the bargaining units; they were approved by the city councils. Promises made to employees were made by elected officials, past and present. Responsibility for formulating and approving solutions to restore the cities' financial stability resides squarely with our elected officials. The economic downturn has placed additional pressure on the situation.

**RESPONSE:** Agree

## **Recommendation 12a**

City council members and mayors should become better informed about the fiscal realities in their cities, long-term costs and commitments, and be cognizant of potential issues in labor agreements.

**RESPONSE:** City has long since implemented. Palo Alto's Council Members are especially well-informed about the City's financial condition and important issues in labor agreements. Palo Alto has a Finance Committee comprised of 4 out of the 9 Council Members to discuss fiscal issues prior to items being presented to the full Council. Meetings and reports on budget issues occur throughout the year. This includes a presentation on the LRFF; quarterly, midyear, and year-end reports on the City's financial condition; preparatory information and staff plans for addressing budget issues prior to Finance Committee and full Council budget deliberations.

In calendar year 2009 staff and Council Members met in 11 closed sessions to discuss negotiations on labor contracts. In calendar year 2010 to-date, there have already been 11 closed session meetings on union contracts.

### **Recommendation 12b**

City councils and mayors should direct city administrators to (re)negotiate collective bargaining agreements that reverse the escalation of employee costs through concessions, cost sharing, and a second tier for new employees.

**RESPONSE:** This recommendation has been implemented and will continue to be followed to ensure a sustainable budget. As stated in Finding 5, the City imposed terms and conditions on SEIU that has contained costs and initiated a second retirement tier for new employees. This new tier will apply to management employees as well. Furthermore, the City will pursue two tier retirement plans with its public safety employees as well as concessions to reduce medical and other costs.

### **Recommendation 12c**

City councils and mayors should meet with the bargaining units to clearly outline the cities' financial health and show how employee costs are impacting the budget.

**RESPONSE:** Implemented annually during budget process. Palo Alto has a Council-City Manager (CM) form of government whereby the Council directs the CM to implement its policy goals. During the past several years, the City's CM has held outreach meetings with employees and labor groups to explain the City's financial condition and the rationale for proposed expense reductions. Power Point presentations replete with revenue and expense trend analyses are provided. The CM has met with union employees and the public to explain City finances prior to the budget process and negotiations.

### **Recommendation 12d**

City councils and mayors should inform citizens of their plans for controlling unsustainable employee costs and remove politics from the equation.

**RESPONSE:** Implemented. All budget meetings are held in public sessions. The City Manager's proposed budget is reviewed by the Finance Committee (subset of full Council) in public and public comment is always solicited. During these meetings, Council Members can

discuss any proposal or mechanism for controlling costs including reductions in force and lowering labor costs through wage and benefit reductions. In addition, the City Manager and Director of Administrative Services (includes Finance), held a plethora of community meetings on the proposals to balance the FY 2011 budget.

**Finding 13**

Binding arbitration is not open to the public and results in an adversarial process between the city and employee groups. Binding arbitration limits the ability of city leaders to craft solutions that work for the city's budget. The process has resulted in wage and benefit decisions that have been greater than the growth in basic revenue sources.

**RESPONSE:** The City agrees that binding arbitration limits the ability of city leaders to craft solutions that work for the city's budget.

The City of Palo Alto is bound by a section in its Charter requiring binding arbitration for public safety negotiations that reach impasse. Also, it must follow all legal, regulatory and contractual requirements regarding labor negotiations. The Council, however, recently requested from staff further analysis on the history of binding arbitration in Palo Alto and the pros and cons of having this requirement. In the Fall of 2010, the Council will review binding arbitration and determine whether it will place a measure on the ballot to rescind it from the Charter.

**Recommendation 13a**

San Jose City Council should make binding arbitration open to the public.

**RESPONSE:** This recommendation is not applicable to the City of Palo Alto, however, please refer to the response under Finding 13.

**Recommendation 13b**

San Jose City Council should prepare a ballot measure asking voters to repeal Section 1111 of the City Charter that addresses binding arbitration.

**RESPONSE:** This recommendation is not applicable to the City of Palo Alto.



## ATTACHMENT B

The City of Palo Alto would like to correct or clarify information in the Grand Jury's Report of May 26, 2010 as follows:

For table 3, page 6 in the report, monthly health care premiums comparing 2001 to 2010 should be:

<u>Most Expensive Plan</u> <u>Family</u>	<u>Employee Only</u>	<u>Employee +1</u>	<u>Employee +</u>
2001 PERS CARE	\$343.00	\$686.00	\$892.00
2010 Blue Shield Access	\$577.33	\$1,154.66	\$1,501.06

For table 5, page 9, the retirement formula should state "highest" year instead of "final" year.

For table 7, page 13, the days off per year given by the City needs correction. All employees/labor groups in the City have 2 personal business days. SEIU members have 3 float days for SEIU. The minimum to maximum potential total days off for each labor group are as follows:

Management	=	51 to 61* days
SEIU	=	39 to 54* days
Fire	=	32 to 43* days (based on 10 hour day/shift)
Police	=	29 to 42* days (based on 11 hour day/shift)

It is important to note that employees do not necessarily use all of sick leave or vacation time allotted to them.

\*A range is provided based on the increasing number of vacation days as work longevity increases. In the 20<sup>th</sup> year of service, employees earn the maximum number of vacation days in the labor agreements.

In addition, here are the revised figures for the grand jury report for estimated median total compensation for public safety:

Police, FY 2000: \$102,771

Police, FY 2010: \$171,970

Fire, FY 2000: \$107,634

Fire, FY 2010: \$169,709