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REPORT TO MAYOR AND CITY COUNCIL

SUBJECT

Overview of City Council Operational and Strategic Priority Setting Sessions

EXECUTIVE SUMMARY

I want to thank the City Council for assigning two-days to review the state of the organization, advancements of policy priorities, and key data that provides direction on managing the City going forward. I have spent the last year observing and engaged in dialogue with employees, stakeholders, and the community in order to become more informed on our major lines of business as well as opportunity areas. With my first year completed, my understanding is more thorough and, in some cases, further reinforces my initial observations from last year.

I continue to believe strongly that our highest priority and focus is remaining fiscally stable because, all of our public services depend on it and, without it, we cannot continue to provide our community with a broad range of quality services and maintain the high performing workforce that serves our City. Equally as important is our workforce, which is our greatest investment and asset. As a service organization, our employees are the key to the high ratings the community gives the City and it is important to review the care, training/development, and workplace that we provide to retain and recruit our valued and talented employees.

Last year, during the Council's Priority Setting Session, I spent quite a bit of time on reviewing the State of the Organization and the major administrative gaps that existed (i.e. manual processes, risk management and the absence of modernized enterprise-wide systems). Although many of these gaps still exist, we are making significant strides towards addressing them, as I will present at this year's session.

Improving administrative processes are foundational to a high-functioning workforce. As we discuss some of the progress in these process areas, this year's main focus will move the conversation to addressing workforce needs. Both process and people are equally as important to delivering efficient, effective and the high-quality service/programs to which our community is accustomed.

This year's session will also show that the City has achieved a more balanced policy approach and internal governance structure with the appointment of the Council's third Council Appointee, the City Auditor. Each Council Appointee (City Manager, City Attorney, and the City Auditor) will present at the session. It is important to note that while the organizational governance foundation has been achieved, the Council itself is in transition with the newly formed Council Districts as was discussed at the December 13, 2018 Governance Session, and the organization will need to adapt from

a workload perspective to this new governance system.

Major outcomes of this Session include:

1. Review of the State of the Organization
 - Updates/accomplishments from last year's January Priority Setting Session and Current State of the Organization, including a review of operational, staffing, and key data/metrics (City Manager)
 - Council Appointee Updates (City Attorney and City Auditor)
 - Specific progress on administrative gap areas from last year:
 - Human Resources Assessment
 - Procurement Reforms
 - Fiscal update
 - Fiscal Outlook
 - Ten Year Financial Forecast
2. Review and assess current Council priorities and policy and related workload and upcoming projects and initiatives for 2019.
3. Department Operational and Strategic Initiative Updates

GOAL SETTING SESSION FACILITATOR

Dr. Shawn Spano will again facilitate this strategic planning session. Dr. Spano has over 18 years of experience working with city government and public organizations. He is a specialist in designing and facilitating public forums, meetings, training workshops and off-site retreats with leaders, executive staff, elected officials, middle managers, commissions and boards, and local residents.

As background, Dr. Spano is a professor at San Jose State University where he teaches courses and conducts applied research in interpersonal and small group communication. He specializes in bridging social construction and dialogue theory with practical skills and tools that enable students to design and facilitate processes to improve communication in community, organizational and interpersonal contexts. Dr. Spano also serves as President of the Public Dialogue Consortium, a non-profit organization committed to fostering high quality communication in the public sphere, collaborative problem solving, appreciation for different perspectives, and common ground for action.

SESSION FRAMEWORK - Day 1 & Day 2

The Session is specifically designed so that the City Council can consider and, more importantly, align the process of goal setting to the City's fiscal condition, operational realities and priorities, and within the context of our strategic pillars:

1. Promote and Enhance Economic and Housing Development
2. Deliver and Enhance High Quality Efficient Services and Infrastructure
3. Enhance Community Sports and Recreational Assets
4. Enhance Community Engagement and Transparency
5. Ensure Compliance with Measure J and Manage Levi's Stadium
- 6. Manage Strategically Our Workforce Capacity and Resources** (previously Maintain Adequate Staffing Levels)
- 7. Sustainability**

Staff will be presenting two amendments to the current Council Priority Pillars for the City Council's consideration - highlighted above in **bold print**. Staff believes that it is time for the Council to add a Sustainability Pillar as the City is accomplishing many measures in this area, but needs to achieve even more results and establish organizational awareness on this key priority. I am also recommending a change to the pillar related to adequate staffing to better reflect a set of comprehensive actions needed to align the City's needs with the description of this pillar.

With this framework in mind, below is an overview of our two-day Session:

Day 1 will consist of a thorough presentation by the City Manager on the State of the Organization, progress from 2018, and an overview of key workforce and staffing metrics. This will be followed by updates from each Council Appointee, the City Attorney and the City Auditor. Staff will also present key updates on Procurement and Human Resources and the

City's current fiscal condition and presentation of a 10-Year General Fund Financial Forecast.

Day 2 will begin with each department providing a review of service delivery highlights, upcoming policy issues, operational constraints, and areas for opportunity. After all department heads have presented their information, the City Council will then be guided on a focused discussion of aligning policy priorities and determining any adjustments necessary to sustain strategic efforts. As additional policy priorities/goals surface, the Council will be asked to consider these efforts within the context of current fiscal and workforce resources and capacity (See 10-Year Financial Forecast Section) and what operational or priority tradeoffs to consider.

Day 1 Agenda: Operational

- Context Setting
- Update on the State of the Organization (City Manager)
- Council Appointees (City Attorney, City Auditor)
- Updates on Key Administrative Gap Areas
- Fiscal Outlook and Budget Update
- Update of Current Council Priorities

Day 2 Agenda: Priority Setting

- Department Review of Operational Priorities
- Council Discussion on Priorities, Alignment, and Resources
- Aligning Council Priorities and Council Action
- Wrap-up/Next Steps

I am hopeful that our work over these 2 days will culminate into common priorities and clear policy direction for the upcoming year as we look at issues and projects on the horizon. I believe this approach supports the City Council well in its governance role and will advance strategic policy priorities with clear information on the needed resources to achieve them within the context of the City's fiscal outlook. It is also well acknowledged that this is a new approach for the City and we will learn how to work together under this integrated framework.

STATE OF OPERATIONS

As part of the state of operations overview, as your City Manager, I want to recognize the incredible work that the City Council and the organization have accomplished. In October 2018, and the completion of my first year, I released a Community Letter that provides the many successes of the City (Attachment 1). While there are too many specific accomplishments to list, below are just a few to highlight the successes.

Fiscal Outlook - through diligent review of the City's past budgeting practices and assumptions, we:

- significantly corrected and reduced, for FY 2018/19, an \$8.5 million budget shortfall to \$1 million without cuts in services (saving 40-50 General Fund jobs) and successfully balanced the budget;
- transitioned to a two-year budget cycle to make longer-term budget decisions;
- moved from a 5-year to 10-year financial forecast to better project deficits and surpluses, and review budget decisions within a longer-term context;
- ensured that we are on track to contribute \$80 million to our reserves in the first 16 months of my tenure and all operating reserves are at or above Council required levels; particularly, the General Fund Budget Stabilization Reserve is scheduled to be funded at \$78 million by February 2019, which is 25% above the Council required reserve level; and,
- developed a revenue generating strategy for the City Council to consider over the upcoming years with viable options and projected revenue to be generated.

Strategic Project Delivery - focused on strategic initiatives that respond to our community's interests:

- hand-in-hand with our community, we made unprecedented progress to realize the future reconstruction of Santa Clara's downtown through funding the development of a Precise Plan and negotiating agreements for street rights to sections of Franklin and Washington Streets, and we are now positioned to work on the land use planning/visioning for the downtown through a community-oriented process;
- after years of litigation, worked with the Mayor and Council to reach settlement agreements for: (1) build out of the CityPlace project with a total transportation improvement package of about \$70 million and (2) protection for the City's interests from San Jose's Santana West development impacts resulting in nearly \$8.7 million of housing and traffic improvements benefiting Santa Clara. CityPlace currently has a planned groundbreaking in late 2019 and brings a large-scale, mixed-use development in a geographically strategic area, directly across from the

Levi's Stadium;

- completion of a City facility and infrastructure assessment (e.g., parks, facilities/buildings, public works systems, etc.), which provides an inventory of the state of our infrastructure and road map for future needed investments and critical improvements required to sustain quality of services;
- launched implementation of a capital projects management system to streamline tracking, management, oversight, and implementation of the City's 800 capital projects, transitioning from a manual process to a software system that provides real-time information of valued projects; and
- obtained and improved key financial data to transparently manage the Santa Clara Stadium Authority and have answered basic questions about the Authority's financials, while completing nearly 70 percent of the Measure J Compliance Audit recommendations and issuing a transparent budget and marketing plan.

Administrative Improvements and Modernization - through review of our service delivery systems, we found the absence of, and established, the following new focused services:

- filled, for the first time, the City and Santa Clara Stadium Authority Auditor position with a Certified Public Accountant who has met the audit experience hours requirement, from the State, qualifying her to attest reports and audit engagements; she is now developing an auditing program to be presented in early 2019;
- established a Risk Manager position and hired a manager to improve risk management of basic City services (e.g., workplace risk, contractual risk, insurance requirements, etc.);
- established a Public Records position and hired a manager to improve our overall records management and public records request processes;
- improved procurement processes and contract oversight of the many public contracts that the City issues, supporting Council's focus specifically on Levi's® Stadium and the Convention Center;
- reduced manual processes by incorporating technology tools to improve efficiency and address administrative gaps, such as: public records management system purchased, re-launch of the City's Customer Relationship Management system - MySantaClara, and Council agenda development software implemented;
- developed a prevailing wage program to ensure compliance with state law including the implementation of a new tracking software and hiring of an outside contractor to help ensure compliance, provide training and perform audits of our public works projects, and;
- implemented City's new Computer Aided Dispatch System for our public safety departments.

Capacity-building/Streamlining to Continue to Transform the Organization - we have also invested in employees through training and staff development to keep skills sharp and modern, while assessing City's portfolio for staffing needs. The City had many vacancies (for instance, the City Manager's Office had a 60 percent vacancy rate of key personnel) and relied on several "acting" positions to deliver service, which is not a sustainable or stable long-term strategy. We have made progress, in likely the nation's toughest market to recruit talent, with filling our many vacancies. We have also completed five labor agreements, within the City's ability to pay, and are working with our five other bargaining units to reach successful labor agreements.

MANAGEMENT GRIP AND ADMINISTRATIVE GAPS

At last year's session, I discussed the unprecedented volume of new initiatives and the increased pace of the organization being disproportionate to its capacity/resource increases. I also discussed key administrative gap areas, mistakes in upholding policy or implementing direction, risks in administrative processes, or inaction that is from assigning focus and capacity over upholding conventional administrative processes. This past year, I worked with staff to establish some metrics and governance structures on key policy areas to more appropriately base our work on data-driven information. We have made progress on some of the administrative gap areas that I identified last January, which I will present at the Session, however, I continue to have serious concerns about the City's ability to manage its grip on several significant initiatives at once. Our resources are below the levels needed to support the workload and capacity is finite. Decisions to expend City resources/capacity must be strategic and calculated so that they do not detract from value-add initiatives. Examples of our continuous improvement efforts include:

- Procurement/streamlining reforms;
- Appointing a City Auditor and developing an Audit Workplan;
- Conducted a Human Resource Organizational Assessment;
- Hired a Risk Manager;
- Hired a Public Records Manager;
- Established a dedicated media and public relations program and hired a Communications Director;

- Evaluated our overall assets to ensure they are being managed and governed properly;
- Re-launched our city-wide customer relationship management system (CRM) - MySantaClara to better address and be responsive to our citizen request; and
- Developed and presented for Council approval Legislative Guidelines and Legislative tracking systems.

WORKFORCE DEVELOPMENT

After presenting the progress made in 2018, I will quickly move to operational, staffing and workforce metrics that drive the organization's work. As I have already stated, workload continues to outpace the organization's capacity and investment in our workforce is essential to build capacity. This information will show that cities nearly half our size have more staff per capita and comparable cities are far less complex in service delivery. The data will also show that the City is largely built for operations, with about 92% of our workforce dedicated to operations. This leaves less than 8% for innovation and transformation of the organization, since our managers are "working managers" and employed with operational oversight and delivery, as well. In order to **transform** our operations and **invest** in our workforce, we need to integrate intentional skill building to ensure that our staff is trained with modern approaches to completing work, matched with modern processes.

The data that I share will also reveal that we have a workforce that is not near retirement age, which makes retention and recruitment more of a strategic focus and a challenge in our high-cost region and unprecedented competitive job market. I will spend a great deal of time reviewing these metrics with the City Council at the session, given that our largest investment and asset are our valued employees.

BUDGET UPDATE & 10-YEAR FINANCIAL FORECAST

Last year, staff developed a 10-Year General Fund Financial Forecast and called for a review of our budget principles to validate the long-term financial condition of the City. As part of this session, I recommend that we review an update to the 10-Year General Fund Financial Forecast. We have also updated the 2019 Budget Principles for Council's consideration (Attachment 2)

After review of the state of the organization, we will present a revised 10-Year General Fund Financial Forecast and discuss the implications to our strategic planning and action. While the fiscal outlook is not as grave as originally projected in the last Adopted Budget, we still have forecasted structural deficits within the 10-Year Forecast. However, the budget continues to be on edge as there are indications for a potential economic slowdown in the near future and other factors that can impact our assumptions. We continue the approach of solving annual deficits with ongoing budget solutions as shown through the "net operating margin" model, on-going expenditure reductions or an increase in ongoing revenues are required in order to stabilize the City's fiscal condition. We have built up our General Fund Budget Stabilization Reserve, demonstrating the incredible work that we have completed. This affords the City Council and staff time to work strategically, holistically and collaboratively on solutions. Our goal is to align expenditures with revenue growth which may require new revenue sources, service changes and/or reductions. It also requires the continued leadership and discipline that the City Council has practiced and the significant partnership that our bargaining units have provided in the best interest of the City.

The City's fiscal outlook while stable contains many risks like many other local municipalities. Particularly of note is that our General Fund relies heavily on volatile revenue sources (e.g., sales tax and transient occupancy tax), which is a vulnerability for service levels. With these volatile revenue sources, and the predictably rising pension cost expenditures and liabilities for other post-employment benefits, what quickly surfaces is a need for a strategic work plan on new revenue opportunities and expenditure growth management. As reported earlier this month, pension costs alone are predicted to increase significantly over the next ten years while the City's Unfunded Accrued Liability (UAL) for pension costs is projected to grow over 70%. With additional risk that CalPERS will not meet the assumed investment return, these costs could increase even more.

Within this context, the overall budget approach for Fiscal Year 2019/20 is to position the City for on-going budget balancing measures with the least amount of service impacts while avoiding spending incongruent with the proposed budget principles. Where we have additional funds, we should set those aside for future deficits or times of economic slowdown.

TWO-YEAR BUDGET PLANNING

As approved last year, I will be proposing that we continue the City's fiscal plans over a two-year cycle and a two-year Annual Operating Budget for this upcoming budget cycle (rotating Capital in Fiscal Year 2020/21), which allows for staff to spend the next year fiscally aligning and incorporating the City Council priorities to resource investments.

The opportunity to focus on one budget, over a two-year term, also preserves capacity of our limited budget staff during a time when we need to initiate and pursue revenue opportunities and expenditure growth management. The combination of two-year operating and capital budgets aligned to our strategic pillars, and in the context of a 10-Year financial forecast, is an improved practice of understanding today's fiscal actions over the long term, rather than budgeting year-to-year in a shorter five-year fiscal context.

In addition, in the instance of the Operating Budget, all line items will be reviewed for funding level and priority with a focus on continuing our City's high service levels and including resources that will be essential in critical operational areas. Budget decisions will be made with long-term implications taken into account using data from the 10-Year Financial Forecast. The Annual Operating Budget will also look to address critical gaps in staffing and will continue community engagement and transparency efforts.

Key to this process is to track and disclose to the City Council the universe of un- or under-funded service needs. To make sure the Council has a more comprehensive assessment of service needs, beyond existing operations, a lengthy list of unmet, under- or unfunded needs (such as public facility and utility infrastructure) has been developed (Attachment 3) and is part of our work in the short- and long-term to stabilize both our financial and service conditions and for which dedicated capacity is required to develop realistic work plans. We must begin to address these gaps in service and make them part of our discussion when we consider new initiatives/priorities. As these needs have gone un- or under-funded, solutions to address them have also been un- and under-staffed.

Our highest priority is our fiscal stability and strong management so that we can continue to provide our residents with a broad range of quality services and maintain the high performing workforce that serves our City so well. I also believe that our current and past practices acknowledge that from the sustainment of fiscal stability and strong management, all other policy priorities are possible within the available resources. That said, as we work to address the current expenditure growth increases, economists continue to state the likely possibility of an economic slowdown that many experts project is over the next 18-24 months. It is important to acknowledge, that we should not assume that past solutions that existed during the Great Recession are available to resolve current or future conditions.

As a separate matter, this work is being completed concurrently with the Fiscal Year 2019/20 Stadium Authority Budget process which has already begun and will be brought to the Stadium Authority Board in March 2019. As reflected recently in the media, the Forty Niners have departed from their past budget submittals and the impact of their proposed budget requires significant review and deliberation.

Additionally, the City Auditor will provide as part of her presentation an updated FY 2018/19 (mid-year) and 2019/20 workplan (Attachment 4). The original workplan was approved by the audit committee on Dec. 3, 2018.

CONCLUSION

I respectfully request that the City Council continue to practice discipline in directing new work efforts and allow for us to consider the required work to stabilize the organization and, more importantly, focus on existing priorities, revenue opportunities, and investment in our workforce.

Through this session, we will illustrate how our resources are already extremely stretched and how adding new assignments must come with trade-offs and delay in ongoing work. It is my strong desire to work with the City Council on managing our resources while achieving our goals and the opportunity to surface the context of our work is much appreciated.

In closing, these sessions offer the City Council an opportunity to continue setting the City on a strategic path. City staff is fortunate that the City Council has elected to hold this Session and discuss, through a deliberative process, the City's future and key initiatives. I have attached the PowerPoint slides for both days for the Council's and the Community's reference (Attachments 5 and 6).

RECOMMENDATION

1. Adopt the 2019-2020 Budget Principles;
2. Accept the 10-year Financial Forecast;

3. Validate Pillars and approve recommended amendments as follows:
 - a. **Manage Strategically Our Workforce Capacity and Resources** (changed from Maintain Adequate Staffing Levels);
 - b. Addition of a new **Sustainability** Pillar;
4. Approve the City Auditor's Annual Audit Workplan for FY2018/19 (mid-year) and 2019/20; and
5. Provide direction to the City Manager to continue to work on the two revenue strategy options (Transit Oriented Tax and the Utility Users Tax) and bring back a work plan for the City Council.

Approved by: Deanna Santana, City Manager

ATTACHMENTS

1. October 2018 City Manager Community Letter
2. Proposed Budget Principles 2019-2020
3. Unfunded Projects and Infrastructure
4. City Auditor's Annual Audit Workplan for FY2018/19 (mid-year) and 2019/20
5. Session Slides for Day 1
6. Session Slides for Day 2