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January 24, 2005

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FINAL ADJOURNMENT: The meeting adjourned at 11:00 p.m. 431

The City Council of the City of Palo Alto met on this date in the Council Chambers at 6:45 p.m.

PRESENT: Beecham (arrived at 6:50 p.m.), Burch, Cordell, Freeman, Kishimoto, Kleinberg, Morton (arrived at 7:10 p.m.), Mossar, Ojakian

Special Orders of the Day

1. Presentation from Foothills/DeAnza Community College District

Martha Kanter, Chancellor of Foothill-DeAnza Community College District, said the Foothill-DeAnza Community College District provided a dynamic learning environment that fostered excellence, opportunity and innovation in meeting the needs of the diverse students and community. The Foothill-DeAnza District was among the top three community colleges in the state to: 1) transfer students to the universities of their choice; 2) train and retain thousands of students for jobs; 3) provide opportunity and educational excellence in order for students to achieve their hopes and dreams; and 4) to have the support of the community members, including foundation board members. She asked the communities for their continued support and leadership on behalf of the students they represented.

Council Member Freeman noted she was a current student of Foothill-DeAnza Community College, Middlefield Campus. She expressed her appreciation for the atmosphere and the quality of professors at the Middlefield Campus.

No action required.

2. Appointment of Candidates to the Library Advisory Commission

FIRST ROUND OF VOTING FOR THE LIBRARY ADVISORY COMMISSION

VOTING FOR SANDRA HIRSH: Beecham, Burch, Cordell, Freeman, Kishimoto, Kleinberg, Mossar, Ojakian

VOTING FOR LENORE JONES: Beecham, Burch, Cordell, Freeman, Kishimoto, Kleinberg, Mossar, Ojakian

VOTING FOR PAULA SKOKOWSKI: Beecham, Burch, Cordell,
Freeman, Kishimoto, Kleinberg,
Mossar, Ojakian

VOTING FOR VALERIE STINGER: Beecham, Burch, Cordell,
Mossar, Ojakian

VOTING FOR TOM WYMAN: Freeman, Kishimoto, Kleinberg

City Clerk Donna Rogers announced that Sandra Hirsch, Lenore Jones and Paula Skokowski (with eight votes), and Valerie Stinger (with five votes) were appointed on the first ballot to three-year terms ending January 31, 2008.

ORAL COMMUNICATIONS

Aram James spoke regarding cameras in police cars.

Linda Mabry, Erswild Court, spoke regarding the Police Department and their treatment of people of color.

City Manager Frank Benest noted the Police Department had not stopped collecting racial profiling data.

CONSENT CALENDAR

MOTION: Council Member Ojakian moved, seconded by Mossar to approve Consent Calendar Item Nos. 3 and 4.

LEGISLATIVE

3. Resolution 8498 entitled "Resolution of the Council of the City of Palo Alto Amending the Compensation Plan for Police Non-Management Personnel Adopted by Resolution No. 8082 and Amended by Resolution Nos. 8244, 8253 and 8346, to Add the City Of Palo Alto's PERS Choice/PORAC Medical Incentive Plan Through June 30, 2007"

Resolution 8499 entitled "Resolution of the Council of the City of Palo Alto Amending Section 1601 of the Merit System Rules and Regulations Regarding the Memorandum of Agreement Between the City of Palo Alto and the Palo Alto Peace Officers' Association, to Add the City of Palo Alto PORAC Medical Incentive Plan Through June 30, 2007.

ADMINISTRATIVE

4. Amendment No. 1 to Agreement No. C05109546 Between the City of Palo Alto and Economic and Social Opportunities, Inc. (ESO) for \$30,000 in Additional Funding to be Allocated During Fiscal Year 2004/05 Under the Community Development Block Grant Program

MOTION PASSED 8-0, Morton absent.

UNFINISHED BUSINESS

- *5. Public Hearing: Considering a Request by Trumark Companies on Behalf of 928 E. Meadow Partners, et. al. for a Vesting Tentative Map for a Proposed Residential Infill Development Located at 928, 940, and 1180 East Meadow Drive. This Map is Required in Order to Merge Three Parcels (Approx. 4.4 acres) and Create 76 Condominium Units. Environmental Assessment: Categorically Exempt from the California Environmental Quality Act Per Section 15332--Infill Development Projects. Zone District: LM. [04-PM-01]. *(Item continued from 01/10/05)*

**This item is quasi-judicial and subject to Council's Disclosure Policy*

Director of Planning and Community Environment Steve Emslie said the Comprehensive Plan (Comp Plan) Policy L-47 addressed the East Meadow Circle area, which specifically encouraged higher density housing to create a better transition to the existing single-family neighborhoods. The project was located in the LM Zone District, which referenced multi-family development standards for RM-30, and complied in terms of density, coverage and height. A preliminary application was submitted to the Architectural Review Board (ARB) in December 2003, reviewed in June 2004, and approved in October 2004. The item before the Council that evening required a review and approval of the subdivision map findings in the staff report (CMR:140:05). The California Environmental Quality Act (CEQA) provided a number of processes for identifying and disclosing environmental impacts. The categorical exemption used for the proposed project was recently added by the State of California to encourage redevelopment of sites within developed areas using existing infrastructure. In order to make the findings, several studies were required: 1) traffic comparison of trips on a daily basis and during the morning/afternoon peak hour; 2) noise impacts; 3) air quality; and 4) hazardous materials. A soils report was conducted that determined the site was buildable based on the current geotechnical conditions, which were incorporated into the ARB's approval. The proposed project was included in the current nexus study, which would analyze the potential of assessing a fee on the Charleston Corridor to fund improvements.

Planning and Transportation Commissioner Lee I. Lippert relayed to the Council comments made at the Planning and Transportation Commission (P&TC) meeting. He said the project created a transition that was discussed

in the Comp Plan between R1 and the light industrial, and the LM zone. He also noted the project met several important overall Comp Plan goals.

Mayor Burch said the item was quasi-judicial and subject to Council's disclosure.

Council Member Morton said he had nothing to disclose.

Council Member Cordell said she attended a meeting at the request of Robin Yemens, who worked with the developer. She indicated she had learned nothing new.

Mayor Burch declared the Public Hearing open at 7:18 p.m.

Ken Brownlee, 3617 Louis Road, requested the Council withhold the approval of the merged three lots until the plan was significantly reduced in density. While he welcomed the conversion of the light industrial buildings to residential use, he felt that 76 three-story condominiums in his quiet neighborhood of single family homes was excessive.

Garrett Hinds, Trumark Companies, said Trumark had developed high quality, attainably priced neighborhoods in and around the Bay Area for almost 20 years. The developer worked closely with the neighbors and community leaders to create an appropriate housing opportunity. The project was in close proximity to City parks, schools, public transportation, freeway access, and shopping. The current LM zoning allowed for residential use, as well as higher density housing. The site consisted of three existing office buildings totaling approximately 87,000 square feet, of which 900 square feet was presently occupied. The site was 85 percent impervious due to the massive rooftops and surface parking, and was on an existing bus route that ran along East Meadow Drive. The site was surrounded by existing tall mature trees, which would be preserved along East Meadow Drive in keeping with the streetscape feeling, and along the south edge to work as a natural buffer to maintain its setback and the privacy of the six adjacent single-family neighbors. The project did not require any variances and was within the Floor Area Ratio (FAR) guidelines. Each home would have a two-car garage with extra storage, two to three bedrooms, and seven different floor plans ranging from 1,227 square feet to 1,580 square feet. Fifteen percent of the homes (12 in total) would be built and then priced at Below Market Rate (BMR) prices per the Palo Alto Housing Corporation (PAHC). The BMR units would be equally dispersed and fairly represent the mix of each floor plan offered. Aggressive "green building" guidelines had also been established in the project, which would reduce housing expenses for owners, including a photovoltaic system that would reduce homeowner association costs for electricity. Other sustainable applications included recycling the

demolition and construction waste materials, exceeding Title 24 standards by 15 percent, the use of certified lumber products, and meeting all C-3 State and City drainage standards.

Sally Probst, 735 Coastland Drive, expressed support for the proposed project and was pleased to see that the Comp Plan and the Housing Element had a BMR requirement. She commended City staff, the ARB and the P&TC for all their hard work.

Arthur Keller, 3881 Corina Way, said he hoped the developer would contact a number of neighbors whose properties were adjacent to the proposed project. He believed it was a reasonable project; however, he had concerns about traffic. He suggested applying the impact fees towards putting a traffic light at East Meadow Drive and Fabian Way.

Bob Moss, 4010 Orme Street, said he was pleased to hear that a soils analysis would be conducted in Phase Two. He suggested a formal requirement be made for a soils analysis and additional toxic study. He expressed concern about the City ignoring CEQA and not conducting a traffic study. He expressed support for the project, believed it was good use of the site, and was glad to see that the BMR units were typical of the rest of the units and would be dispersed throughout the development.

Jeff Rensch, 741 Chimalus Drive, expressed support for the proposed project with its current density. He urged the Council to vote in favor of the tentative map.

Joy Ogawa, Yale Street, expressed concern that the project had not undergone a thorough environmental checklist review even though hazardous chemicals had previously been used on the site. She concurred that a formal requirement be made for a soils analysis and toxic study.

Mr. Hinds said the Phase One Hazardous Materials Study recognized that hazardous materials were stored at the property for a number of years. Since then, those materials had been cleaned up. He was in agreement that a written requirement for a Phase Two soils analysis study was appropriate and would be conducted if it were deemed necessary.

Council Member Mossar said she understood the individual homeowners would be given the option of having a photovoltaic system upon purchase. She asked how that would be handled for the BMR units.

Mr. Hinds said he had not given it much thought.

Council Member Mossar said it would seem advantageous for someone who was purchasing a BMR unit to have the benefit of a lower utility bill.

Mayor Burch declared the Public Hearing closed at 7:45 p.m.

City Manager Frank Benest said he believed it would be helpful if the City Attorney outlined the decision the Council was required that evening.

City Attorney Gary Baum said the Tentative Map, not the whole project, was the only item before the Council that evening. The Government Code and the Subdivision Map Act statutorily limited under what conditions the Council could deny such a project. Grounds for denial were limited to: 1) whether the proposed map was consistent with the Comp Plan; 2) whether the site was physically suitable for the type of development and density proposed; 3) whether there was a substantial environmental impact that would injure fish or wildlife or their habitat; 4) whether the subdivision was likely to cause serious public health problems; and 5) where there was an issue with public easements.

Vice Mayor Kleinberg asked if the Council were to approve the Tentative Map, was it appropriate and timely to entertain certain requirements.

Mr. Baum said there were a number of restrictions on adding conditions; however, if related to the subdivision map they could be added.

Vice Mayor Kleinberg asked whether the requirement of a soils analysis was appropriate for that evening, or would it come up at a later time.

Mr. Baum said he believed requiring a Phase Two study and an appropriate remediation was acceptable.

Mr. Emslie said that was correct.

Vice Mayor Kleinberg queried whether the timing was appropriate for that evening.

Mr. Baum said yes.

Council Member Morton expressed concern about a traffic light at East Meadow Drive and Fabian Way, and believed it to be a part of the safety and general well being of the community. He asked whether that was going too far.

Mr. Baum said the Council would need to find it was related to a serious public health problem and not a technical issue concerning traffic.

Council Member Morton asked whether it could be approached indirectly if the Council expressed concern or preferences when the item returned to Council.

Mr. Emslie said the project would not return to the Council. Once the Tentative Map was approved, the Council would receive the Final Map for review and approval; however, that would not be an appropriate time to add conditions.

Council Member Morton asked when Council would be able to express concerns to the other review bodies concerns about traffic, height or density.

Mr. Emslie said even if the Council had the ability to condition the project, traffic signals could not be required. There was not a connection between the impacts of the project and the requirement for traffic signals. The project would generate far less traffic than what would be allowed on the site, and the law stated unless there was an impact created directly by the development and was proportionate to the impact, the conditions could not be required. However, there was a safety and improvement plan for moving traffic through the Charleston Corridor. The proposed project was within the study area of the nexus analysis, and could possibly pay a proportionate share to fund the improvements for the Charleston/Arastradero Corridor that addressed safety concerns if staff could make the required findings to recommend there was a link.

Council Member Morton clarified the Council could look to staff to help with the nexus and the wording.

Council Member Freeman said Palo Alto recently added new housing at University South. In addition, the Jewish Community Center (JCC) had new housing in their plans, and new housing was planned in other areas of the City. She asked whether staff had any quantification of the catch-phrase "jobs/housing" imbalance.

Mr. Emslie said the City had a jobs/housing imbalance of more than two jobs for every house. There were a number of projects on the horizon that could provide a better equilibrium in meeting the City's jobs/housing imbalance. He offered to provide the Council with an informational report on the status of upcoming projects, and how they would affect the imbalance.

Council Member Freeman said she did not anticipate a one-to-one ratio for jobs/housing. She asked how the Palo Alto Unified School District (PAUSD) viewed the increase in the number of school-aged students.

Mr. Emslie said all school districts in the State of California were able to set impact fees for growth. Impact fees would be collected for the proposed project and used by the PAUSD to offset impacts to its schools.

Council Member Freeman expressed concern that the PAUSD might not be aware of the proposed project.

Mr. Emslie said he would verify with staff whether the PAUSD received notice.

Vice Mayor Kleinberg said she understood when the Council voted for or against housing, they were not to take into account impacts on schools. She asked if that was correct.

Mr. Baum said the Council could take into consideration the broad context; however, they were limited to the findings. The item could only be denied on the findings. The State statute referred to by the Director of Planning and Community Environment capped the fees for schools at a certain level. The PAUSD raised those fees to the maximum.

Council Member Freeman asked what each housing unit was priced at.

Mr. Hinds said in 2005 dollars they would cost approximately \$700,000 to \$900,000. The BMR units would sell for half of the market rate prices.

Council Member Freeman said she noticed the Tentative Map had private roads on it. She asked staff whether it was common to have private roads in developments.

Mr. Emslie said yes. It occurred most often in developments where Homeowner Association Fees (HOA) maintained the parking and landscaping.

Council Member Freeman clarified the homeowners would have to take care of the internal streets. She said page three of the Tentative Map indicated the Public Utility Easement (PUE) would be abandoned; however, the subsequent page showed new PUE's. She asked who would pay for the new PUE's.

Mr. Emslie said the Tentative Map reflected a change in location of the PUE and all the costs were borne by the developer. The City incurred no costs in the relocation.

Council Member Freeman asked whether the old PUE's would remain or be removed.

Mr. Emslie the old PUE's would be disposed of in a way approved by the City Utilities Department.

Council Member Freeman said when the time came to make a motion she would like to see the approval conditional on the soil analysis in Phase Two with any remediation reported back to staff.

MOTION: Council Member Morton moved, seconded by Kleinberg, to approve the staff and Planning and Transportation Commission (PTC) recommendation to approve the proposed Vesting Tentative Map to merge three parcels (approximately 4.4 acres) and create 76 condominium units, based upon the findings and conditions contained within the Record of Land Use Action (Attachment A of CMR:140:05) with the addition of securing a written soils analysis in Phase Two with the appropriate remediation.

Council Member Morton said he would also like to see an appropriate contribution to the nexus study for a traffic light at Fabian Way and East Meadow Drive. Although some might not consider it a major health hazard, children who got hit at intersections did pose a health issue. The developer enticed the City with the suggestion of some photovoltaic elements; however, it should be required in all of the units, unless the homeowners opted to "elect out" if they did not want it. He suggested adding to the motion a requirement of the developer to include photovoltaic in all the housing units.

Mr. Emslie said the only participation of the project in future improvements on Charleston Road would not be related to a signal on Fabian Way, but would be a proportionate share as determined by the nexus study with fees retroactively applied. The concern about photovoltaic was covered in the ARB's approval, which contained the sustainability conditions and the program outlined by the applicants. The applicant could volunteer to reverse the provision for photovoltaic as suggested by Council Member Morton; however, staff felt the issue had already been covered in the decision of the ARB.

Vice Mayor Kleinberg expressed support for the motion. She noticed the project was not built out to the density that it could have been based on the zoning, and the developer showed restraint and sensitivity to the neighborhood. The City had a requirement and commitment to build more housing in Palo Alto and the proposed project would help in terms of the City's housing element, especially in an area that would be much improved and on the outskirts of residential areas.

Council Member Kishimoto asked whether the soils analysis in Phase Two was a part of the ARB's approval.

Mr. Emslie said no. It was now a part of the motion presently on the table. The Phase One analysis did not recommend going any further.

Council Member Kishimoto clarified the Council would just be approving the Tentative Map, and would not see the project come before them because it was within the zoning guidelines.

Mr. Emslie said that was correct. The entitlements for the major architectural review had been granted and conferred upon the site.

Council Member Kishimoto said a member of the public raised a question about notification to the public, and asked whether proper notification was done.

Mr. Emslie said notification to the public was expanded to double the number of residents. Staff would follow-up to make sure there were not any technical issues that prevented notices from getting mailed.

Council Member Kishimoto asked whether there were any relevant creek setback guidelines for channelized creeks.

Mr. Emslie said the Santa Clara Valley Water District (SCVWD) owned the property including the creek on either side, which contained their access and setbacks. Additional setbacks were not required because adequate room existed within the existing right-of-way.

Council Member Kishimoto asked whether the reason a categorical exemption had not been previously applied in Palo Alto was because it was a fairly new exemption.

Mr. Emslie said yes. A categorical exemption had been instituted within the last three to five years. The proposed project was the first of its kind that met all the criteria.

Council Member Kishimoto expressed overall support for the project. She did not believe, however, the traffic study looked at a hypothetical scenario of what the streets would look like with a Comp Plan build out.

Mr. Emslie said there was good information that related to the site in the environmental documentation for the Charleston/Arastradero Plan, which was conducted less than one-year ago. The proposed project was much less than the assumptions made even with existing conditions. Staff adequately concluded the trips generated on an ideal or peak hour basis involved a fraction of the trips generated from the uses studied in the Charleston/Arastradero Plan or under their full usage.

Council Member Kishimoto said the Comp Plan called for a gradual transition from industrial to residential, especially at the proposed site. While the City

had a parks impact fee, there was not a process in place to allocate land to ensure a neighborhood park. She asked for staff to look into the matter.

Mr. Emslie said staff would rely on the City's land use and advanced planning processes to determine those types of needs, which were generally done in updates of the Comp Plan.

Council Member Kishimoto clarified it could possibly be done when the P&TC did their annual review of the Comp Plan implementation, or perhaps it could be referred by the Council.

Mr. Emslie said that was correct.

Council Member Mossar said although the Council could not condition the photovoltaic issue, she stated a strong preference to have it utilized throughout the project, and thereby not disadvantaging the BMR housing units. She appreciated the fact there was a bus route already in place; however, it underscored the reason why the Council had taken public action to ask for fairly geographically distributed funding from the Santa Clara Valley Transportation Authority (SCVTA). She said if more funds were available for the cities in the North County, perhaps the presently sagging bus route could become more robust and ultimately more usable by the residents of the project. She reminded her colleagues that purchases of land with parks fees would not become commonplace; however, there were things the City could do with the fees to make the City's existing parks more useful and modern.

Council Member Cordell said she hoped when the BMR units were put on the market, the price would be set as low as possible. She believed none of the conditions required to deny the Tentative Map existed. It was: 1) consistent with the Comp Plan; 2) physically a suitable site for the density; 3) demonstrated no substantial environmental damage unless, or until, the soils analysis proved otherwise; and 4) there was no issue regarding a public easement problem. She said the project was well within the set guidelines and she believed approval of the project was warranted.

Council Member Ojakian said there were quite a few vacancies in the industrial park. He asked whether plans were in the works for the industrial park.

Mr. Emslie said there were a number of industrial buildings in the Bay Area that had reached the end of their usefulness. The present trend and turnover made sure there was adequate infrastructure and services. Staff favored development on the west side of the Bayshore Freeway because of its

proximity to City parks, schools, and other services, as opposed to other industrial park areas within the City in more remote locations.

Council Member Ojakian asked whether there were other potential applicants.

Mr. Emslie said staff knew of a number of properties on the market, but had no applicants at this time.

Council Member Ojakian said the project designated an area of the development as the "Reading Room." He asked what the Reading Room would it be for.

Chris Magnussen, Project Manager, said the Reading Room was designed to be an outdoor interpretive area for the residents to mingle with their neighbors, and to enjoy the vegetation.

Council Member Ojakian said essentially it was a public meeting area, but was restricted to the homeowners.

Mr. Magnussen said most likely the homeowners would use the area more regularly; however, there was no restrictive access from persons walking along the public right-of-way.

Council Member Ojakian asked about public art being included in the project.

Mr. Magnussen said the Council did not have the complete set of architectural plans, nor the project materials binder. That information included samples of various types of public art that would be proposed on the site. The applicant retained an artist.

Council Member Ojakian asked whether the Public Art Commission (PAC) would review the various types of public art.

Mr. Magnussen said the Planning staff would be involved with the applicant in more detail upon the building permit review.

Council Member Ojakian expressed his support for the main motion and the idea of the Phase Two soils study. He appreciated the fact the project completed housing on the site all the way to the corner.

Council Member Beecham said there was a misconception that new residents did not pay their fair share within the community. New residents paid the highest amount of property taxes because of Proposition 13. In fact, new residents would pay more in property taxes in the next five years than he

had over the past 25 years. While the City wishes to be environmentally correct and urge people to use photovoltaic, it was not necessarily the correct approach. The Council recently approved contracts for wind power and solid waste power. The City, however, did have a subsidized program within the Utilities Department for the use of photovoltaic.

Mayor Burch said he did not believe the applicant should be required to place photovoltaic on all the units because a number of them might not have the right exposure to make it viable.

Council Member Morton said the motion also included the explicit insertion that the developer would pay the appropriate share of the traffic impact mitigations in the area.

Mr. Emslie said the inclusion to the motion was not needed because it would be determined by the nexus study.

Council Member Morton said sometimes items not included in the motion did not get done. He would like to have it included.

Vice Mayor Kleinberg said she did not believe it was necessary.

Mayor Burch said staff had assured the Council it would be covered if there were an appropriate nexus.

MOTION PASSED 9-0.

REPORTS OF COMMITTEES AND COMMISSIONS



6. Update to the Long Range Financial Plan from the Finance Committee Meeting of December 14, 2004

Council Member Mossar said the Finance Committee unanimously approved the Long Range Financial Plan (LRFP) at its meeting in December 2004.

Director of Administrative Services Carl Yeats said the national economy appeared to be trending upwards with a 3 percent growth in the Gross Domestic Product (GDP) through 2005. Challenges included budget and trade deficits, high oil prices, weakness of the dollar, and rising interest rates, which had nearly doubled over the last seven quarters. On the State economy, unemployment rates had dropped with a 2 percent annual job growth rate through 2006. Challenges included growing State budget deficits and a lack of infrastructure funding. In the time it took to prepare the staff report (CMR:139:05), the State budget deficit had grown from \$5 billion to \$8.3 billion. On the County front, unemployment rates had declined, but job creation was weak and fewer people were employed in June 2004 than in 01/24/05

June 2003. The unemployment rate for Santa Clara County was presently 5.5 percent. Challenges included the State budget deficit. Staff had already seen in Governor Schwarzenegger's proposed preliminary budget, a take away of gas tax revenues and maintenance for other types of projects the State had traditionally funded, such as booking fees and library bond measure funding. In the 2004-05 and 2005-06 fiscal years, Palo Alto would pay into the Education Revenue Augmentation Fund (ERAF) 3, which would result in a reduction in General Fund revenues of approximately \$1.5 million. To date, the City had lost nearly \$38 million in General Fund revenues to the ERAF 3, which began in 1992-93. Since the economic peak of 2000-01, Palo Alto had seen a \$10 million decrease in general tax revenues and an \$8.1 million increase in expenses, Most were in the area of benefits, such as health care and retirement costs, the result was an imbalance of \$18.1 million. In past years, the imbalance had been dealt with through a variety of methods: 1) using the "strengthening the bottom line" approach to reduce the City's budget by 5 percent or \$5 million; 2) eliminating more than 40 positions and restructuring around vacancies; 3) imposing hiring freezes, an employee furlough, and a two-tier retiree medical program; 4) enhancing revenues through the selling of services to other agencies; and 5) extending the replacement life for vehicles and equipment. In spite of the ongoing reductions over the past four years, staff had maintained services, maintained the commitment to the PAUSD of approximately \$6 million per year, and continued the investment in the City's infrastructure. Due to sluggish revenues and escalating benefit costs, the City had been treading water for the past four years.

Deputy Director of Administrative Services Joe Saccio said when staff conducted revenue projections, it typically looked at the historical revenue growth over the past ten years and incorporated any future changes identified, such as the closing of Hyatt Rickey's. Overall, there was a 3.4 percent increase in revenues over the next ten years, which was slightly less than what was projected in 2004. Palo Alto had retreated almost seven years in terms of sales tax and Transient Occupancy Tax (TOT) revenues due to the economic downturn. The forecasted revenue was conservative but realistic given some future known factors, such as the slow job growth and competition from the big-box retail stores and malls.

Budget Manager Charles Perl said the key point to the expenditures was their continued growth over revenues in the next ten years. In looking at the next budget process, it would be important for the City, as well as the next LRFP review, to see that the revenue growth was at, or would exceed, the expenditure growth. Employee salaries were expected to grow a little more than 3 percent over the next ten years, but would remain flat at approximately 45 percent of total expense. Employee benefits, however, were expected to grow at a rate of 6.2 percent, which was a growth from 18

percent to approximately 24 percent of total expense. Over the next ten years, employee salaries and benefits were expected to grow from approximately 63 percent to approximately 69 percent of total expenses. The growth was primarily due to retiree pension contributions, having doubled to \$11 million in the past few years, and health care costs, which had increased by approximately 50 percent or \$10.8 million in 2005. In the next ten years, health care costs were expected to double again. Due to the cyclical nature of the business cycle, staff anticipated a recession to occur in 2010.

Mr. Yeats said Palo Alto was presently looking at a \$1.5 million imbalance for 2004-05. For 2005-06, staff anticipated a deficit of approximately \$5.2 million. If nothing were done to correct the deficit in the next budget cycle or during the 2005-07 budget, the City would face deficit spending for the subsequent nine years. For 2004-05, the shortfall was mainly caused by lower building permit activity, as well as a delay in the Paramedic Basic Life Support (BLS) program. At the time the City's budget was adopted, the State had not adopted its budget, which left a \$500,000 takeaway. In addition, there had been a number of budget amendment ordinances from the City Attorney's office for litigation. Both of those items would be incorporated into the mid-year budget. The 2005-06 shortfall was primarily caused by: 1) lower building permit fees; 2) a delay in full implementation of the paramedic program; 3) lower sales and TOT tax revenues; 4) additional State takeaways of approximately \$500,000; 5) an increase in the California Public Employees Retirement System (CALPERS) retirement rates of approximately \$1.3 million; and 6) funding for the Technology Fund. Staff made a commitment to the Council they would continue to fund the City's infrastructure at a certain level. More had been funded in certain years than the target of \$2 million per year. For the next few years, including the current year, staff would not be able to make that commitment because of an insufficient surplus of revenues over expenditures. At the end of the 2005-07 budget cycle, the goal was to have enough savings to begin the process of refunding infrastructure into the future. Currently, the General Fund was subsidizing or transferring funds to the Storm Drain Fund at approximately \$800,000 per year. If the Storm Drain Fee did not increase, that trend would continue. The \$800,000 was built into the LRFP. The State's financial condition was forever changing. The passage of Proposition 1A gave the City a little breather; however, it was anticipated the State would become more creative in how local governments were funded. In 2013, the Refuse Fund would cease paying rent on the landfill, which was approximately \$4.5 million. In the long-term, as staff looked at funding strategies, a revenue source would be needed to fill that gap in 2014.

City Manager Frank Benest said because there was not one overall solution to solve the problem, staff anticipated doing a variety of things and coming

up with a package to balance the City's budget and reduce the structural deficit of \$5.2 million, which did not include any funding currently being discussed in negotiations with the hourly employee unit. Staff developed a "hard" hiring freeze, and new positions were not being approved unless it was a public safety position related to minimal staffing or certain enterprise or utility fund positions. As vacancies occurred, restructuring around those positions would continue. There were very few things left to do without cutting services and implementing layoffs. Most of the 40 positions eliminated were in the administrative support or management realm.

Council Member Morton asked whether the projected \$1.5 million imbalance in the previous two-year budget cycle was after the \$2 million transfer to the infrastructure and after the State budget.

Mr. Benest said once the Infrastructure Reserve Fund (IRF) was shifted into the Capital Projects Fund (CPF), it provided \$1 million of infrastructure funding through interest earnings. In the General Fund outside of the CPF, was the \$5.2 million deficit.

Council Member Morton said the fund itself had generated its own million dollars, and the budget for 2005 would not include a transfer.

Mr. Benest said that was correct. In past years, at least \$2 million had been contributed to the IRF, even in tough times. In order to make the annual contribution in 2005, staff hoped to make additional monies through savings throughout the year.

Council Member Morton said staff had been more than successful in funding the IRF, when the City had been treading water. He found it remarkable that in the past four years in Palo Alto more could be put into the IRF than was budgeted.

Mr. Benest said he agreed staff had done an excellent job in that regard.

Council Member Morton asked about the shortfall with respect to building permit fees. He said, as with many of the City's fees, the hope was to recover staffing costs. However, when the number of applications for home improvements dropped, costs were not necessarily cut proportionately. He asked whether it was something that could be looked at in the coming year.

Mr. Yeats said it would be reviewed during the budget cycle. The goal was for 100 percent cost recovery. Staff would also explore whether there was a trend whereby the number of permits had slowed down. If so, then related costs would also need to be looked at.

Council Member Morton asked whether the long-term deficit projection included a continuous contribution of \$1 million until the Storm Drain Fee passed.

Mr. Yeats said yes. There was a funding program in place to repay the City's Storm Drain Fee of approximately \$3 million.

Council Member Morton said Governor Schwarzenegger had plans to take on the defining benefit commitment that most public entities had made. He asked if Palo Alto had the ability to move from a defined benefit to a defined contribution or a 401K model, and did staff envision whether it would impact the City's commitment.

Mr. Yeats said it would be much like the two-tier system already in place for the retiree medical benefit. Anyone who became employed with the City after a certain date had a different type of benefit.

Council Member Morton clarified the defined contribution would not help with the City's existing contractual commitments.

Mr. Yeats said that was correct.

Council Member Morton said it only enabled the City not to have them grow quite as fast as they would otherwise.

Mr. Yeats said the chart on Public Employees' Retirement System (PERS) baseline indicated a number of years where the contribution rate was zero. While there was presently much discussion on the issue, it was something that had been going on for a number of years. He believed PERS was in the process of changing investment strategies, which would allow for longer term growth at much more moderate rates than in the past.

Council Member Kishimoto asked whether the \$1.5 million deficit for 2005-07 included the transfer to the Storm Drain Fund.

Mr. Benest said after the transfer of money to the CPF, there was still a \$1.5 million deficit in the General Fund. Staff planned to submit a proposed solution to the problem to Council at mid-year.

Council Member Kishimoto asked whether staff had looked into a "Part B" to the Environmental Services Center (ESC), which the Refuse Fund had not paid rent on.

Mr. Benest said staff would have a definitive answer on the issue at the Council meeting of February 14, 2005.

Council Member Kishimoto said one of the fundamental problems was the ongoing shift in the composition of the economy from tangibles to services. She believed in order to have a fair tax base that would not be burdensome on those being taxed, staff needed to figure out a way, while working with the State, to shift Palo Alto's tax base to a broader service base.

Mr. Benest said Palo Alto's tax system was completely outmoded, and was not based on the present economy.

Council Member Kishimoto said not only should staff look at what services could be cut, but also they should make a concerted effort to look at efficiencies and alternatives in service delivery when looking to develop the next two-year budget.

Council Member Freeman said it was noted in the LRFP regarding Storm Drains, that if the fee increase was not approved, no capital work would be completed and resources would continue to be diverted away from General Fund services to support Storm Drain operations. She asked whether it was fair to say that although there was no set figure, it was in staff's thinking as the budget was being developed.

Mr. Benest said currently the City spent approximately \$800,000 for basic operations and maintenance for the Storm Drains. Without the fee increase, that figure would grow over time. Should the fee increase be approved, the City would take the \$800,000 to use to prepay and jump-start the program, while the new fee would continue to cover basic operations and maintenance.

Council Member Freeman asked whether the \$1.5 million shortfall included the \$800,000.

Mr. Benest said yes. The \$5.2 million deficit included the continuing contribution to the Storm Drain Fund.

Council Member Freeman asked depending on the upcoming Storm Drain election, how would the money shift for the Storm Drains.

Mr. Benest said because the \$800,000 was part of the overall Storm Drain solution, it would not reduce the City's deficit.

Council Member Freeman said major facility projects, such as the renovation or replacement of the Municipal Services Center (MSC), and the expansion of the new police space were wonderful to have, but were not fully approved as yet.

Mr. Benest said staff's perspective was to advise the Council of the major project needs; however, they were aware any new projects would need their own revenue source because General Fund dollars were not available.

Council Member Freeman said she appreciated the variety of options presented by staff. She expressed concern the City's largest expenditure was salaries and benefits, which was presently at 63 percent and climbing to 70 percent of the General Fund.

Mayor Burch believed Council Member Freeman's comments would be fully vetted at the Council Retreat scheduled for January 29, 2005.

Council Member Freeman said staff was using money that was frozen for projects, which meant it was not a reduction.

Mr. Benest said staff utilized the money from frozen positions to solve the current year's deficit. Staff was very interested in saving as much as possible through the freeze to deal with the deficit. When looking at service reductions and layoffs for 2005-07, staff anticipated looking at the frozen positions for possible inclusion in the layoffs.

Council Member Freeman said while she sat on the Finance Committee for a number of years, she did not understand the difference between frozen and eliminated positions in terms of where the money was being used. She requested to make a motion.

Mayor Burch said there was no motion to be called for. The item was presented for advisory purposes only.

Council Member Cordell said given the dire situation the City was in, there were two ways in which to fix things. One was to deal with the status quo, which included hiring freezes and layoffs, and the other was to find ways to still increase revenue. She asked whether there would be a discussion at the Council Retreat about increasing revenues. She also noted she reviewed the Auditor's Report of April 2004, "The Audit of Restructuring Efforts and Management Span of Control", and asked whether the matter of span of control would be on the table for discussion at the Council Retreat.

Mr. Benest said the Council in the past three years had authorized the following committees: 1) Committee on Enhancing the Economic Base; 2) Ad Hoc Committee on Retaining Palo Alto's Retailers; and 3) Ad Hoc Committee on Attracting New Retail Businesses and Sales Tax. The Council's recent action for the auto overlay district was a first step towards looking at one of the City's major revenue producing sectors, and how to support them. Staff believed there were opportunities to look at span of control; however, it was

not realistic, as indicated by comments in response to the City Auditor's Report, to increase them at will. In the Police and/or Fire Departments, there might be one span of control; however, in other situations the span of control could be larger. Staff would continue to look for ways to restructure and increase the span of control, but in a less mechanistic process.

Council Member Cordell asked whether the topic of span of control was off the table for discussion at the Council's Retreat.

Mr. Benest said he welcomed discussions on the topic.

Council Member Beecham said he was pleased by staff's presentation, agreed with the projections, and believed there were no sacred cows in the community. He looked forward to staff's recommendation on the LRFP.

Council Member Ojakian said at one point in staff's presentation it was said that sales tax had stabilized, while the TOT had risen slightly. Yet, the power point slide showed \$600,000 in reductions. He believed there should be a healthy discussion about why money was being put in the Technology Fund.

Council Member Freeman said she would like to see staff quantify the staffing issue.

No action required.



7. Finance Committee Recommendation regarding Criteria for Prioritization of Services from Finance Committee Meeting of December 14, 2004

City Manager Benest said over the past four years, the City had utilized a variety of solutions and strategies to balance the budget without significant impacts on service levels. Based on the continuing trend of General Fund operating deficits, staff recommended that a methodology be developed to provide a prioritization of Citywide services and service levels. The Finance Committee reviewed and commented on the Program/Tier Table in the staff report (CMR:515:04), and recognized the complexity and difficulty in developing a prioritization of General Fund services with the goal of reducing service levels or expenses to meet projected deficits identified in the LRFP. In reviewing the Program/Tier Table, the Committee made several suggestions and those were incorporated into the revised table. Of particular concern to the Committee, was the broad category of "Essential Services (encompassed Health and Safety and Legal Mandate)," which had now been separated into two categories, "Legally Mandated" and "Health and Public Safety." In addition, the Committee stated the category "Comprehensive Plan Policy or Program" was too broad, in that it encompassed almost

everything the City did. That category was eliminated. Finally, the Committee recommended the category "Program targets children/teens/seniors" be modified to include the phrase "at-risk" after the word "targets." The Committee recommended full Council review of the Program/Tier Table on January 24, 2005, in order to focus discussion at Council's January 29, 2005 retreat.

Council Member Morton said he was surprised that "Revenue Generating/Self Supporting" criteria were listed as Tier Two. If the City could not get things to generate more revenue or become self-supporting, then there would not be any money to solve some of the other problems.

Mr. Benest said that was a reasonable position, and could be moved up if a majority of the Council agreed.

Council Member Kishimoto clarified the criteria for prioritization was an ongoing interim process, and the Council was not locked into anything.

Mr. Benest said that was correct. It was a typical way of having a rational basis for ordering services or getting some type of idea on what was more or less important.

Council Member Kishimoto said she was unsure whether "Enhances Productivity/Customer Service" would apply to an entire program area, such as the investment the Community Services Department (CSD) made in automating the class registration. She was also unsure whether it was a program that could be ranked or worth the investment to save money in the long term.

Mr. Benest said one example was the self-service technology at the library. It was a productivity enhancement to promote customer service. Another example was the Information Desk in the lobby of City Hall.

Council Member Kishimoto asked whether the criteria would also be applied to Capital Improvement Projects (CIP's).

Mr. Benest said it was for General Fund services and programs. The staffing committed to the General Fund CIPs should be in the prioritization. To the extent that one of Council's Top 5 Priorities was Infrastructure/CityWorks, then staffing related to the General Fund CityWorks program would be listed in Tier Two.

Council Member Kishimoto said it made sense to her that "Enhanced Productivity" or service delivery should fall in Tier Two. She clarified that whichever tier a program went into, they were subject to cost effectiveness.

Mr. Benest said yes. Just because a program or service was in the top tier did not mean it was a sacred cow. There were legally mandated and health and safety programs where Palo Alto spent more than minimally required by law.

Vice Mayor Kleinberg said she was unsure whether the criteria listed and program tiers were meant to be as general and vague as they sounded to her. She asked what types of decision points were made using the listed terminology.

Mr. Benest said in his previous experience using the same type of program tier table, the ranking of adult recreation programs fell to the bottom of the list. Although the Council would not be able to arrive at a quantitative formula that led to where cuts could be made, it would provide a basis for making certain judgments.

Vice Mayor Kleinberg said it would be helpful to have an understanding of the consequences in the way of scenarios.

Mr. Benest said staff had put together a matrix that looked at service impacts.

Vice Mayor Kleinberg said if the Council had to decide where priorities should be in the Program/Tier Table, then she would like to know where the City was. As an example, if affordable housing was something that had become routine, did it qualify as a priority.

Mr. Benest said part of his presentation at the Council Retreat would focus on the amount and intensity of the staff effort currently versus previously.

Vice Mayor Kleinberg clarified the criteria was based on a set of surveys that were done.

Mr. Benest said no. When staff presented its prioritization of services, it would be based on two things: 1) data from a citizen's survey collected a few year's prior; and 2) a ranking of programs based on the eventual criteria that Council would help develop.

Council Member Beecham said although he had no idea how the criteria for prioritization would work out, he was willing to go through the process. Council would have control and ultimately make the final decision.

Mayor Burch said he looked forward to a healthy discussion, and believed it would prove valuable.

No action required.

COUNCIL COMMENTS, QUESTIONS, AND ANNOUNCEMENTS

Council Member Mossar noted the Council had received an unfortunate letter from the Silicon Valley Manufacturing Group (SVMG) related to the set policy of the Palo Alto City Council. She requested the Mayor respond to the SVMG and include copies of letters stating the Council's policy on the funding approach of the Valley Transportation Authority (VTA) noting that VTA should be more geographically fair. She also noted Council Member Kishimoto had carried forward the City Council's position.

Council Member Ojakian stated he sat on the VTA Policy Advisory Board and had requested the SVMG be notified that Council Member Kishimoto represents the policies of the City of Palo Alto. Also, the other 15 members on the Board recently elected Council Member Kishimoto Chair for 2005.

Council Member Morton noted his appreciation for Mayor Burch's tactful approach to the press on recent issues.

Council Member Cordell said Tom Wyman should be acknowledged for his time and energy given to the City on the Library Advisory Commission (LAC).

Mayor Burch noted selection of LAC members was a very difficult decision as all candidates were very well qualified.

Council Member Freeman spoke regarding the recent instances of police handling of racial issues.

City Manager Frank Benest noted, based upon his discussions with Council Members, that he would join Police Chief Lynne Johnson at the next Human Relations Commission (HRC) meeting concerning those issues.

Council Member Kishimoto thanked her colleagues for their support regarding the recent correspondence from the SVMG. She also referred to the report on the Lytton Plaza Improvements clarifying the City was the applicant, and the Public Art Commission was looking forward to reviewing the public art aspect of the project.

Mayor Burch announced the Bay Area Water Supply and Conservation Agency (BAWSCA) elected Bern Beecham as the Chair.

Council Member Beecham corrected the impression of an earlier speaker regarding the "Friends of the Police" by stating Police Chief Lynne Johnson did not initiate the "Friends" group.

CLOSED SESSION

The meeting adjourned at 10:00 p.m. to a Closed Session.

8. CONFERENCE WITH LABOR NEGOTIATORS (Hourly Employees Unit)
Agency Designated Representatives: City Manager and his designees pursuant to the Merit System Rules and Regulations (Frank Benest, Leslie Loomis, Richard James, Glenn Roberts)

Employee Organization: Local 715, Service Employees' International Union, AFL-CIO, CLC

Authority: Government Code section 54957.6(a)

The City Council met in Closed Session to discuss matters regarding labor negotiations, as described in Agenda Item No. 8.

Mayor Burch announced there no reportable action was taken.

FINAL ADJOURNMENT: The meeting adjourned at 11:00 p.m.

ATTEST:

APPROVED:

City Clerk

Mayor

NOTE: Sense minutes (synopsis) are prepared in accordance with Palo Alto Municipal Code Sections 2.04.180(a) and (b). The City Council and Standing Committee meeting tapes are made solely for the purpose of facilitating the preparation of the minutes of the meetings. City Council and Standing Committee meeting tapes are recycled 90 days from the date of the meeting. The tapes are available for members of the public to listen to during regular office hours.