City Manager's Budget Message
Martín Bernal

May 30, 2013

To the Honorable Mayor and Members of the City Council

Staff is pleased to deliver the Proposed Fiscal Year 2014 Annual Budget for the City of Santa Cruz. More than a collection of figures, this budget reflects the Council's strategic goals and is intended to serve as a policy document, a financial plan, a communications device, and an operational guide.

Last year's budget message focused on the City's "Path to Fiscal Sustainability." I am pleased to report that we have successfully followed that path. We expect to complete the current fiscal year with a General Fund surplus of nearly $1.5 million.

Thanks to the talent, creativity, and sacrifice of our employees, this is the fourth consecutive year that the City has ended the year in the black. Unlike the previous three budget surpluses, this year's returns relied less on one-time resources, such as Federal ARRA funding for Police and Fire services, and more on the underlying strength of the local economy.

While conditions are improving in the aggregate, and we have grown a healthy General Fund Balance in excess of staff's recommended two-month reserve level, we must be cautious in projecting future revenues and expenses. This is why our current Proposed General Fund Budget still projects a 2.3% structural deficit (half the size of 2013's structural deficit).

In light of this financial standing, we are proposing to use a portion of General Fund reserves for one-time strategic investments, while maintaining a fiscally prudent two-month reserve and continuing to meet or exceed the expectations for service that our community expects. Acknowledgment and credit must be given to the City's public officials, its leadership team, our employees, and the electorate; all of whom supported various measures to bring us toward fiscal sustainability.

A Time of Great and Sudden Challenges

Last year, the City faced significant challenges it had never grappled with before.

The February 2013 murder of two of our police officers traumatized this community. The sadness and outrage that this community felt from the loss of Detectives Baker and Butler has ensured that public safety remains our top priority.

Following that tragedy, the City Council moved to utilize salary savings to: (1) authorize the over-hire of police officers to mitigate against position turnover, and (2) initiate hiring

incentives to attract experienced and qualified officers able to immediately support the City's safety needs.
Like all public agencies, the City will continue to adjust its long-term planning to account for changes to the California Public Employees' Retirement System (CalPERS). Pension reform initiatives adopted in the last year will likely significantly increase the City's annual pension contributions over the next five years.

These changes include lowering the expected rate of return in 2012 and increasing annual service payments to offset the system's catastrophic investment losses in 2007 and 2008. It is highly probable that CalPERS will update its demographic trend models to account for higher life expectancy later in 2014. It is also prudent to plan for another reduction in the expected rate of investment returns.

The ramifications of the Affordable Care Act, signed into law in 2010, will become a reality during the next fiscal year. Our projections assume a continued trend of health care cost increases, albeit slightly lower than the prior year's 12.5% increase. The State's Health Benefits Committee of CalPERS is expected to finalize rates for 2014 on June 18, 2013.

Within the past two months, the City has been the recipient of two major claims against our assets. The first is a judgment made on a property claim surrounding a small landslide on Branciforte Drive. Damages in this matter could exceed $1 million. Fortunately, the City has sufficient Liability Fund claim reserves to cover this amount. These reserves will need to be replenished over the coming years, however, to backfill this payment.

The second, and more significant claim, has been made by the State of California's Department of Finance as part of its ongoing attempt to claw back funding held by the Successor Agency to the City's former Redevelopment Agency.

The State has errantly claimed it is owed $2.1 million based on a partial review of the City's audit package submitted to the State. Staff is encouraged and hopeful that the State will evaluate the complete audit submission and appropriately and significantly reduce its claims against local tax revenues. Otherwise, the City will consider legal action.

Finally, what is probably the singlemost significant challenge to the City and region is the ability to provide a reliable water supply in time of drought and to prevent sea water intrusion. Just how we have managed our finances, we need to also manage our water system. A long-term, regional perspective needs to be taken.

We know that we will face a drought, and when the time comes we will not be able to provide sufficient water to our residents and businesses, unless we have a plan in place. Without a plan, the impact of a drought will be devastating, both environmentally and economically. The Soquel Creek Water District is already confronting sea water intrusion.

We have spent many years analyzing and studying how best to address this problem and identified sea water desalinization as the most viable regional alternative, along with continued conservation and curtailment in time of drought.

Optimism Turning to Opportunities

At the completion of our last budget cycle, we maintained an optimistic view of the City's economic future, supported by the City and community's repeated efforts to provide viable paths towards fiscal health. Our economic development efforts have been successful, and 2012 saw the opening of the Paradox Hotel on Ocean Street; the Monterey Bay National Marine Sanctuary Visitor Center across from the Municipal Wharf; and a new anchor store for Pacific Avenue, Forever 21. Thanks to an "all-hands-on-deck" effort throughout the summer and fall, Santa Cruz also welcomed the Warriors to their new facility on Front Street in time for their first home game on December 24, 2012.

Current levels of economic activity, including proposed and permitted infill development, hotel projects, and business expansion, as well as signs of a strengthening housing market, are encouraging. But complete economic recovery may still be 18 to 24 months away.

Given this progress, we believe that the City is in a position to look to one-time, strategic investments funded from our reserves. The recommended strategy is to invest these one-time funds toward: (1) general infrastructure and facility projects to reduce the level of deferred maintenance, (2) investing in City staff, and (3) creating a restricted reserve towards reducing unfunded liabilities.

Santa Cruz is an older City and desperately needs an ongoing capital improvement funding program, particularly since the loss of Redevelopment. During the lean budget years since the Great Recession, the City has deferred more than $102 million in infrastructure and facility projects.

These projects include facility and community investment projects like parks, storm drains, recreational upgrades, and street maintenance above and beyond the funding received from Measure H sales tax receipts.

In addition to outlining a strategy to guide one-time investment in infrastructure projects, staff will be developing a debt strategy to take advantage of historically low interest rates to pre-fund larger-scale infrastructure projects during calendar year 2014 by leveraging Measure H future revenues.

Staff believes a target-funding rate of $10 million to $12 million is achievable. However, both the one-time allocation and a potential bond issue will only address approximately 10% of the 90% of deferred capital projects. In addition, there are likely to be other neighborhood and greater community project improvements that could benefit from a larger capital improvement plan as noted above.

By December of 2013, all of the City's bargaining unit contracts will be up for renewal. Over the past five years, staff has made significant sacrifices to be a part of the longer-term path towards fiscal sustainability.

At the beginning of this calendar year, all employees completed the transition off of the temporary furlough model while maintaining a loss equal to or greater than 8% from their prior compensation levels (not adjusted for inflation).

In addition to this monetary sacrifice, staff have been increasing their overall work scopes to meet the community's high service levels, often absorbing functions left unfilled due to the loss of additional staffing. In recognition of these factors, we are proposing to utilize funding from the General Fund's fund balance to provide one-time, contractual benefits to employees in recognition for their sacrifices, hard work, and long-term commitment to our community.

City Council Strategic Plan and Three-Year Goals

We are in our third year of the first-ever adopted City Council Strategic Plan. The plan outlines three-year goals. This year the City Council approved updates and revisions to the plan, including the addition of a sixth goal. The six goals are:

- Enhance Environmental Sustainability and Resources
- Enhance Community Safety
- Promote Economic Vitality and Retain and Attract Businesses and Jobs
- Maintain Fiscal Stability and Sustainability
- Improve and Maintain the Infrastructure
- Enhance Community Engagement and Outreach (new)

A summation of the City's progress on each of these goals is included in **Appendix A** of this budget document. We are proud to report significant progress on each goal. Some highlights include:

Enhance Environmental Sustainability and Resources

- Adopted the City's first-ever Climate Action Plan.
- Significantly reduced the City's overall use of paper by delivering agendas for the City Council and advisory bodies in electronic formats, streaming and archiving Council meetings online, and moving bid documents and other previously published and mailed materials into electronic formats.
- Developed innovative programs in waste management to further extend the life of the City's landfill, while utilizing food waste to extract energy at the Resource Recovery Facility.
- Integrated storm water management best practices into private development project requirements.
- Prepared ordinances for single-use bag reduction, which included prohibitions on the sale of additional polystyrene/plastic foam products. Single-use paper bags are now available citywide for .25 cents.
- Retrofitted 325 streetlights to LEDs, dramatically reducing energy consumption.

Enhance Community Safety

- Hired six police officers.
- Implemented a predictive policing pilot project that was cited as one of *Time Magazine*'s top inventions of the year.
- Dramatically increased the Police Department's community outreach efforts, including launching a blog, an award-winning mobile application, two PRIDE program sessions, four Citizen Police Academy classes, and the establishment of a teen Police Academy Program.
- Expanded the First Alarm patrol program, providing extra public safety protection downtown, around City Hall and the Central Branch of the Library, and in Harvey West Business Park.
- Established higher levels of coordination between Police and Parks patrols.
- Served more than 900 participants in the Junior Lifeguard Program and increased Captain's Corp participation by 50%.

Attract and Retain Businesses and Jobs

- Successfully negotiated a sweeping series of agreements with the Santa Cruz Warriors and the Seaside Company to bring an NBA D-League franchise to Santa Cruz in a newly constructed arena.
- Completed and opened the Monterey Bay National Marine Sanctuary Visitor's Exploration Center adjacent to the Municipal Wharf.
- Facilitated the renovation and reopening of the Hotel Paradox, a new 160-room hotel on Ocean Street, as well as participating in the recruitment and opening of Forever 21, a new downtown anchor tenant.
- Partnered with Code for America, a national nonprofit, to develop the nation's first GIS-enabled small business permitting portal, OpenCounter.
- Implemented a series of policies and initiatives that increased access and adoption of downtown parking resources, including incentive programs for new leasing activity in the parking district, implementing variable rate parking, launching pay-by-phone and mobile app payment options, and holding a sold-out GroupOn event for downtown park cards.

Achieve Financial Stability and Sustainability

- Maintained the City's strong fiscal position (thereby reducing borrowing costs) by retaining an AA bond rating.
- Maintained a healthy reserve throughout the fiscal year.
- Partnered with the University of California at Santa Cruz on consolidation of Fire Operations, reducing administrative costs for both agencies.
- Applied for and received millions of dollars in external grant support, including more than $200,000 in Police Department grants and $850,000 to support the Municipal Wharf.
- Issued Pension Obligation Bonds to lower existing pension debt service expenses.
- Received the Certificate of Achievement for Excellence in Financial Reporting from the Government Finance Officer Association of the United States.

Improve and Maintain Infrastructure and Facilities

- Invested in numerous equipment upgrades to increase the efficiency and environmental sustainability of storm and wastewater treatment facilities, both throughout the City's system of storm drains and laterals, as well as at the Wastewater Treatment Plant.
- Completed a series of capital projects in the Downtown Parking District to increase accessibility and safety, including new security cameras and lighting, better sidewalks, and landscaping.
- Continued to improve the water delivery system's reliability and capacity through projects like the North Coast Water Main Replacement.
- Improved the City's transportation infrastructure via projects like the lower Pacific Avenue roundabout, the West Cliff Drive paving project, and the 2012 Cape Seal Program.
- Invested in City Parks, including the renovation of Field 1 at Harvey West through a partnership with Santa Cruz Little League and the renovation of Beach Flats Park, as well as securing Coastal Commission approval for the Arana Gulch Master Plan.

This proposed budget provides enhancements to further these goals, including funding for:

- Implementing the newly adopted Climate Action Plan by adding a Transportation Planner position, increasing the Green Building Environmental Specialist function from half-time to full-time, converting from a temporary to permanent position the Sustainability and Climate Action Coordinator, and providing temporary hours for a Climate Action Community and Schools Coordinator.
- Expanding the Park Ranger Program to address increased public safety concerns in the City's parks and open spaces.
- Hotel/Motel Façade Improvement Program.
- Capital Projects. An additional $2.1 million in funding for Capital Projects is included in the proposed budget. Significant projects to be funded include the Arana Gulch Multi-Use Trail Project and design/engineering for Ocean Street Beautification Project.
- A Community Engagement and Outreach Manager position, as well as additional funding for enhanced outreach and communications functions in the Water and Public Works Departments.

Acknowledgments

I want to thank the Mayor and Councilmembers for their dedication and leadership as we continue to navigate towards a path of fiscal stability. I also want to thank the City's department heads and senior staff who provide internal leadership, wisdom, and continued flexibility in crafting solutions to meet the community's service demands despite the budgetary challenges that we have faced since 2008. Finally, I want to thank each and every employee of our City, for it is your efforts that make the City of Santa Cruz an outstanding place to live, work, and conduct business.

The Finance Department deserves credit as well for crafting and compiling this Proposed Fiscal Year 2014 Annual Budget, with support from our Finance Director Marcus Pimentel, Assistant Finance Director Cheryl Fyfe, Division Manager Raymond Chin, and Senior Accountant Sallie McAndrew, who led the development of the assumptions, forecasts, and spending plans outlined in this document. Together they, with the other support managers, Patty Haymond and Laura Nolan; Senior Accountant Kim Wigley; accountants Ralph Reader, Ray Galindo, Shelley Horrow, Tracy Cole, and Amy Schmidt; and with support by Administrative Assistant III Natalia Duarte and the rest of the Finance Department staff, did a wonderful job within an exceptionally busy timeframe compiling this report. This City is very fortunate to have this caliber of dedicated, intelligent, and resourceful staff.

Sincerely,

Martín Bernal
City Manager

Recent Accomplishments

Despite the challenges from the Great Recession and the related reductions in employee compensation, benefits, and work hours, the City has had many recent positive highlights and notable achievements. Some of these are listed below within the five goals of the City Council's three-year strategic plan: Enhance Environmental Sustainability and Resources, Enhance Community Safety, Achieve Financial Stability and Sustainability, Attract and Retain Businesses and Jobs, and Improve and Maintain the Infrastructure and Facilities. Note that this is not a comprehensive list, but does highlight some of the key accomplishments.

ENHANCE ENVIRONMENTAL SUSTAINABILITY AND RESOURCES

- Reduced use of paper resources and supported remote access to reduce fuel emissions (real-time, online streaming of City Council meetings, online Public Records Act requests, and a simplified gateway to City documents).
- Implemented paperless agendas and document sharing for the City Council and City staff, decreasing resource use and increasing productivity.
- Completed projects recommended from the State Energy Commission energy audit of the wastewater facility.
- Developed Food Waste Receiving Project components to extract energy from waste stream.
- Converted electric motors to energy-efficient controls, reducing energy demands.
- Completed insulation of digester domes to optimize heat recovery and reduce energy costs.
- Continued energy reduction project to retrofit centrifuge process equipment to optimize operations and reduce costs.
- Implemented Storm Water Quality Low-Impact Development Requirements into private development projects.
- Completed the greenhouse gas emissions report from the City's Resource Recovery Facility to the California Air Resources Board and the Environmental Protection Agency.
- Prepared draft ordinances for single-use bag reduction and prohibitions on sale of additional polystyrene/plastic foam products (as recommended by the Transportation and Public Works Commission).
- Implemented components of a pilot program to convert pre-consumer food waste to energy (using the wastewater digester and generators).
- Reduced energy consumption by retrofitting 325 streetlights (ARRA grant) to LED lights.
- Removed up to 85% or more of the soot from the exhaust gases of diesel engines through the City's diesel particulate filter (DPF) program.

- Upgraded Soquel Garage EV Charger.
- Completed EV Charging Stations Design for parking garages.
- Climate Action Plan was adopted by City Council.
- Arana Gulch Master Plan was approved by the Coastal Commission.
- Completed the Draft Habitat Conservation Plan Strategy for Steelhead and Coho to the National Oceanic and Atmospheric Administration and the California Department of Fish and Game.
- Conducted scoping meetings and initiated the CEQA process for the desalination project.
- Completed the energy study that gives the desalination project a roadmap to carbon neutrality.
- Completed an agreement with Santa Cruz Archers.
- Developed a draft Interpretive Program for Arana Gulch with the Natural History Museum staff.
- Established a “trail crew” to maintain trails and provide additional greenbelt monitoring.
- Conducted several “Volunteer Days” on trails throughout the greenbelt.
- Installed waterless and low-flow urinals throughout the parks system.
- Incorporated drought-tolerant plants and drip irrigation at several City locations.
- Decreased the use of paper by going electronic with bid documents, commission packets, and other previously printed and mailed materials.
- Facilitated a February 2012 education exchange with Alushta, Ukraine.
- Completed a Demonstration Garden Project at the Fire Department Administration Building featuring drought- and fire-resistant plants.
- Completed erosion-control measures at the Golf Course.
- Presented the Heritage Tree Ordinance amendments to the Parks and Recreation Commission.
- Completed the assessment of the Museum of Natural History Collections.
- Provided financial direction and support for the City Hall and Police Department Solar Panel Project.
- Implemented an automated remittance processing system.

ENHANCE COMMUNITY SAFETY

- Facilitated the development of the Tobacco Retailer License Program.
- Completed the Emergency Relocation Project for the Water Street Storm Drains.
- Upgraded security cameras at the River/Front Garage.
- Completed Housing Element State Mandates regarding SB2 and Transitional Shelters.

- Launched social media suite focused on public safety (Facebook, Twitter, YouTube, Flickr, and Santa Cruz Police Department Blog).
- Implemented the Predictive Policing pilot project (First in Nation/*Time Magazine*'s 50 inventions of the year).
- Developed the first consumer-focused mobile app for law enforcement (2011 Helen Putnam Award Winner).
- Hired six police officers.
- Initiated Teen Police Academy.
- Completed two PRIDE program sessions.
- Graduated four Citizen Police Academies (two English/two Spanish).
- Implemented Teen Jeopardy tournament with City Schools.
- Expanded Police Department's volunteer program.
- Enhanced First Alarm Security Program.
- Facilitated and participated in three Parent Education Nights through BASTA.
- Joined County Gang Task Force.
- Hired two Police Records Technicians.
- Acquired grants to fund Traffic Safety and Safe Routes to School projects.
- Completed the Laurel Street Pedestrian Safety Project.
- Increased neighborhood and Parks security and safety.
- Established regular coordination meetings with Police Park Units and Parks and Recreation Rangers.
- Filled the vacant Chief Ranger position.
- Provided additional training to Park Rangers.
- Hired private security to address specific issues on the Wharf, along the levee, and in some parks.
- Amended the Surf School Ordinance.
- Supported youth through more than $10,000 in scholarship awards from the "Friends of Parks and Recreation."
- The Jr. Lifeguard Program served over 900 participants and increased Captains Corp participation by 50%.
- Abated lead and asbestos with funding from a Brownfields Grant and demolished the former Stroke Center facility in DeLaveaga Park.
- Abated the lead paint on windows at Louden Nelson Community Center and replaced damaged windows.

ATTRACT AND RETAIN BUSINESSES AND JOBS

- Facilitated City Council initiatives and strategic goals to support business and jobs.
- Managed the Technology Task Force, including the Code for America new business portal.

- Repealed the downtown dog ban.
- Facilitated the downtown business incentive program.
- Assisted with approving the local purchasing preference program.
- Facilitated over 160 special events, film permits, and block parties that provided community benefits and attracted visitors.
- Implemented a community outreach program, which includes a social media presence on Facebook and Twitter, an Annual Report, and regular e-newsletters.
- Implemented pay-by-phone options for parking meters.
- Created the Groupon PARKCARD parking promotion.
- Promoted downtown business through ads of downtown parking tips.
- Promoted new bike locker logo.
- Implemented Pay on Exit Option at Soquel Garage.
- Implemented temporary reduction in Parking Deficiency Fees.
- Completed the Monterey Bay National Marine Sanctuary Visitor Center.
- Completed evaluation that improved the Insurance Service Organization rating of the City (lowered community's insurance premiums).
- Supported World Disc Golf Tourney through partnership with DeLaveaga Disc Golf Club (erosion control and course improvements).
- Improved visitor experience through ticket scanners at the Civic Auditorium.
- Beautified beaches through purchase of beach rake and tractor for cleaning and grooming (used Measure E funding).
- Promoted and held a “Chris Rene” event at the Civic Auditorium to celebrate *X-Factor* contestant.
- Supported downtown businesses by Parks and Recreation participation in the Downtown Association Holiday Parade.
- Supported possible business connections by raising more than $36,000 for disaster relief through the Sister Cities Program for Shingu’s Sister City Natori, Japan, post-earthquake and tsunami.
- Coordinated the January 2012 Mayor’s Delegation to Jinotepe, Nicaragua, including the presentation of a surplus Public Works Department refuse truck.
- Coordinated a March 2012 Spring Student Delegation to Shingu, Japan.
- Celebrated the 25th Anniversary of the Alushta Sister City relationship.
- Provided financial direction and support for the potential Golden State Warriors Developmental Team relocation to the City of Santa Cruz.

ACHIEVE FINANCIAL STABILITY AND SUSTAINABILITY

- Maintained the City’s strong fiscal position through retention of AA bond rating and healthy reserve.
- Conducted revenue and cost-saving assessments.

- Implemented UCSC's University Comprehensive Settlement Agreement.
- Wrote and received $200,000 in Police Department grants.
- Shared services with UCSC for the Fire Chief position.
- Completed the comprehensive organizational review (Avery Associates report).
- Received a $50,000 planning grant for the Civic Auditorium from the Packard Foundation through partnership with Cabrillo Music Festival.
- Received a Teen Center Sustainability Grant from the Packard Foundation and began working with a consultant team and community members.
- Reduced Golf Course full-time staff and incorporated additional seasonal/temp staffing.
- Reduced staffing required for turf aeration at the Golf Course.
- Raised $20,000 at the first CruzaPalooza event, a family event and Teen Center fundraiser held at Louden Nelson Community Center and Laurel Park with major support from Zoccoli's Deli.
- Helped generate $70,000 from the Clam Chowder Cook Off (estimated 10,000 attendees).
- Completed the Coffee Cruzer Café lease to offer specialty items at Louden Nelson Community Center.
- Generated over $2,000 in the Birdies for Charity Fundraiser (the Teen Center participated for the first time).
- Increased Depot Park Freight Building rentals by 75%.
- Increased softball tournament rentals by 30%.
- Conducted Request for Proposals for the leasing of Harvey West Pool.
- Consolidated departmental operations to reduce overall costs.
- Implemented e-payables resulting in rebates back to the General Fund.
- Enhanced financial system training opportunities for City employees.
- Automated purchasing approval process to reduce operating costs.
- Automated Capital Improvement Program budget development to reduce staffing support.
- Issued Redevelopment Agency Bonds in anticipation of funding ongoing Redevelopment Projects.
- Issued Pension Obligation bonds to lower existing pension debt service expenses.
- Received the Certificate of Achievement for Excellence in Financial Reporting from the Government Finance Officers Association of the United States.

IMPROVE AND MAINTAIN INFRASTRUCTURE AND FACILITIES

- Increased Primary Sedimentation Structure's useful life through rehabilitation project.
- Completed Gravity Thickener Rehabilitation Project.

- Completed various storm drain maintenance and repair projects in the San Lorenzo River levee.
- Completed the Evergreen Cemetery Drainage Project.
- Completed the design for the Sunnyside Sanitary Sewer Project and established an assessment district to fully fund the project.
- Established the Wastewater Treatment Facility Strategic Maintenance Painting Program.
- Completed Scrubber Maintenance Area Improvements within Soquel Garage.
- Upgraded lighting at Locust and Soquel Garages.
- Completed improvements at Parking Lot 16 (Previous “Sentinel” Lot).
- Completed Sidewalk Repairs on all parking lots.
- Completed improvements on Parking Lot 9 Landscape and Surfaces.
- Completed surface improvements on Parking Lot 7.
- Completed General Plan Draft Environmental Impact Report and underway with final hearings.
- Ocean Street Area Plan adopted by City Council for the purpose of CEQA compliance.
- Completed a major project to rehabilitate the North Coast Raw Water Main.
- Acquired a Coastal Commission Development Permit for Arana Gulch.
- Completed the design development for the Riverside Avenue Utility Undergrounding and Streetscape Project and established the Utility Undergrounding District.
- Completed the Highway 1/9 Environmental Review process.
- Completed the East Cliff Slope Stabilization Project.
- Completed the award-winning Depot Intersection Roundabout Project.
- Completed the West Cliff Drive Paving Project.
- Implemented the Spring 2012 Cape Seal Program.
- Completed the design concept for the Branciforte Creek Bike and Pedestrian Bridge and Path.
- Renovated Harvey West Park's Field 1 through partnership with Santa Cruz Little League.
- Completed Woodrow Avenue and Water Street Median Renovation Phase I.
- Painted the California National Guard Armory and removed the water tower as a condition of the pending land swap in DeLaveaga Park.
- Received approval by the California Coastal Commission for the Arana Gulch Master Plan.
- Completed park design for the new Lower Ocean Street Neighborhood Park – Prop 84 Grant.
- Received approval by the Parks and Recreation Commission and City Council for the Pogonip Multi-Use Trail and Master Plan Amendment.
- Completed renovation of Beach Flats Park.