BUDGET
’04 – ‘05

TO: HONORABLE CITY COUNCIL
FROM: CITY MANAGER DEPARTMENT: ADMINISTRATIVE SERVICES
DATE: JUNE 28, 2004 CMR:316:04
SUBJECT: ADOPTION OF THE 2004-05 BUDGET AND APPROVAL OF A BUDGET ADOPTION ORDINANCE, INCLUDING THE 2004-05 CAPITAL IMPROVEMENT PROGRAM, CHANGES TO THE MUNICIPAL FEE SCHEDULE, UTILITY RATES AND CHARGES, AND CHANGES TO COMPENSATION PLANS

RECOMMENDATION
Staff recommends that the City Council approve the following:

1. The Budget Adoption Ordinance (Attachment 1), which includes:
   a. The City Manager’s Proposed 2004-05 Budget (Exhibit A - previously distributed).
   b. All changes detailed in the Amendments to the City Manager’s Proposed 2004-05 Budget (Exhibit B).
   c. Proposed 2004-05 Municipal Fee Schedule (Exhibit C - previously distributed).
   d. Revised pages to the Table of Organization (Exhibit D).
   e. Amendments to the Proposed 2004-05 Municipal Fee Schedule (Exhibit E).

2. Resolution Amending Utility Rate Schedules to affect an electric rate increase (Attachment 2). Please note the effective date of this rate increase will need to be included in the Council motion.

3. Resolution Amending Utility Rate Schedules to affect dark fiber licensing rate changes (Attachment 3).

4. Resolution Amending Utility Rate Schedules to affect a gas rate increase (Attachment 4).
5. Resolution Amending Utility Rate Schedules to affect a wastewater collection rate increase (Attachment 5).

6. Resolution Amending Utility Rate Schedules to affect a water rate increase (Attachment 6).

7. Resolution Amending Utility Rate Schedules for various refuse service rates (Attachment 7).


BACKGROUND
The City Manager’s 2004-05 operating budget was approved in-concept by the City Council on June 16, 2003 (CMR:316:03). An updated operating budget was submitted to the Council on May 4, 2004, and the 2004-05 Proposed Capital Budget was submitted a week later on May 11, 2004. During the month of May and early June, the Finance Committee held hearings and reviewed the Proposed Budget, including the General Fund and Enterprise Fund Capital Improvement Programs and the Municipal Fee Schedule. 2004-05 is the second year of the City’s two-year budget process, therefore the focus of the document and public hearings were on the changes to the in-concept plan approved a year ago. Along with the seven public hearings held in 2003, four additional hearings were held in 2004 on May 4, 11, 18 and June 1, and included 12 hours of committee review and discussion of the City’s operating and capital expenditures. The Finance Committee also reviewed several proposed rate adjustments within the Enterprise Funds. As a result of the hearings, the Finance Committee and staff have recommended changes to the Proposed Budget (Exhibit B).

DISCUSSION
This staff report focuses on the financial changes recommended by the Finance Committee and the adjustments suggested by staff that have a fiscal impact. A wrap-up memorandum was presented to the Finance Committee on May 18, 2004, describing changes made to-date to the City Manager’s Proposed 2004-05 Budget (Appendix 5).

The following are a list of follow-up items that, while not approved by a Finance Committee motion, staff has promised to report back on during the 2004-05 fiscal year.
• The City Manager will return to the Finance Committee in September 2004 with an informational item describing the long-range plan for the External Services Fund.
• In the future, the City Manager will more formally present the Planning Commission recommendations on the Proposed Capital Improvement Plan to the Finance Committee.

Finance Committee-Recommended Changes to the City Manager’s Proposed Budget

• The 2004-05 Council Contingency has been allocated as follows:

1. **Reinstate College Terrace Library hours** – During the Finance Committee meeting held on 5/29/03, $12,000 was allocated to the Library Department budget in 2004-05 to support the current five-day staffing level.
2. **Downtown Lights** – Although the Finance Committee committed contingency fund support for downtown holiday light maintenance, the Public Works Department has subsequently reallocated $7,500 in non-salary operating funds for this service. No contingency funds will be used for this purpose in 2004-05.
3. **Human Services Resource Allocation Process (HSRAP)** – During the Finance Committee meeting held on May 18, 2004, $75,000 of additional one-time funding requests were granted to the following HSRAP agencies: Adolescent Counseling Services ($15,000), La Comida Senior Nutrition ($35,000), and Urban Ministry of Palo Alto’s Hot Meal Program ($25,000). The Urban Ministry funding of a seventh weekly meal represents an increased service level funded by the City. Permanent funding of this additional meal will need to be requested in future years, as this is a one-time item for 2004-05 only. The other items do not represent increased service levels.

<table>
<thead>
<tr>
<th>2004-05 Council Contingency</th>
<th>2004-05</th>
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</thead>
<tbody>
<tr>
<td><strong>Beginning balance</strong></td>
<td>$285,000</td>
</tr>
<tr>
<td>Library – restore College Terrace Library hours</td>
<td>($12,000)</td>
</tr>
<tr>
<td>CSD – Adolescent Counseling Services; additional one-time funding</td>
<td>($15,000)</td>
</tr>
<tr>
<td>CSD – La Comida Senior Nutrition; additional one-time funding</td>
<td>($35,000)</td>
</tr>
<tr>
<td>CSD – Urban Ministry of Palo Alto – Hot Meal Program; additional one-time funding</td>
<td>($25,000)</td>
</tr>
<tr>
<td>PWD – Banners / Downtown Tree Lights</td>
<td>($0)</td>
</tr>
<tr>
<td><strong>Ending Balance</strong></td>
<td><strong>$198,000</strong></td>
</tr>
</tbody>
</table>
• Funding of catering expense council meetings – As a result of the motion, $2,500 was added as ongoing expense to City Council general expense budget for council meeting meals.

Capital Budget
• Internet Site Upgrade (TE-05003) – As a result of the motion by the Finance Committee on May 11, 2004, staff proposes a $240,000 capital project in 2004-05, to upgrade the City’s current internet site and search engine (appendix 4). This additional Technology Fund project will delay other projects due to limited staff resources, including: Human Resources Class Registration system; Operating System Standardization project; SAP training program; and SAP’s Employee Self Service system.

Staff-Recommended Changes to the City Manager’s Proposed Budget
Reserve Policy Revisions
One of the City Auditors’ recommendations from the 2002 Long Range Financial Plan, was to relocate the Infrastructure Reserve (IR) from the General Fund (GF) to the Capital Fund. The text of the recommendation is as follows:

Recommendation #2: To simplify tracking infrastructure funds, we recommend staff assess the feasibility of (1) moving the Infrastructure Reserve from the General Fund to the Capital Projects Fund, and (2) retaining unspent project funds in the Capital Projects Fund.

The main operational challenge with this recommendation surrounds the loss of interest income within the General Fund, and the necessary budget balancing efforts it presents. Staff has incorporated an estimated $1 million interest income shift to the IR for 2004-05, as the IR will have an estimated balance of $30 million when it is moved to the Capital Fund. This interest income will fund half of the current $2 million annual transfer from the General Fund to the IR for future Infrastructure Management Plan (IMP) capital expense.

A reserve policy change is needed to guide operations as of July 1, 2004, for several reasons:
• To establish a Capital Fund reserve policy prior to the IR transfer
• To appropriately accrue interest income
• To retain unspent project monies within the IR
• To define the target reserve level for the Budget Stabilization Reserve (BSR) rather than a floor/ceiling approach
The City Manager will continue to state the BSR target (currently 18.5 percent) during the annual budget process and will continue to observe the 15 – 20 percent range as the acceptable reserve funding levels. However, with the relocation of the IR to the Capital Fund, the General Fund no longer has a reserve for yearend net fund balance (savings) to reside. The balance of the BSR will be reported quarterly to the Council, at which time direction can be made to transfer fund balance if reserves exceed acceptable levels.

On June 1, 2004, a revision to the City’s Reserve Policy was presented to the Finance Committee (Appendix 5) and is being forwarded for City Council review with a 2-2 recommendation.

General Fund:
Community Services
- As part of a continued effort on restructuring, two staff members responsible for Infrastructure Management Plan (IMP) oversight, specifically for parks, medians and open space, are being transferred to the Public Works Department in 2004-05. This change centralizes contracting and administrative functions, while leveraging resources of the City’s professional engineering staff.

Capital Fund
The Finance Committee approved seven changes to the 2004-05 Capital Budget on May 11, 2004. Amended pages to the capital budget document are attached (Appendix 3), and funding adjustments have been incorporated into the associated financial summaries. The following are the amended projects within the Capital Fund:
- **Arastradero Preserve Gateway (PE-05300)** - Staff proposes additional funds of $21,501 be used to fund additional contingency costs related to the contract for building the Gateway Facility. Grant revenues fund this expense.
- **Police Building Project (PE-98020)** – Additional proposed funding of $75,000 for City staff support to complete the schematic design phase of this project. The Infrastructure Reserve funds this expense.

Other CIP
- **Enterprise Resource Planning (TE-02016)** – Project funding of $0.7 million is removed from the 2004-05 proposed budget due to delay in SAP phase III.
- **Permit Information Tracking System (TE-95016)** – Project funding of $0.1 million is removed from fiscal 2006-07 as funding is not needed in that year.
- **Telephone System Replacement (TE-00010)** – Project funding of $0.1 million is removed from fiscal 2007-08 and 2008-09 as funds are not needed in those future years.
- **New Housing Development (SR-01053)** – Project funding of $71,173 is removed from the 2004-05 proposed budget, to match the Finance Committee recommended funding of $409,312.
Enterprise Funds
In response to an inquiry by the Finance Committee on May 18, 2004, the City of Palo Alto Utilities (CPAU) Rate Assistance Program (RAP) is expected to grow by 9.5 percent to $289,000 in 2004-05 as a result of the proposed electric, gas and water rate increases. 953 customers are expected to participate in RAP over the period.

Electric Fund
- **Baylands Undergrounding (EL-02009)** – Additional proposed funding of $150,000 from Electric Fund Rate Stabilization Reserve to be used for undergrounding the overhead electric, telephone, and cable TV facilities on Harbor Road from the entrance of the Baylands Park to the Interpretive Center.
- **Relocation – Alma Substation (EL-05003)** – An additional 2004-05 Electric Fund capital project is proposed for engineering design related to relocation of the Alma Substation to the Quarry Substation site (Appendix 3). Project expense is estimated to be $0.5 million in 2004-05. Please refer to CMR:298:04 for more information related to this item.
- **Proposed 8.5 percent Electric Rate Increase** – The Finance Committee recommends the proposed 8.5 electric rate increase become effective on January 1, 2005. This is six months later than the staff recommended July 1, 2004 effective date. The Resolution amending the electric rates (Attachment 2) has an open-ended effective date, therefore, the Council motion regarding this proposed rate increase will need to specify the relevant effective date.

Water Fund
- **Reduce Water Commodity Purchase Budget by $0.7 million** – Lower water rate projections by the Bay Area Water Supply and Conservation Agency (BAWSCA) will result in a 9 percent reduction in water purchases to $7.6 million. This lower expense has been incorporated in the rate model proposed for 2004-05.

Refuse Fund
- **Cart Exchange Fee of $15** – On the proposed refuse rate schedule R-1 (Attachment 7), effective 7/1/04, the Finance Committee requested follow-up on the need for a $15 cart exchange fee. The following are reasons cited for the new fee:
  - Residents allowed to change carts once per year for free
  - Variable can rate remains in effect, keeping the incentive with the customer to reduce service levels
  - 37 percent of the calls received from the pilot area were related to cart exchange
  - Minimizes cart inventory and program expense
  - Recovers costs associated with service level
Storm Drainage Fund

- *Removal of Debt Refinancing Savings of $50,000* – Recent market interest rate changes may postpone the refinancing of 1995 debt during the 2004-05 period. Any cost savings realized from refinancing activity will be directed towards capital expense.

Special Revenue Funds

On May 18, 2004, the Finance Committee approved the addition of $100,000 within the Residential Housing Fund to provide funding for a contribution to the Santa Clara County Housing Trust in 2004-05. The City contributed $500,000 to the trust in 2002, with the stipulation that the funds would be spent in Palo Alto. Two sizeable grants have been received from the trust since this original contribution: Oak Court and the Opportunity Center. Other cities have committed to providing additional trust funding during this recent funding drive.

Compensation Plans

Several classification changes are proposed in the Management and Professional, Classified, and Fire Safety Compensation Plans (Attachments 8, 9, 10). New or amended classifications are further described in the departmental and Table of Organization sections of the budget document.

Table of Organization

Amended pages to the proposed 2004-05 Table of Organization are included with this report (Exhibit D). These pages reflect a reconciliation of reallocated staffing costs with the SAP position control system that have occurred since the proposed budget was produced. The majority of the changes involved Public Works Department enterprise staff allocations. There is no change to budgeted staffing costs as a result of these amendments.

Implementing the payroll and human resources modules of SAP in December 2003 has moved the City to a model whereby staffing costs are allocated based on budget. Employee productivity has improved as a result of reduced administrative burden of tracking hours worked; only hours that vary from the plan are recorded.

Municipal Fee Schedule

*Performance Permit Fee* – The Community Services Department proposes to charge a permit fee for participation in the Arts & Culture sponsored concert series (Exhibit E). This item was presented to the Finance Committee on May 18, 2004.

*Returned Check Fee* – The Administrative Services Department proposes to increase the returned check fee from $10 to $35 to more accurately recover costs associated with processing returned checks (Exhibit E). This change will increase fee revenue by
approximately $7,500 per year. This item was presented to the Finance Committee on June 1, 2004.

Contract Scopes of Professional Service Agreements Greater than $65,000
In the 2003-05 budget cycle, staff provided Council with the contract scopes of professional services agreements greater than $65,000 (CMR:321:03). During the 2004-05 budget cycle, Infrastructure Management Plan project Photovoltaic Design and Installations (PE-05001) is proposed for the 2004-05 capital plan. This additional scope was presented to the Finance Committee for review on June 1, 2004 (Appendix 6).

RESOURCE IMPACT
The 2004-05 Proposed Budget as submitted to the Finance Committee resulted in a $0.8 million increase to the General Fund Budget Stabilization Reserve (BSR) in 2004-05. The changes resulting from the Finance Committee hearings and staff recommendations resulted in no significant change to BSR funding (Appendices 1 & 2). The projected 2004-05 ending balances for the BSR and IR are $21.5 million and $27.2 million respectively. Additional changes to the Enterprise Funds result in an approximate $0.5 million overall increase in reserve balances in 2004-05 from the proposed document.

POLICY IMPLICATIONS
Adoption of this ordinance will revise the Council-directed reserve policy by removing the current 20 percent cap on the General Fund’s Budget Stabilization Reserve, and establishing the Capital Fund Reserve policy. Both of these changes are prompted by the planned relocation of the Infrastructure Reserve to the Capital Fund in 2004-05.

ENVIRONMENTAL REVIEW
Adoption of the budget does not represent a project under California Environmental Quality Act (CEQA).

ATTACHMENTS
Attachment 1: Budget Adoption Ordinance with the following Exhibits:
   Exhibit A: City Manager’s Proposed 2004-05 Budget
   Exhibit B: Amendments to the City Manager’s Proposed 2004-05 Budget
   Exhibit C: Proposed 2004-05 Municipal Fee Schedule
   Exhibit D: Revised Pages in the 2004-05 Table of Organization
   Exhibit E: Amendments to the 2004-05 Proposed Municipal Fee Schedule

Attachment 2: Resolution of the Council of the City of Palo Alto Amending Utility Rate Schedules E-1, E-1-G, E-2, E-2-G, E-4, E-4-G, E-4-TOU, E-7, E-7-G, E-7-TOU, E-14, E-16, E-18, and E-18-G of the City of Palo Alto Utilities Rates and Charges Pertaining to Electric Rates
(Please note the effective date of the electric rate increase will need to be included in the Council motion.)

Attachment 3: Resolution of the Council of the City of Palo Alto Adopting Revised Utility Rate Schedule EDF-1 of the City of Palo Alto Utilities Rates and Charges Pertaining to Dark Fiber Licensing Services

Attachment 4: Resolution of the Council of the City of Palo Alto Amending Utility Rate Schedules G-1, G-2, G-6, and G-10 of the City of Palo Alto Utilities Rates and Charges Pertaining to Gas Rates

Attachment 5: Resolution of the Council of the City of Palo Alto Amending Utility Rate Schedule S-2 of the City of Palo Alto Utilities Rates and Charges Pertaining to Wastewater Collection Rates

Attachment 6: Resolution of the Council of the City of Palo Alto Amending Utility Rate Schedules W-1, W-2, W-4, and W-7 of the City of Palo Alto Utilities Rates and Charges Pertaining to Water Rates

Attachment 7: Resolution of the Council of the City of Palo Alto Amending Utility Rate Schedules R-1, R-2, and R-3 of the City of Palo Alto Utilities Rates and Charges Pertaining to Refuse Collection

Attachment 8: Resolution of the Council of the City of Palo Alto Amending the Compensation Plan for Management and Professional Personnel and Council Appointed Officers Adopted by Resolution No. 8353, and Amended by Resolution No. 8378, to Amend One Classification and add two New Classifications


Attachment 9: Resolution of the Council of the City of Palo Alto Amending the Compensation Plan for Classified Personnel (SEIU) Adopted by Resolution No. 8056, and Amended by Resolution Nos. 8059, 8141, 8180, 8242, 8251, and 8313 to Add Two New Classifications

Exhibit A: 2004-05 Compensation Plan Changes for SEIU Personnel

Attachment 10: Resolution of the Council of the City of Palo Alto Amending the Compensation Plan for Fire Department Personnel (IAFF) Adopted by Resolution No. 8362, to Change One Employee Classification, and to Add One New Classification

Exhibit A: 2004-05 Compensation Plan Changes for IAFF Personnel
Appendix 1: 2004-05 General Fund Summary and Reserve Balances

Appendix 2: 2004-05 Utility Fund Summary and Reserve Balances

Appendix 3: Capital Improvement Fund Summaries and Amended Projects

Appendix 4: May 18, 2004 Memorandum to Finance Committee detailing changes to 2004-05 City Manager’s Proposed Budget to date

Appendix 5: 2004-05 Proposed Reserve Policy Revisions

Appendix 6: 2004-05 Contract Scopes of Professional Service Agreements Greater than $65,000


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