



2004-2005 SANTA CLARA COUNTY CIVIL GRAND JURY REPORT

SAN JOSE TRASH DEAL – HOW THE CITY WAS DUPED INTO WASTING \$11.25 MILLION

Summary

The 2004-2005 Santa Clara County Civil Grand Jury (Grand Jury) received a complaint that for four years the Mayor of San Jose concealed and misrepresented relevant facts from the San Jose City Council (Council) in promoting Norcal Waste Systems, Inc. (Norcal) as one of the two waste haulers for the City of San Jose. These acts, in apparent violation of San Jose's City Charter, ultimately cost the City of San Jose \$11.25 million. The concealments and misrepresentations resulted in a majority of the Councilmembers unwittingly being convinced by the Mayor and his Policy and Budget Director (Budget Director) that San Jose was obligated to pay Norcal, Inc., and its subcontractor, California Waste Solutions (CWS), \$11.25 million for alleged unanticipated increased labor costs. But Norcal, the Mayor and the Mayor's Policy and Budget Director knew about these costs in advance of Norcal being approved – the Mayor just did not tell the Council before it voted to approve Norcal as a vendor in October 2000.

As a result of its inquiry, the Grand Jury has serious concerns about the deceptive conduct of the Mayor and others, and about the resulting vote by the Council to approve the \$11.25 million payment to Norcal.

Accordingly, the Grand Jury has made 17 findings, the most significant of which are summarized here and explained in more detail in the *Findings and Recommendations* section in this report:

- Prior to the Council's first vote on Norcal in October 2000, the Mayor, his Budget Director and Norcal knew that CWS would have to pay higher International Brotherhood of Teamsters (Teamsters) wages instead of lower International Longshoremen's Association (Longshoremen) wages, and that this would cost CWS an extra \$2 million or more a year. The Mayor had a duty to disclose this information to the Council, but he did not do so, in apparent violation of the City Charter.
- When initially interviewed by the Grand Jury in March 2005, the Mayor and his Budget Director insisted that the Mayor never met with the representatives of Norcal or CWS. At that time, the Mayor contended that, in order to avoid the appearance of impropriety, he did not meet face-to-face with Norcal or CWS because he did not want to be criticized about "backroom discussions." In subsequent interviews with the Mayor and his Budget Director, they admitted that indeed such a meeting had occurred on October 6, 2000, in the Mayor's conference room, four days *prior* to the Council's vote on October 10, 2000 to approve Norcal as a vendor. The Mayor and his Budget Director either had a

memory lapse or they did not tell the truth initially. In any event, the Mayor took part in “backroom discussions,” and this conduct was improper and appears to be in violation of the City’s Independent Judgment Policy and/or City Charter.

- For a period of almost four years, between October 2000 and early September 2004, the Mayor and his Budget Director *concealed from the Council*: (a) the occurrence of the October 6, 2000 “backroom discussion” the Mayor had with Norcal and CWS; (b) the Mayor’s October 6, 2000 assurance to Norcal and CWS that the Mayor would take the steps necessary to have San Jose pay the increased costs; (c) that the \$11.25 million in increased costs were known and anticipated prior to the Council’s October 10, 2000 vote to approve Norcal as a vendor; (d) that the primary purpose of a nine percent garbage rate raise in FY 2003-2004 was to cover the increased costs to Norcal; and (e) that the threatened strike by the Teamsters in February 2003 was primarily caused by the Mayor’s delay in asking the Council to pay Norcal the \$11.25 million.
- The payment of \$11.25 million appears to be a gift of public funds. The Mayor’s assurance to Norcal to pay Norcal the extra labor costs, without Council approval, appears to be a violation of the City’s Charter and may be voidable under California law.
- The Mayor and his Budget Director knew that Norcal was willing to take less than \$11.25 million, but the Mayor chose not to negotiate, and the Mayor did not advise the Council that Norcal would take less than the \$11.25 million. Further, the City Manager and Director of Environmental Services were authorized to negotiate with Norcal, but they made no effort whatsoever to negotiate a lower settlement.
- The October 6, 2000 meeting was initiated and chaired by the Mayor. The Mayor made it clear that he wanted the Teamsters to represent the CWS workers. It appears to the Grand Jury that the Mayor’s intervention on behalf of the Teamsters may have been a violation of federal and/or state labor law.
- There were many discrepancies or versions of the facts related by the 18 people who were interviewed during the investigation by the Grand Jury. The Grand Jury finds that the only way to ascertain all of the facts, and the ultimate truth, is to have City officials testify under oath and under penalty of perjury.

Based on these findings, crucial parts of the Grand Jury recommendations are that: (1) an independent special investigator be retained to take statements under oath, obtain all of the documents, and then decide who acted inappropriately, and what sanctions should be sought, and (2) the City Attorney or the special investigator should take the legal steps necessary to rescind the \$11.25 million Norcal/CWS reimbursement.

Background

On December 14, 2004, the Council approved paying \$11.25 million to Norcal, San Jose's largest waste hauler, to reimburse Norcal for allegedly unanticipated labor costs incurred by its subcontractor, CWS, which is responsible for sorting and recycling. The seven-to-three vote in favor of paying Norcal occurred despite the efforts of three Councilmembers who asserted that the City was not contractually obligated to make such a payment. The three dissenting Councilmembers contended that: (1) the payment would be an illegal gift of public funds; (2) San Jose was not obligated to bail Norcal out of its labor problems; (3) San Jose should have tried, at a minimum, to negotiate a lesser payment with Norcal; and (4) such a gratuitous payment would set a dangerous precedent. To understand how this Council vote occurred, it is necessary to review the background history of San Jose's selection of Norcal, Norcal's dealings with the Mayor and his Budget Director, and the Mayor's efforts at protecting Norcal while ignoring his ethical obligation to disclose to the Council the material facts which the Council needed to make informed decisions.

To gain insight into the history of the City's decision to pay Norcal \$11.25 million, in March and April 2005, the Grand Jury reviewed hundreds of documents and interviewed the Mayor twice, the Mayor's Budget Director three times, the Director of Environmental Services (DES), the Deputy City Manager, the City Attorney, eight current Councilmembers (excluding the District 10 Councilmember who took office in January 2005), the President and two other representatives of Norcal, the President of CWS, and the Secretary-Treasurer of Teamsters Local 350. Those interviewed had different recollections of events, and the Grand Jury concluded that, when there was a conflict between an individual's recollection of events and the documents related thereto, that the documents were given greater credence.

Given the opportunity to interview 18 individuals, plus review hundreds of pages of documents, e-mails, secret agreements and secret communications, some of which had to be subpoenaed from reluctant parties, the Grand Jury has pieced together many of the facts, the half-truths, concealments, misrepresentations and deceptions being foisted upon the Council and public. This is a lengthy narrative, but an important one for the citizens of San Jose.

The sequence of events over time will be important to the subsequent discussion, and key meetings and communications are shown on a timeline in Figure 1.

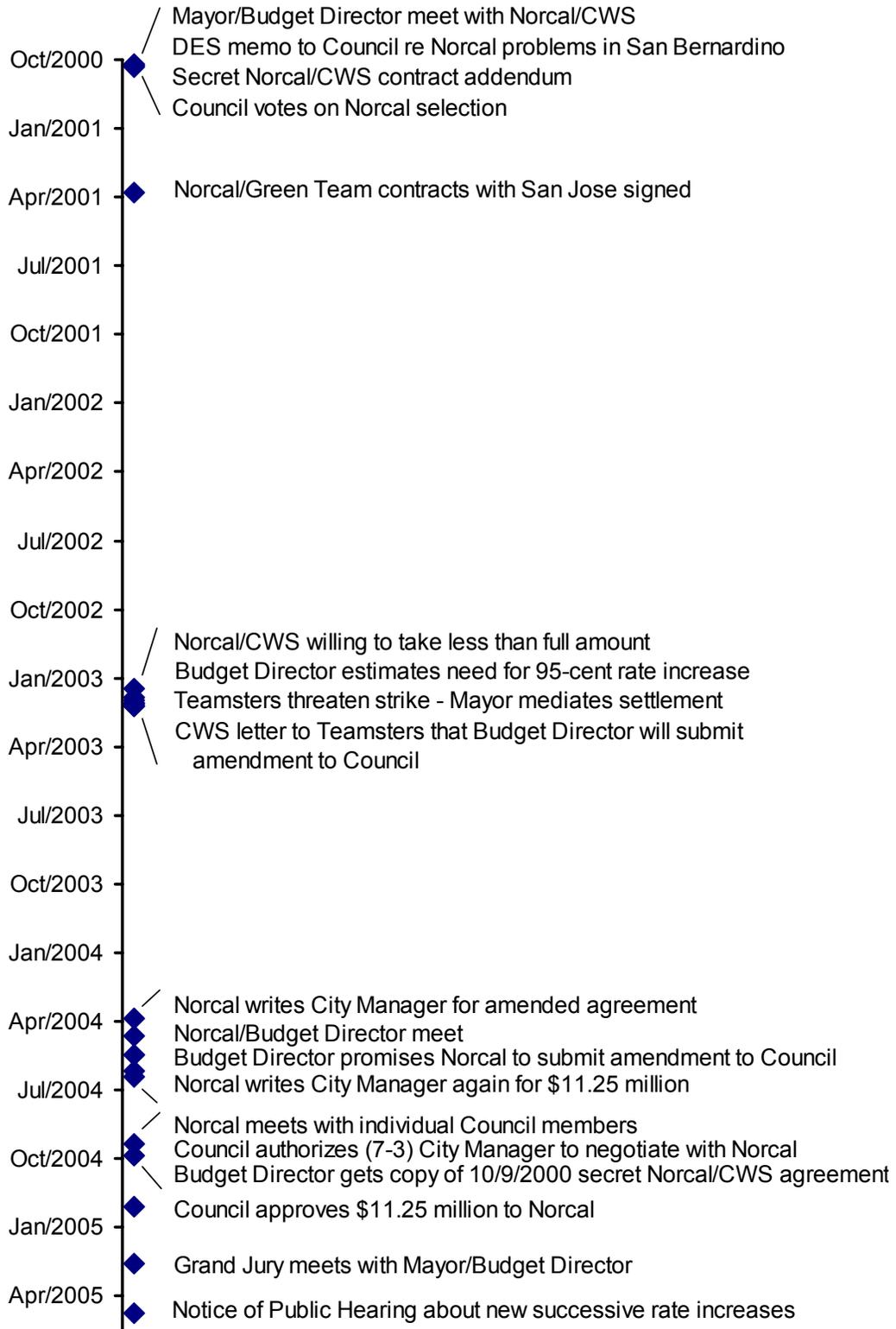


Figure 1: Timeline of key events in the Norcal/CWS contract and \$11.25 million payment

Discussion

THE ROLE OF THE MAYOR AND HIS POLICY AND BUDGET DIRECTOR

The Mayor has repeatedly stated that, as Mayor of San Jose, he is “flying at 30,000 feet.” That is, to run such a huge, populous city, he looks at the big picture, and then delegates broad policy to his staff to address the details. In the case of Norcal, the Mayor contends he delegated the handling of Norcal’s and CWS’ problems involving labor peace, worker retention and prevailing wages to his Budget Director. The Mayor believes that when his Budget Director acts, he is doing so on behalf of the Mayor.

It is important to note the role of the Budget Director. The Mayor appointed him and he is a member of the Mayor’s staff. The Budget Director and Mayor made it clear that the Budget Director works for the Mayor, not the Council. The Budget Director contends that, while in the employ of the City, his loyalties are to the Mayor, not the Council, and it was not his duty or job to disclose or share with the Council what he had learned about Norcal and CWS.

The Mayor’s Budget Director recalls having “a few” meetings and phone conversations with representatives of Norcal and CWS over the increased wages issue. Other parties state they had over 10 face-to-face meetings and over 20 phone conversations with the Budget Director between the October 2000 commitment by the Mayor and the December 2004 vote by the Council to pay the \$11.25 million. During this time period, the Budget Director did not advise a single Councilmember, other than the Mayor, of these meetings. Allegedly, the Budget Director repeatedly assured Norcal and CWS representatives that there would be “no problem” in obtaining the Council’s approval to pay the \$11.25 million, but that it would take time to put the paperwork together, and that Norcal and CWS had to prepare certain cost analyses to justify the payment from San Jose.

THE RECYCLE PLUS 2000 PROGRAM TO RETAIN NEW TRASH HAULERS

Every city needs to have its garbage picked up, disposed of, and recycled. Virtually everyone interviewed agreed that historically garbage contracts are fraught with unfair and unethical business practices. On June 26, 2000 the Mayor and Vice Mayor recommended that the Council approve guidelines to evaluate the Request for Proposals (RFPs) for the San Jose “Recycle Plus” program leading to multi-year contracts covering garbage, recycling, and yard waste. This included evaluations of the six companies that submitted competing bids, two of which would ultimately be approved. Green Team, Inc. and Norcal were selected in October 2000, with Green Team selected to cover District B, and Norcal selected to cover Districts A and C. San Jose’s RFP explicitly required that any vendor submitting a bid had to promise labor peace, worker retention (the new vendor would have to offer jobs to the employees of the displaced vendor), and prevailing wages (which in this case meant Teamsters’ wages, since the majority of the recycling workers were currently Teamsters). The Director of Environmental Services was assigned the task of receiving the vendors’ proposals, assessing the relative abilities of the competing vendors, and then advising the Council which of the vendors met the requirements of the RFP. Norcal was the lowest bidder by several million dollars.

MAYOR RECOMMENDS NORCAL DESPITE ITS PROBLEMATIC HISTORY

The Mayor's June 26, 2000 recommendation of Norcal to the Council describes Norcal's history and serious legal problems. The history discusses San Bernardino County's lawsuit against Norcal, alleging bribery, fraud, and unjust enrichment. An 18-month jail sentence for a Norcal employee, who admitted taking bribes, and a \$6.5 million settlement payment by Norcal to San Bernardino County were also discussed and described in the Council memorandum. The Grand Jury has not been able to ascertain why no one on the current San Jose Council recalls ever reading this history.

A September 22, 2000 Memorandum from the City Manager to the Mayor and Council recommended using Norcal and Green Team, with a projected savings of \$70 million over a new 11-year term. The contract included an initial contract period of five years, with two three-year options. The City Manager reported that Norcal rated high in services, that it had extensive experience, that it had a thorough transition plan, and that Norcal had a proven record of good customer service. The City Manager also reported that the City's RFP included mandatory contract requirements, including prevailing wages, retention of displaced workers, and labor peace. The City Manager also indicated that Norcal would comply with the worker retention provisions of the RFP, and that Norcal had already initiated discussions with the union representing the current drivers, Teamsters Local 350, and had included in this proposal a Memorandum of Understanding between Norcal and Local 350.

On October 2, 2000, the DES and the City Manager provided background information to the Council on the six companies that submitted proposals in response to the RFP. This information consisted of newspaper articles published in California. Most of these articles contained negative comments about the companies, and many were repetitive. This background information included eight articles about Waste Management, one about Republic Services, Inc., one about Browning Ferris, two about Green Team, and 37 about Norcal. The articles about Norcal included references to Norcal's difficulties in San Bernardino County. The articles also discussed Norcal's problems in San Francisco, where a recent mayor settled a garbage strike by Norcal's employees, and received \$5,000 from Norcal for an inaugural party and more than \$10,000 for campaigns over the years. No one currently on the Council recalls ever reading this information about Norcal.

There is no evidence that any Councilmember ever expressed concern or asked any questions about a supplemental DES memorandum to the Council, dated October 6, 2000, describing how Norcal agreed to pay San Bernardino County \$6.5 million in exchange for a dismissal of a civil lawsuit against Norcal. In this memorandum, the San Jose Mayor and the Council were advised that Norcal was accused of fraud, unjust enrichment, bribery, violations of the Political Reform Act, the Unfair Competition Law, and the False Claims Act, and that on July 26, 2000, 44 days after being served the lawsuit, Norcal agreed to pay back San Bernardino \$6.5 million of the \$20 million the County had paid Norcal pursuant to a garbage-hauling contract.

There is no evidence that any Councilmember ever expressed a concern or asked a single question about San Bernardino County having precluded Norcal from submitting any bids to the County of San Bernardino for a period of five years after the then existing contract was ended on June 30, 2001. Thus, at or about the same time that the City of San

Jose was approving Norcal as a vendor for 11 years, the County of San Bernardino was telling Norcal it would not be permitted to even bid on a contract for five years, and it forced Norcal to give back \$6.5 million to the County of San Bernardino. The minutes of the Council reflect that no Councilmember asked questions or made comments about Norcal's very serious problems in San Bernardino County.

Norcal's October 4, 2000 facsimile letter to the Mayor (but not to the Council) stated that Norcal "commits to worker retention for all displaced employees currently represented by [Teamsters] Local 350." The letter also states "Our subcontractor, California Waste Solutions is also committed to worker retention and plans to offer positions at their new San Jose facility to Material Recovery Facility workers displaced by the RFP process... The employees of that (CWS) facility will be represented by a Collective Bargaining Agreement with International Longshoremen Workers Union (Longshoremen) Local 6." Thus, the Mayor knew, or should have known, no later than October 4, 2000 that, since CWS was proposing the use of Longshoremen rather than Teamsters, there was a potential labor problem between the Teamsters and Longshoremen. There is no evidence that the Mayor ever shared this letter with the Council. Meanwhile the Teamsters Union had voiced serious concerns about CWS' position. The Teamster representative persuasively argued that the San Jose RFP required the displaced workers be offered jobs, and that they were entitled to prevailing wages (i.e., higher Teamster wages). This issue was coming to a head just before the October 10, 2000 vote to approve Norcal as a vendor, and it was of great concern to all of the parties, in particular the Mayor, who did not want to have a garbage strike.

THE OCTOBER 6, 2000 MEETING WITH THE MAYOR, NORCAL AND CWS

When the Grand Jury first interviewed the Mayor and his Budget Director in March 2005, they both insisted that the Mayor never met with the representatives of Norcal or CWS in October 2000. The Mayor contended that, in order to avoid the appearance of impropriety, he did not meet face-to-face with Norcal or CWS because he did not want to be criticized about "backroom discussions." But when the Grand Jury interviewed the Mayor a second time in April 2005, the Mayor acknowledged that his computer calendar confirmed he did meet with Norcal representatives on Friday, October 6, 2000, although he could not recall any of the specific topics discussed, or whether any CWS representatives were present. The Mayor's Budget Director, when interviewed for a third time in April 2005, also acknowledged to the Grand Jury, for the first time, that such a meeting occurred. The Grand Jury concludes that there were at least three Norcal representatives and two CWS representatives at this meeting. The October 6, 2000 meeting occurred three days before Norcal and CWS signed an October 9, 2000 secret contract addendum, discussed below, and four days prior to the October 10, 2000 Council meeting to vote on Norcal as a vendor.

The October 6, 2000 meeting was initiated and chaired by the Mayor, with his Budget Director also in attendance, and was held in the Mayor's conference room at San Jose City Hall. Participants at that meeting told the Grand Jury that the Mayor told the Norcal and CWS representatives that he wanted labor peace and he wanted the Teamsters to represent the CWS workers. The Grand Jury believes that it may have been a violation of federal and/or state labor laws for the Mayor to express a preference for one particular union.

At the October 6, 2000 meeting, the Norcal and CWS representatives advised the Mayor about the issue of increased labor costs. The President of CWS calculated that the first-year cost would be approximately \$2 million, with additional increases each succeeding year. The President of Norcal, in an interview with the Grand Jury, acknowledged that it was clear that Norcal would have to pay the recycle sorters Teamsters wages (at that time \$10.85 per hour, plus \$637.90 health and welfare benefits per month) and not Longshoremen's wages (\$7.00 per hour plus \$113.90 health and welfare benefits per month). The Mayor assured Norcal and CWS that he wanted the CWS workers to receive Teamsters wages, and he would take the steps necessary to see that San Jose would pay the increased costs. The Mayor and his Budget Director did not disclose this information to the Council until early September 2004.

At the October 6, 2000 meeting, the President of Norcal advised the Mayor that if San Jose agreed to pay for the increased costs, Norcal would pass the payment through to CWS.

The Mayor's Sunday, October 8, 2000 memorandum to the Council states, "Direct the Administration to clarify the City's prevailing wage, employee retention and labor peace policies as they relate to the RFP for Recycle Plus. Further, ensure that these policies are included in the negotiated contract.... The proposals we have received include mandatory contract requirements for prevailing wages, retention of displaced workers, and labor peace.... Because of the significant savings that the City expects to realize with the new contracts, we believe the City has an opportunity and an obligation to our residents to share the benefits of these savings. This could be in the form of prudent rate reductions or in the form of improved or new services that contribute to the quality of life in our neighborhoods."

THE OCTOBER 9, 2000 SECRET DEAL TO THE NORCAL AND CWS CONTRACT

Norcal and CWS signed a contract addendum, dated Monday October 9, 2000, three days after the October 6, 2000 meeting with the Mayor. The existence of this contract addendum was kept secret from the City of San Jose. This addendum expressly stated that Norcal would pay CWS for the increased costs that CWS would incur as a result of CWS having to pay the higher wage and benefit package costs required by San Jose. This addendum was not contingent upon San Jose reimbursing Norcal. The terms of this addendum were apparently never divulged to the Teamsters, and were not divulged to anyone at the City of San Jose for a period of four years, until October 7, 2004, when Norcal's attorney sent a facsimile copy to the Mayor and/or his Budget Director. By that time the Council had already voted on September 21, 2004 to authorize the City Manager to negotiate the terms of the increased payment to Norcal.

COUNCILMEMBERS UNAWARE OF EVENTS ON OCTOBER 6 AND OCTOBER 9

The current Councilmembers stated they were unaware of either the Mayor's October 6, 2000 meeting, or Norcal's October 9, 2000 contractual obligation to CWS to pay the increased costs. They all stated that the first time they ever heard of the meeting, saw the document or were aware of Norcal's contractual promise to pay CWS the increased costs, was when they were interviewed by the Grand Jury in March and April 2005.

OCTOBER 10, 2000 COUNCIL MEETING APPROVING NORCAL AS VENDOR

Just one day after the Norcal/CWS contract addendum, on October 10, 2000, the Council conducted its regular Tuesday meeting. An item on the agenda was the selection of the two vendors who would be used for the next 11 years to haul and recycle garbage. The total contract amount exceeded \$500 million over the 11 years, and Norcal would be receiving over half of the amount. On October 10, 2000, the Mayor and his Budget Director knew, but did not disclose to the Council, the following information:

- That they had just convened and chaired a meeting with Norcal and CWS representatives, in which the Mayor expressed a desire that the Teamsters would represent the CWS sorters, and advised Norcal that the Mayor would take the necessary steps to have the City reimburse Norcal for those costs;
- That Norcal verbally agreed to reimburse CWS for the increased costs; and
- That the Mayor, Norcal and CWS knew those costs would amount to around \$2 million the first year, and increase each year thereafter.

When the City Attorney was interviewed in April 2005, he told the Grand Jury that the Mayor should have advised the Council of the above information. It appears to the Grand Jury that the Mayor failed to provide the above information to the Council on October 10, 2000, and continued to conceal this information from the Council for a period of almost four years.

Council minutes reflect a nine-to-one vote in favor of awarding the Recycle Plus contracts to Norcal and Green Team, and directing the staff to prepare contracts. (The actual contracts were not signed until March 27, 2001.)

The DES also reported that, under the new contracts, performance bonds of over \$6 million for Norcal and over \$3 million for Green Team would initially be required, and that "In the event of contractor default, these amounts should be more than sufficient to guarantee continued services while an emergency and/or replacement contractor is secured and begins performance."

The Council asked the City Auditor to conduct an audit of Norcal's response to the RFP. The City Auditor's December 8, 2000 report states, "Norcal has a Memorandum of Understanding with [Teamsters] Local 350 to recognize Local 350 as the sole and exclusive bargaining representative for all the employees performing services under Recycle Plus 2002 contracts."

SAN JOSE'S CONTRACT WITH NORCAL IS SIGNED IN MARCH 2001

On March 16, 2001, the DES and the City Manager recommended approval of the contract with Norcal, with indications that the contract included provisions for prevailing wages and worker retention to protect the interests of the employees providing service through the existing agreements. On March 27, 2001, the Council voted unanimously in favor of approving the contract between the City and Norcal. Norcal was to commence operations on July 1, 2002.

The March 27, 2001 Agreement between Norcal and San Jose contains pertinent provisions:

Section 17.02.3 No Compensation Adjustment. CONTRACTOR shall not be entitled to any adjustments in the compensation paid to CONTRACTOR by CITY under this Agreement as a result of any adjustment of the wage rates which CONTRACTOR is required to pay its employees pursuant to the Prevailing Wage requirements of this Agreement.

Section 17.03 Worker Retention. CONTRACTOR acknowledges that when collection services are transferred to CONTRACTOR, workers who perform services for CITY's current contractors will be displaced from their employment. CONTRACTOR shall offer employment to all qualified displaced workers...

Section 17.04 Subcontractors. CONTRACTOR shall ensure that any subcontractor who provides services under this Agreement shall pay Prevailing Wages to any person employed or retained by the subcontractor to drive a collection vehicle. CONTRACTOR shall further ensure that any subcontractor who operates the Materials Recycling Facility [MRF] shall adhere to the Worker Retention requirements set forth in Section 17.03 with respect to any qualified displaced workers.

The above contract provisions establish that Norcal was contractually bound to pay prevailing wages, offer employment to all displaced workers, and seek no adjustments from San Jose due to increased wages. It appears to the Grand Jury that these contract provisions precluded Norcal from seeking any labor cost increases and relieved the City of San Jose from any responsibility to pay any such proposed increases.

JANUARY AND FEBRUARY 2003 EFFORTS TO GET SAN JOSE TO PAY

A January 22, 2003 CWS letter to Norcal assured Norcal that "CWS will continue to work with Norcal to help Norcal receive reimbursement from the City of San Jose *for some or all* of the sums paid to CWS by Norcal under the addendum. But the fact is that by virtue of the addendum, the risk of the City's non-payment or a shortfall in the City's payment rests squarely with Norcal and not CWS." [Emphasis added] *This letter confirms that Norcal was willing to settle for less than the full amount they were claiming.* The Mayor's Budget Director received a facsimile copy of this January 22, 2003 letter. The Mayor stated he never saw this document prior to his second interview by the Grand Jury in April 2005. The Councilmembers never saw this letter until March and April 2005, when the Grand Jury showed it to them. It is difficult to imagine why the Budget Director would keep from the Mayor the fact that Norcal was willing to take less than the full \$11.25 million. The Grand Jury concludes that the Mayor and his Budget Director knew, or should have known, that Norcal was willing to take less than the \$11.25 million, but that the Councilmembers did not know this.

On February 6, 2003, a letter from the CWS President to the Mayor's Budget Director confirmed that CWS and the Teamsters had reached an agreement regarding increased hourly wages, contingent upon "written direction by the City to pay the wages and benefits identified above." That letter calls the payment from San Jose a "subsidy" and

characterized the payment from San Jose as a “commitment.” This letter states that the “year one subsidy is approximately \$2.3 million and each year thereafter will be an additional approximately \$250,000 based on 75 employees.” No one on the Council recalls ever having seen this letter until the Grand Jury showed it to the Councilmembers in March and April 2005. But that’s not all that the Council did not see.

The Budget Director’s February 10, 2003 memo regarding “Teamster 350 labor subsidy” also contains information that the Budget Director did not share with the Councilmembers (with the possible exception of the Mayor). In that memo, the Budget Director advised the DES, the City Manager and the City Attorney that it was the Budget Director’s intent to amend the contract with Norcal to pay it \$1.9 million the first year, and \$2.15 million in year two. He wanted to know if those payments would be covered by *immediately* implementing a 95-cent rate increase to the customers. Another noteworthy comment by the Budget Director is that “This increase would still keep NorCal’s [sic] bid approximately \$2 million [per year for five years] below the Waste Management bid.” The first time the Councilmembers stated that they saw this memo was at the time of the Grand Jury interviews in March and April 2005.

On the same day the Budget Director issued the February 10, 2003 memo, he also e-mailed a letter to the President of CWS. The Budget Director’s e-mail to CWS confirms that a 95-cent-per-customer rate increase would cover the payments to Norcal/CWS. No one on the Council has apparently ever seen this e-mailed letter. Having read other correspondence that referred to such a letter, the Grand Jury asked the Budget Director and City Attorney for a copy, but their respective secretaries and the Budget Director said it did not exist. The Grand Jury procured this letter and other missing or misplaced documents by subpoenaing Teamsters Local 350, which had a copy of the e-mail transmission.

In light of the Budget Director’s inquiries about whether a 95-cent rate increase would cover the payment of \$11.25 million to Norcal, the Grand Jury had concerns about three rate increases. It is significant to keep in mind that, when Norcal was first approved as a vendor in October 30, 2000, the DES advised the Mayor and Council that *existing garbage rates could be maintained until FY 2005-2006*. In March 2001, at the time the actual contract with Norcal was signed, the citizens of San Jose were advised again that, as a result of the substantial savings with the new contracts with Norcal and Green Team, *there would be no rate increases until FY 2005-2006*. However, there were subsequently three rate increases: three percent in FY 2002-2003, nine percent in FY 2003-2004, and another nine percent in FY 2004-2005. When the Grand Jury asked current Councilmembers the reasons for the rate increases, they could not recall the reasons with any specificity. The Council votes for those three rate increases occurred prior to the December 14, 2004 vote to pay Norcal \$11.25 million, and the DES has stated that the \$11.25 million payment may necessitate a future rate increase. This rate increase issue will come up again when the Council’s September and December 2004 votes are discussed. Suffice it to say at this time, it appears that the Council was never told that any rate increase was intended to pay for the “subsidy” to Norcal.

THE THREAT TO STRIKE IN FEBRUARY 2003 – REAL, IMAGINED, OR A PLOY?

Norcal and CWS, tired of waiting for San Jose to formally agree and pay for the increased costs, apparently decided that if the Teamsters threatened to strike, this would put pressure on the Mayor to keep his commitment to have San Jose agree to pay the extra costs.

On February 12, 2003, the President of CWS wrote a letter to the Secretary-Treasurer of Teamsters Local 350, to confirm that “[the Mayor’s Budget Director] has asked you not to strike my San Jose facility because he is working on preparing all of the documents necessary to ensure that my company will receive the appropriate labor rate subsidies from the City of San Jose.” All Councilmembers stated that they were never aware of this letter until the Grand Jury showed it to them in March and April 2005.

When the Mayor heard about a possible strike, he offered to act as a “mediator” among the interested parties. The Mayor called the Secretary-Treasurer of Teamsters Local 350, who stated that he and his union members were tired of waiting for the promised wage and benefit increases. The Mayor replied, “We cannot have a disruption in service.” The Mayor assured the Teamsters representative that San Jose was moving forward on making the payment to Norcal, and the Teamsters representative agreed to wait for San Jose to formally vote to cover the increased costs. When the Secretary-Treasurer of the Teamsters was interviewed by the Grand Jury in April 2005, he insisted that he was unaware of the secret October 9, 2000 deal between Norcal and CWS, i.e., if he had known about Norcal’s promise to pay for the extra costs, the Secretary-Treasurer would have included that important fact in his correspondence to San Jose, Norcal and CWS.

On February 13, 2003, the Secretary-Treasurer of Teamsters Local 350 wrote to the President of CWS that there was an agreement, and that “[the Mayor’s Budget Director], City of San Jose, is working in [sic] the process to provide your company with a subsidy.” No one on the Council ever saw this letter until the Grand Jury showed it to the Councilmembers in March and April 2005.

On February 13, 2003, the President of CWS wrote a letter to the Secretary-Treasurer of Teamsters Local 350 stating “We are working hard with Norcal and the City to secure the subsidy. As you know from the correspondence you got from [the Mayor’s Budget Director] today, the City has not indicated that funds are immediately available which will allow us to execute our agreement with you tomorrow.... I was counting on our agreement that you would not call for a strike while the City and Norcal figured out how to pay the differential on your members’ wages. We have both committed to our agreement and now it is just a matter of timing. We have resolved our differences already and I have been paying Teamster wages and benefits since the inception of my contract. CWS will continue to work hard to secure the necessary subsidy as soon as possible.” Again, the Council was unaware of this letter until the Grand Jury met with the Councilmembers in March and April 2005.

Having been assured by the Mayor that he would deal with the Council, the Teamsters, Norcal and CWS waited for the Mayor to make good on his commitment. Time passed. Norcal called and met with the Budget Director numerous times. The Budget Director repeatedly assured Norcal that it would take time, but the Mayor would present

the issue to the Council in due time. Finally, on May 26, 2004, during a face-to-face conference with the Budget Director at City Hall, the President of Norcal asked for written assurance. The Budget Director went to his office and typed a letter, dated May 26, 2004. This letter, hand delivered to the President of Norcal, states, "I wanted to confirm for you that our office is working with the City Manager and the City Attorney to process a contract amendment pursuant to our previous discussions related to unforeseen labor costs. I am hopeful that we can come to a quick resolution of the issues that are internal to the City and bring forward an amendment to the City Council for approval shortly. Please accept my apologies for the delay in this matter." The President of Norcal stated that when he read the letter, he noticed that it was not on City of San Jose letterhead. He asked that the letter be placed on City letterhead, but the Mayor's Budget Director emphatically responded, "You've got what you're going to get."

There was little likelihood of a strike due to the nonpayment of Teamsters wages, based not only on the secret contract addendum between Norcal and CWS, wherein Norcal was contractually bound to pay, but for other persuasive reasons. Norcal stood to receive close to \$250 million over the projected 11-year term of the contract with San Jose. Norcal was required to post a \$6 million performance bond, which Norcal would likely lose if it failed to pay and the truth about Norcal's contractual obligation to CWS was ultimately discovered. Further, if Norcal or CWS went on strike or walked off the job, the DES had previously assured the Council, during the RFP process, that another vendor was fully capable of taking over the entire operation within 24 hours.

AFTER MORE DELAYS, COSTS ISSUE REACHES COUNCIL IN SEPTEMBER 2004

Despite the Mayor's October 2000 verbal assurances that the reimbursement issue would be presented to the Council for approval, and despite the many letters and communications from Norcal and CWS to the Mayor and his Budget Director, the reimbursement issue was not submitted to the Council until September 2004. Other than a short-term enforcement problem with CWS, there has been no explanation for the four-year delay and the four-year concealment from the Council of the Mayor's commitment to Norcal and CWS that San Jose would be asked to pay for the increased costs.

Prior to actually submitting the reimbursement issue to the Council, the Mayor, through his Budget Director, continued to exchange communications with Norcal and CWS about the reimbursement, but those communications were apparently not shared with the other Councilmembers prior to their vote in September 2004.

Another letter between Norcal and CWS, dated March 11, 2004, discusses the proposed "Second Amendment to Subcontract" between Norcal and CWS. The letter states, "Norcal has requested that the City of San Jose agree to an amendment of the Recycle Plus Agreement to pay for the increased wages for the workers who process the recyclables." It also stated that Norcal and CWS would present a letter, signed by Norcal and CWS to the DES "instructing the City where to direct the Additional Payments." Further, it states, "Norcal and CWS shall at all times utilize their good faith best efforts and work cooperatively to cause the City to agree to such an amendment." The additional payments referenced in this Amendment total approximately \$11.25 million. The Mayor and/or his Budget Director received a copy of this letter and the proposed addendum;

however no one on the Council ever saw this letter until the Grand Jury showed it to Councilmembers in March and April 2005.

On April 6, 2004, Norcal wrote to the DES to ask for an amended agreement that would pay Norcal \$11.25 million. On April 30, 2004 the DES replied, "... [T]here is nothing in the Recycle Plus Agreement that provides for such payments. Additionally, there is nothing in the Agreement that is binding or that imposes any obligation on the City."

On June 16, 2004, Norcal's letter to the City Manager repeats the request for \$11.25 million in additional payments to Norcal. This letter stated that Norcal had discussions with City officials in 2000, without specifying with whom, and that in October 2000, prior to the execution of the Recycle Plus Agreement, "City officials" committed to Norcal that the City would make additional payments to Norcal with respect to these labor costs. [The Grand Jury was told by the President of Norcal that references to "City officials" or "Mayor's office" meant the Mayor and/or his Policy and Budget Director.] On June 25, 2004, the DES advised Norcal that neither the DES nor his staff had any such discussions, and that the Council did not authorize these discussions, and thus any "commitment" made by the unnamed City officials was not binding on the City.

Norcal's July 22, 2004 letter to the City Manager summarized the history involving Norcal, CWS, the Teamsters, the Longshoremen, and the Mayor's office. Norcal knew that CWS wanted to employ workers represented by the Longshoremen's Union to handle the recycling work for San Jose, and that they were paid "considerably less." It was apparent to everyone that these displaced workers would choose to operate under the Teamsters union rather than the Longshoremen's Union. Norcal stated that its request for an additional \$11.25 million was based on the Mayor's office assuring Norcal and CWS in October 2000, a few days before the Council's vote to approve Norcal as a vendor, that once the additional costs for the retention of Teamsters were calculated, that Norcal and CWS should submit the extra costs to the City for an appropriate amendment to the contract, and that the Council would pay those extra costs.

The Mayor and his Budget Director deny that any such assurance or promise was made. Instead, the Mayor and Budget Director contend that they couched their "message" to Norcal such that the Mayor would recommend reimbursement of the increased costs, but any such request for additional costs would be subject to Council approval. Other than the October 6, 2000 conference with Norcal, the Mayor insists that he did not take part in any other such discussions. The Mayor and his Budget Director acknowledge that neither the Mayor nor his Budget Director advised the Council of these October 2000 discussions with Norcal and CWS until four years later, in September 2004. When the Budget Director was asked why he did not disclose such discussions to the Council, the Budget Director stated that he worked for the Mayor, not the Council, and that he had no duty or obligation to advise the Council.

In discussions with the Grand Jury, the City Attorney acknowledged that the Mayor and members of the Council have a mutual duty to disclose any material information that could impact a vote or decision of the Council. The City Attorney cited, and provided a copy of, the City's Code of Ethics, first approved in 1982 and later amended in 1991. This Code of Ethics requires that City employees demonstrate "the highest standard of ethics... the highest standards of integrity and to discharge faithfully the duties of their offices.

Persons in the public service shall uphold the public's right to know, and in accordance with the Brown Act, uphold the public's right to know not only the decisions taken, but also the deliberations which shape public policies."

SEPTEMBER 2004 "END RUN" EFFORT BY MAYOR, BUDGET DIRECTOR AND CITY MANAGER

After assuring Norcal and CWS that the "subsidy" issue would be addressed by the Council, the Budget Director, with the approval of the Mayor and City Manager, decided to attempt an "end run" around the Council. Apparently concerned that the Council might question the wisdom or propriety of paying an \$11.25 million "subsidy" to Norcal, the City Manager's office, with the approval of the Mayor, placed on the September 7, 2004 Council Agenda a vague reference to "unanticipated labor costs" for Norcal:

[Agenda Item] 7.1 Approval to amend the agreement with Norcal for Recycle Plus Integrated Waste Management Services. Recommendation: Amend the agreement between the City and Norcal for Recycle Plus Integrated Waste Management Services by incorporating unanticipated additional labor costs, ensuring prevailing wage, and accepting additional services offered by Norcal. (City Manager's Office)

This Agenda Item did not include any explanation for the amendment, the cost of the unanticipated additional labor costs, or details about any additional services being offered by Norcal. No supporting documents were provided to the Council.

The Agenda Item dealing with "Approval to amend the agreement with Norcal" was modified by the Mayor's office for the September 14, 2004 Agenda, such that the Council was being asked simply to adopt "a resolution authorizing the City Manager and City Attorney to negotiate and authorizing the City Manager to execute an amendment to the agreement between the City and Norcal... to include payment for additional labor costs, contribution to a recycle characterization study, an e-scrap collection and processing program, and bins for 10 additional neighborhood cleanups."

Neither the September 7 nor the September 14 Agenda Items advised the Council of the amount of the unanticipated costs, or any of the details of the Mayor's commitment four years earlier to pay for the additional costs. In fact they incorrectly state that the costs were "unanticipated" when in truth they were anticipated. At least two Councilmembers who read these two Agenda Items for September 7 and September 14 questioned what they meant.

According to several Councilmembers, and based on simple logic, if the Council had voted to approve this Item on September 7 or September 14, 2004, the actual amount of the increase would never have been brought to the Council's or public's attention.

A FEW ALARMED COUNCILMEMBERS RAISE QUESTIONS AND SEEK ANSWERS – MAYOR'S OFFICE INITIATES A "FULL-COURT PRESS"

Councilmembers read the Agenda Item dealing with "Approval to amend the agreement with Norcal", and asked many questions about the details of the alleged unanticipated labor costs, the amount of those costs, and reasons for this Agenda Item. Once it became clear that the Council would discover the actual increased costs of \$11.25

million, the Mayor's Budget Director encouraged Norcal representatives to talk to each of the Councilmembers to sell them on the issue. Norcal representatives then talked to almost every Councilmember, and during these conversations Norcal convinced the majority of them that the Mayor had made a commitment. When interviewed, several of the Councilmembers who voted to approve the \$11.25 million stated that it was their sense that the Mayor's commitment was something they were obliged to honor.

The Budget Director also met with several Councilmembers, and for the first time in four years disclosed to them the issues first raised in October 2000 involving Teamsters vs. Longshoremen and of CWS' increased costs of \$11.25 million.

Three of the Councilmembers, all of whom are attorneys, stated that the payment of \$11.25 million to Norcal would constitute an illegal gift of public funds. The City Attorney agreed with that analysis. The Mayor and his Budget Director then asked the City Attorney to investigate the gift-of-public-funds issue, and, at the urging of the Mayor, the City Attorney came up with a "creative" method to address the issue.

The City Attorney, the Mayor, and every Councilmember interviewed agreed that under the contract between Norcal and San Jose, there was nothing that obligated the City to pay the \$11.25 million. There was near unanimity that, had the Council voted to simply give Norcal the \$11.25 million it requested, it would have been a gift of public funds, and that would have been illegal. So the City Attorney suggested that, if Norcal were to give "something" back to San Jose, even if it were something small, that there could arguably be adequate "consideration" for the \$11.25 million payment. So the City put together a package deal: in exchange for receiving \$11.25 million from San Jose, Norcal would give San Jose up to \$100,000 for a recycle characterization study, plus provide an "e-scrap" collection and processing program for obsolete or damaged computers, monitors and electronics, and provide bins for 10 additional neighborhood cleanups. Several City representatives valued the "consideration" from Norcal at approximately \$150,000.

On September 16, 2004, the Mayor, Vice Mayor and one other Councilmember issued a memorandum recommending approval of an \$11.25 million payment to Norcal. This memo states that it was "...*after* [italics added] Council approval, the Mayor's office learned that the workers to be retained from Waste Management would be expected to change unions. It was then learned that this would mean the retained workers would be taking a pay cut. This would be untenable for vendor, workers, the unions and the City because the result could not meet the Council's desire to have both worker retention and labor peace." *The Mayor's Budget Director acknowledged the word "after" should have been "before" since the Mayor and his Budget Director knew of this problem before the October 10, 2000 vote approving Norcal as a vendor.* This memorandum also states that CWS and the Teamsters ultimately agreed on a new wage rate, and CWS did in fact hire and retain Teamsters rather than Longshoremen. "The new Teamster contract was for higher wages. The Mayor's office told Norcal to request a contract amendment from the City and that he [the Mayor] would recommend to the City Council its approval since these labor costs were clearly unanticipated within the proposal that Norcal made to the City in 2000." Actually these increased labor costs were clearly anticipated by the Mayor and Norcal and CWS prior to the vote in October 2000, as admitted to the Grand Jury by the Mayor, his Budget Director, and the President of Norcal.

The Mayor wrote that, while the Council was not required by its original contract to pay the requested \$11.25 million, there were three legitimate business reasons to pay: (1) settling the labor issues and establishing a better wage for the sorters at the recycling facility is beneficial to the effective delivery of services to San Jose residents; (2) San Jose successfully prevented any work stoppage by avoiding a conflict between the Teamsters and International Longshoremen Workers Union (ILWU); and (3) the overall costs of the proposed amended agreement would still be less than what Green Team or Waste Management would have charged for the same scope of work.

On September 16, 2004, the Deputy City Manager issued a report regarding Norcal's request for \$11.25 million. Attachments include a recycling study and a payment schedule in the event the Council voted to pay the \$11.25 million to Norcal. This report does not recommend a particular action; instead, it sets forth three alternatives: (1) amend the contract as requested, i.e., pay the \$11.25 million; or (2) provide Norcal with a counter proposal, i.e., negotiate for a lesser amount; or (3) decline to amend the contract.

When recently interviewed about this matter, the Mayor and his Budget Director both stated that it did not occur to them to try to negotiate a lesser amount with Norcal. The Councilmembers, who voted in favor of paying the full amount requested, stated that because of the Mayor's prior commitment they felt obliged to pay the full amount. The Councilmembers were unaware of Norcal's willingness to settle for less than the full \$11.25 million.

THE SEPTEMBER 21 AND DECEMBER 14, 2004 VOTES, AND OPPOSITION THERETO

On September 20, 2004, two Councilmembers issued a memorandum opposing the proposed payment of \$11.25 million, for five reasons: (1) the payment of \$11.25 million appeared to be a gift of public funds, since the contract did not contain a provision that would allow for increased payments other than cost-of-living increases; (2) any promise or representation by the Mayor's office to Norcal were not disclosed to the Council when Norcal was approved as the preferred vendor in October 2000; (3) any agreements made with Norcal without Council approval would be a violation of the Charter and void under California law; (4) allowing a side deal to alter the terms of the contract would not be fair to the other vendors who participated in the RFP process but were not made aware of this arrangement; and (5) the additional labor costs are over \$11 million and will have to come from reserves and/or additional rate increases.

On September 21, 2004, the Council voted seven-to-three in favor of authorizing the City Manager to negotiate with Norcal to amend the contract, in exchange for which Norcal agreed to offer the City to fund up to \$100,000 for a recycling material characterization study, operate an e-scrap collection and processing program, and provide bins for 10 additional annual neighborhood clean-ups through June 2007. Note that this vote did not authorize the City Manager to insert the \$11.25 million figure into the amended contract; the City Manger was authorized to "negotiate with Norcal." Proponents of the vote were uniform in their support of the workers "receiving a fair wage."

During the September 21, 2004 Council meeting, one of the Councilmembers opposing the deal stated he had never heard of a labor mediation in which both sides looked at the mediator and said, "How about if you pay?" Another opponent said, "I'm not

comfortable protecting Norcal's profits on the backs of the ratepayers". The third opponent said, "The Mayor does not have the authority to bind the city to pay money for extra labor costs. We are prohibited from making gifts with public funds."

WHAT ABOUT RATE INCREASES?

During the September and December 2004 Council meetings, several Councilmembers questioned whether rates would be increased. In response, the Mayor said there would be no impact on rates. "There is not an extra cost to the ratepayers. The rates are staying the same. We're being able to provide for this within the contract without additional cost to the consumer." The Mayor never disclosed to the Council or public that, one year earlier, in February 2003, his Budget Director and the City Manager calculated that the extra \$11.25 million to Norcal would require a 95-cent rate increase, and this was part of the \$1.50 increase approved *prior to* the September and December 2004 votes.

Keep in mind that, in 2001, the citizens of San Jose were initially advised that, as a result of the substantial savings with the new contracts with Norcal and Green Team, there would be no rate increases until FY 2005-2006. Despite these assurances, there were three rate increases, as noted earlier, totaling 21 percent. Those three rate increases occurred prior to the September 21, 2004 vote to pay Norcal \$11.25 million. The Budget Director and the DES stated subsequently that the \$11.25 million payment "might necessitate a future rate increase."

Coincidentally, citizens of San Jose received a May 6, 2005 Notice of Public Hearing proposing consecutive five-percent rate increases in each of the next three years.

BOTTOM LINE – A FAILURE TO COMMUNICATE AND NEGOTIATE

Between September 21, 2004 and December 14, 2004, the City Manager did not negotiate with Norcal over the amount to be paid to Norcal. There was no effort to settle for a lesser amount. Instead, the City Manager negotiated with Norcal the other terms of the amendment to the contract, and on December 14, 2004, the Council approved the payment of \$11.25 million to Norcal. The Council was not told that Norcal and CWS were willing to accept less than the full amount requested. The Mayor and his Budget Director knew this, but they failed to advise the Council and the City Manager. The same three Councilmembers who voted "No" on the September 21, 2004 vote also opposed the December 14, 2004 vote, but the balance of the Councilmembers voted in favor of paying Norcal the \$11.25 million.

THE GRAND JURY QUESTIONS WHY THE COUNCIL WOULD VOTE TO PAY NORCAL \$11.25 MILLION

During interviews in March and April 2005, several of the Councilmembers, plus the President of Norcal and the Manager of Norcal San Jose, stated that it was their distinct impression that the Mayor and his Budget Director committed to Norcal that San Jose would pay Norcal the \$11.25 million. Further, most of the Councilmembers who voted "Yes" stated that it was "important that the workers be fairly compensated."

No one currently on the Council, including the Mayor, could recall there ever being another time, during their respective terms of office, when the Council voted to amend a contract when the vendor knew in advance of signing the contract with San Jose that the

vendor would incur additional labor costs. The Council's decision to pay Norcal the \$11.25 million apparently represents the first time that this type of action was ever taken.

In March 2005, the Mayor announced to the public that the City was facing a deficit for FY 2005-2006 of approximately \$57 million, and that "tough cuts" in the City's budget would be required to balance the budget. The \$11.25 million payment to Norcal amounts to approximately 20 percent of this budget deficit.

GRAND JURY QUESTIONS WHY THE MAYOR WAS NOT PRIVY TO KEY COMMUNICATIONS

During his second interview with the Grand Jury in April 2004, the Mayor was shown eight documents pertaining to the Norcal and CWS costs issue. The Grand Jury has found that all eight of these documents should have been disclosed to the Council prior to the Council's votes in September and December 2004, as they were all relevant to the issues being voted upon by the Council. The Mayor denied ever seeing any of these documents prior to the Grand Jury presenting them to him. These documents include:

- (1) The October 9, 2000 addendum to the Norcal and CWS contract (recall that this secret document was finally faxed to the Mayor and/or his Budget Director October 7, 2004, two months prior to the December 14, 2004 vote by the Council);
- (2) The January 22, 2003 letter from CWS to Norcal, in which CWS confirms that Norcal and CWS are willing to receive from San Jose less than the full amount desired;
- (3) The February 6, 2003 letter from CWS to the Budget Director which states that CWS will not agree to execute a labor agreement with the Teamsters until CWS receives written direction from the City that it will pay the extra wages and benefits;
- (4) The February 10, 2003 memo from the Budget Director to staff members indicating that a 95-cent per month rate increase would be necessary to pay Norcal what it wanted;
- (5) The February 10, 2003 e-mail from the Mayor's Budget Director to CWS about how the 95-cent rate increase would result in funds to pay CWS' increased costs;
- (6) The February 12, 2003 letter from CWS to the Teamsters, assuring the Teamsters that the Teamsters' threatened strike should be averted because the Budget Director was preparing the requisite documents to ensure that CWS would receive the "labor rate subsidies" from San Jose;
- (7) The February 13, 2003 letter from CWS to the Teamsters about how the Budget Director was working on how to pay the increased costs; and
- (8) The May 26, 2004 letter from the Budget Director to the President of Norcal about processing an amendment to be submitted to the Council.

The Mayor conceded that at least some of those documents should have been provided to the Council, but he had no explanation for why it had not been done.

The Budget Director was confronted with the same eight documents during his second and third interviews with the Grand Jury in April 2005. He confirmed that he had seen all eight documents, three of which were authored by him. The Budget Director stated that he did not provide copies of those documents to the Mayor or to the Council. When asked why he did not do so, he stated that he “virtually never” provides the Mayor with documents. The Mayor does not want the “minutiae.” The Mayor wants the “milestones” so occasionally the Budget Director verbally advised the Mayor of the status. There is no way to document what the Budget Director said to the Mayor, since notes were not taken. The Grand Jury asked for all memoranda, e-mails and communications about the Norcal deal, and neither the Mayor nor the Budget Director ever produced a single communication between the Mayor and his Budget Director.

POLITICAL CAMPAIGN CONTRIBUTIONS

The Grand Jury also investigated political contributions to the Mayor’s and Councilmembers’ political action committee accounts and officeholder accounts.

As of October 10, 2000, the Mayor had apparently received no political contributions from Norcal, CWS, or the Teamsters. Thereafter, in 2001 and 2002, he received \$3,000 from CWS, \$4,500 from Norcal, and \$2,500 from the Teamsters. Between 2000 and the present, Councilmembers received a collective total of \$4,950 from Norcal and \$3,250 from CWS. According to the City Clerk’s files, the Mayor and Councilmembers never received a contribution from the Longshoremen.

CITY INDEPENDENT JUDGMENT POLICY

The San Jose City Council Independent Judgment Policy (effective August 24, 1993) requires that “City officers and employees must be independent, impartial and responsible in the performance of their duties and accountable to members of the public.” This Policy applies to both the members of the Council and the Mayor. Pertinent portions of the Policy state that:

“3. No individual member of the City Council shall present his or her views as being the view of the City or the City Council unless that view reflects an official City position or the member has been officially authorized by the City Council to speak on behalf of the City....

“7. No member of the City Council shall negotiate with any property owner or developer for the grant, loan, payment or forgiveness of any sum of money by the City unless either officially authorized by the City Council to do so or done as part of a coordinated negotiating effort in conjunction with City staff and with an express disclaimer that any proposal is subject to approval by the Council as a whole.”

A DISCUSSION OF POSSIBLE WAYS TO UNDO THE LATEST DEAL WITH NORCAL AND GET THE MONEY BACK

Legal opinions are outside the Grand Jury’s role. However, inasmuch as the City Attorney and City Council had communications about the City’s legal contractual rights and responsibilities in the Norcal matter, the Grand Jury considered those discussions as part of the Grand Jury’s obligation to review the conduct of government. The Grand Jury

suggests that there may be several alternative ways to undo the recent amendment to the contract between San Jose and Norcal.

The general rule is that every contract requires consideration. If one party offers a gift to another party, that is not a contract – it is a gift. But if the second party agrees to give something in return, that can form a contract. On October 9, 2000, Norcal became contractually obligated to pay CWS its increased costs and wage benefits; San Jose was not a party to that contract.

The City Attorney suggested that additional “consideration” of services by Norcal might be sufficient to allow San Jose to pay Norcal \$11.25 million. The Grand Jury considered the concept of “consideration.” It appears to the Grand Jury that, under the definition of “consideration,” doing or promising to do what one is already legally bound to do cannot be consideration for a promise. Thus, when Norcal asked San Jose to reimburse Norcal the \$11.25 million Norcal owed to CWS, Norcal was already contractually obligated to pay CWS. When the Mayor and Budget Director assured Norcal that the Mayor would ask the Council to reimburse Norcal, the Mayor’s assurance was not binding upon the City of San Jose; the Mayor and Norcal knew that the Council would make the final determination on whether to reimburse Norcal.

It appears to the Grand Jury that there are a number of ways to void or rescind San Jose’s amended contract with Norcal. The possible grounds on which to void the amended contract include material mistake of fact by one party, misrepresentation, concealment, actual fraud, and/or economic duress.

In the present case, the San Jose City Council was kept in the dark on two key facts: (1) Norcal and the Mayor convinced the Council that the \$11.25 million involved unanticipated costs, when in reality those costs were anticipated and known to Norcal and the Mayor prior to Norcal being approved as a vendor, and (2) Norcal did not tell the Mayor or Council that Norcal had signed a contract with CWS, promising to pay CWS the increased costs. Thus it appears that the Council could assert that, since it was unaware of the fact that Norcal was already contractually obligated to pay CWS, and that Norcal did not advise the Council of this pre-existing obligation, the Council should seek to rescind the December 14, 2004 amendment to the contract.

Further, Norcal’s October 9, 2000 reimbursement contract addendum with CWS was kept secret from the Mayor, the Council and the Teamsters. Norcal and the Mayor attempted to convince the Council that the extra costs were unanticipated when Norcal was approved as a vendor on October 10, 2000, but in fact those costs were anticipated prior to October 10, 2000.

Finally, it could be argued that the Mayor, unaware that Norcal had signed the October 9, 2000 contract addendum with CWS, was under economic duress to settle the labor dispute to avoid a garbage strike. The Mayor was acting under economic duress when he assured the Teamsters and Norcal that San Jose would pay the extra costs.

In the case of Norcal, it appears that Norcal and CWS set San Jose up to be the “fall guy.” When the Teamsters threatened to strike because the payment package had not been executed, the Mayor felt compelled to step in and settle the dispute rather than face a garbage strike, and thereafter the Council felt obligated to support the Mayor.

The Grand Jury believes that the above discussion about consideration, misrepresentation, concealment, fraud, and economic duress may present viable alternative arguments for rescinding the payment of \$11.25 million.

Conclusions

As the Grand Jury surveys this four-year sequence of events, it appears inexplicable why the Mayor, upon being informed in early October 2000 of increased labor costs for the Norcal/California Waste Solutions proposal, did not immediately notify the Council of the issue. Had he provided that new information to the Council in a timely fashion, the approval process might have been delayed. However, since the actual start of the contract was not until July 1, 2002, there was plenty of time for the Mayor to delay the approval process by several weeks, fully inform the Council of the labor cost issues, and let the Council decide how to address the situation. Instead, the Mayor and his Policy and Budget Director embarked on a four-year course of deception, concealment, and misrepresentation, depriving the City and Council of the truth about material matters concerning the Norcal contract.

The San Jose City Charter, Municipal Code, and policies insist on the highest integrity, ethics, and openness on the part of City officials in the conduct of City business. The Grand Jury believes that the Mayor and his Policy and Budget Director failed repeatedly to adhere to these standards as one instance of concealment and misrepresentation led to another and another. If the Council had studied and known the true facts, it may never have voted to pay Norcal \$11.25 million in exchange for \$150,000 worth of services.

The Grand Jury makes 17 Findings and 10 Recommendations as a result of this inquiry:

Finding 1A

Prior to the Council's first vote on Norcal in October 2000, the Mayor, his Policy and Budget Director, and Norcal knew that CWS would have to pay Teamsters wages instead of Longshoremen wages, and that this would cost CWS an extra \$2 million or more a year. Thus, the Mayor, Norcal, and CWS anticipated the extra labor costs incurred by CWS. The Mayor and his Policy and Budget Director should have advised the Council of this information, but they did not do so, in apparent violation of the City Charter.

Finding 1B

When initially interviewed by the Grand Jury in March 2005, the Mayor and his Policy and Budget Director insisted that the Mayor never met with the representatives of Norcal or CWS. At that time, the Mayor contended that, in order to avoid the appearance of impropriety, he did not meet face-to-face with Norcal or CWS because he did not want to be criticized about "backroom discussions." In the second interview with the Mayor and in the third interview with his Policy and Budget Director, they admitted that indeed such a meeting had occurred on October 6, 2000, in the Mayor's conference room, four days prior

to the Council's vote on October 10, 2000 to approve Norcal as a vendor. The Grand Jury finds that the Mayor indeed met with the Norcal and CWS representatives on October 6, 2000. Either the Mayor and his Policy and Budget Director had a memory lapse or they did not tell the truth initially. In any event, the Mayor took part in "backroom discussions," and this conduct was improper and appears to be in violation of the City's Independent Judgment Policy and/or City Charter.

Finding 1C

At this October 6, 2000 meeting, the Mayor asked Norcal and CWS representatives what the extra labor costs would be, and the President of CWS estimated the first year cost would be approximately \$2 million, with additional increases each succeeding year. The Mayor assured Norcal and CWS that he would take the steps necessary to see that San Jose paid the increased costs.

Finding 1D

For a period of almost four years, between October 2000 and early September 2004, the Mayor and his Policy and Budget Director *concealed from the Council*: (a) the occurrence of the October 6, 2000 "backroom discussion" the Mayor had with Norcal and CWS; (b) the Mayor's October 6, 2000 assurance to Norcal and CWS that the Mayor would take the steps necessary to have San Jose pay the increased costs; (c) that the increased costs were known and anticipated prior to the Council's October 10, 2000 vote; (d) that Norcal was willing to take less than the \$11.25 million it requested; (e) that the primary purpose of the proposed nine percent garbage rate increase in FY 2003-2004 was to cover the increased costs to Norcal; and (f) that the threatened strike by the Teamsters in February 2003 was primarily caused by the Mayor's delay in asking the Council to pay Norcal the \$11.25 million.

Finding 1E

The Mayor and his Policy and Budget Director made *several misrepresentations* to the City Council and the public, including: (a) that the increased costs were unanticipated prior to the October 10, 2000 vote, when in fact they were anticipated; (b) that the Mayor found out about the increased costs after the October 10, 2000 vote to approve Norcal as a vendor, when in fact he knew beforehand; (c) that the proposed nine percent garbage rate increase in FY 2003-2004 was needed for reasons other than to reimburse Norcal; and (d) that the Mayor stated that there would be no garbage rate increases as a result of the Council's decision to pay Norcal the \$11.25 million, when other City representatives have admitted that further increases would be required to fund the \$11.25 million payment to Norcal.

Finding 1F

The Grand Jury agrees with the two Councilmembers' September 20, 2004 memorandum opposing payment of \$11.25 million, including the assertions that:

- (a) The payment of \$11.25 million appears to be a gift of public funds. The only way San Jose would have been justified in paying Norcal \$11.25 million was if Norcal had provided consideration of \$11.25 million in additional services; instead Norcal was offering at most \$150,000 in additional services;
- (b) The October 2000 promise or representation by the Mayor to Norcal was not disclosed to the Council when the Council voted to approve Norcal as the preferred vendor in October 2000;
- (c) The Mayor's assurance to Norcal to pay Norcal the extra labor costs, without Council approval, appears to be a violation of the City Charter and void under California law;
- (d) Allowing a side deal to alter the terms of the contract was not fair to the other vendors who participated in the Request For Proposal process but were not made aware of this arrangement; and
- (e) The additional labor costs amount to \$11.25 million and will have to come from reserves and additional rate increases.

Finding 1G

There were many discrepancies or versions of the facts related by the 18 people who were interviewed in this investigation by the Grand Jury. It appears that some of these individuals were not telling the truth, but at times it was difficult for the Grand Jury to determine, with reasonable certainty, fact from fiction. By the nature of this inquiry, these individuals were not under oath and their statements were not recorded. The Grand Jury finds that the only way to ascertain all of the facts, and the ultimate truth, is to have everyone testify under oath and under penalty of perjury.

Recommendation 1

The San Jose City Council should retain the services of a special investigator to:

- (a) Determine if the Mayor and/or the Mayor's Policy and Budget Director or other key City employees violated San Jose's Charter, Municipal Code, Independent Judgment Policy, ordinance, or any state code;
- (b) Determine if the Council's vote to pay Norcal \$11.25 million constituted a gift of public funds;
- (c) Determine if a reprimand, censure, or other sanction should be recommended against the Mayor, his Policy and Budget Director, or other key employees of the City of San Jose, if any are found to have acted inappropriately; and

- (d) Conduct an open hearing wherein the Mayor, his Policy and Budget Director, the City Attorney, the City Manager, the Director of Environmental Services, the members of the Council, and other key employees of the City of San Jose will be asked questions under oath by the special investigator to ascertain what they knew, when they knew it, and what actions they took. If such conduct is inappropriate, the special investigator should recommend what reprimand, censure, or other sanctions to impose.

Finding 2

At the October 6, 2000 meeting, the President of Norcal advised the Mayor that, if the City of San Jose agreed to pay for the increased costs, Norcal would pass San Jose's payment on to CWS. After this meeting, outside the presence of the other parties, Norcal and CWS then signed an addendum to their contract that was kept *secret* from the City of San Jose. This addendum, dated October 9, 2000, expressly stated that Norcal would pay CWS for the increased costs CWS would incur as a result of CWS having to use Teamsters. This addendum was *not* contingent upon the City of San Jose reimbursing Norcal. The terms of this addendum were not divulged to anyone at the City of San Jose for a period of four years, until October 7, 2004, when Norcal's attorney provided it to the City Attorney. By that time the City Council had already voted on September 21, 2004 to authorize the City Manager to negotiate the terms of the increased payment to Norcal. The Grand Jury finds that Norcal, not the City of San Jose, owed CWS the \$11.25 million, and that Norcal appears to have defrauded the City of San Jose by not disclosing the secret contract addendum.

Recommendation 2

The City Attorney or special investigator (see Recommendation 1) retained by the San Jose City Council should take the legal steps necessary to rescind the amended contract with Norcal. The rescission would be based on the fact that Norcal did not disclose to the Council the secret contract addendum between Norcal and CWS, and that Norcal thereby defrauded the City of San Jose. A rescission would result in the return of the millions of dollars San Jose has already paid to Norcal and CWS, and preclude any further payments to Norcal and CWS related to the amended contract. The return of the money would be subject to a reduction of the so-called extra "consideration" given by Norcal, which the Grand Jury believes has a value of approximately \$150,000.

Finding 3

No one on the Council, including the Mayor, could recall another time when the Council voted to amend a contract to pay a vendor additional funds, when the vendor knew, in advance of signing a contract with the City of San Jose, that the vendor would incur additional labor costs. The reason for this is fundamental: once a contract is signed, the parties are required to adhere to the terms of the contract. The Grand Jury has difficulty understanding how the Council could be duped into paying Norcal an extra \$11.25 million when San Jose had no contractual obligation to do so.

Recommendation 3

San Jose should place in its Charter a provision that henceforth it shall never consider amending an existing contract with any vendor, wherein the vendor is aware of actual anticipated additional costs prior to being approved as the vendor.

Finding 4

The Mayor and his Policy and Budget Director knew that Norcal was willing to take less than \$11.25 million, but the Mayor chose not to negotiate, and the Mayor did not advise the Council that Norcal would take less than the \$11.25 million. Further, the City Manager and Director of Environmental Services were authorized to negotiate with Norcal, but they made no effort to negotiate a lower settlement before the Council voted to approve the \$11.25 million reimbursement. The Grand Jury observed that the Mayor and Councilmembers received contributions from Norcal and CWS, but could not determine what might have motivated the City's actions.

Recommendation 4

In addition to the steps detailed under Recommendation 1, the special investigator should determine why the City Council chose to pay the entire \$11.25 million to Norcal rather than, at a minimum, trying to settle for a lesser amount. The special investigator should:

- (a) Determine if some influence, such as political contributions from Norcal, CWS, their employees, and the Teamsters, played a role in the conduct of the Mayor or the Councilmembers who voted in favor of the \$11.25 million payment; and
- (b) Determine if a reprimand, censure, or other sanction should be recommended against the Mayor, his Policy and Budget Director, other key employees, or the members of the Council who voted in favor of paying Norcal the \$11.25 million, should any be found to have acted inappropriately.

Finding 5

The October 6, 2000 meeting was initiated and chaired by the Mayor and it was held at the Mayor's conference room at City Hall. The Mayor made it clear to the Norcal and CWS representatives that he wanted labor peace and he wanted the Teamsters to represent the CWS workers. It appears that the Mayor's intervention on behalf of the Teamsters may have been a violation of federal and/or state labor law.

Recommendation 5

The special investigator (see Recommendation 1) should determine if the Mayor violated federal and/or state labor laws and, if so, report the result to the appropriate authorities.

Finding 6

The current Councilmembers *who were part* of the Council in September 2000, and who were interviewed by the Grand Jury, acknowledged that they never read the documents pertaining to Norcal's history and Norcal's reply to the Request for Proposal, and, as a result, were unaware of Norcal's problematic history in San Bernardino County.

Recommendation 6

Councilmembers should be required to review staff reports pertaining to long-term contracts involving millions of dollars of public funds. Each Councilmember should sign a check-off sheet to verify that: (a) they received the staff report; and (b) they reviewed and considered it prior to voting.

Finding 7

The current Councilmembers *who were not part* of the Council in September 2000, and who were interviewed by the Grand Jury, acknowledged that they never read the documents pertaining to Norcal's history and Norcal's reply to the RFP, and, as a result, were unaware of Norcal's problematic history in San Bernardino County.

Recommendation 7

When a new Councilmember is elected, and thereafter a vote is to be taken on a contract in excess of one million dollars that has been previously discussed and voted on, the new Councilmember should be required to review the prior staff reports and the prior minutes, and file a statement with the City Clerk that the prior staff reports and minutes have been reviewed.

Finding 8

Between January 2000 and December 31, 2004, every Councilmember received political contributions, including from Norcal.

Recommendation 8

Prior to any vote on a contract in excess of one million dollars involving any party or entity that has contributed to one or more of the members of the City Council, the City Clerk's office should prepare a staff report that identifies the names and affiliations of the contributors, the names of the recipients, and the dates and amounts of the contributions. This staff report should be available prior to any discussion or consideration of such proposed contract.

Finding 9

The Mayor and/or his Policy and Budget Director received several relevant communications from Norcal, CWS and Teamsters. The Mayor and his Policy and Budget Director had a duty to disclose and provide those documents to the Council, but failed to do so.

Recommendation 9

When the Mayor's office or any Councilmember receives written communications from a vendor, a lobbyist or union representative involving a planned contract or existing contract in excess of one million dollars, the Mayor or Councilmember should assure that copies of all such communications are provided in a timely fashion to the City Clerk, who will have the responsibility to provide copies to every member of the Council.

Finding 10

The Mayor's Policy and Budget Director authored several communications to Norcal and CWS. Copies of those communications apparently were not provided to the Council prior to the Council's vote.

Recommendation 10

When the Mayor's office authors written communications to a vendor, a lobbyist or union representative involving a planned contract or existing contract in excess of one million dollars, the Mayor's office shall ensure that copies of all such communications, and any responses thereto, are provided in a timely fashion to the City Clerk, who will have the responsibility to provide copies to every member of the Council.

Finding 11

The three Councilmembers from Districts 1, 4 and 8 are commended for their efforts in opposing the increased payments to Norcal. These three Councilmembers demonstrated exceptional integrity and courage in voicing their concerns, in criticizing the Mayor's conduct, and in attempting to save the City \$11.25 million.

Recommendation 11

None.

PASSED and ADOPTED by the Santa Clara County Civil Grand Jury on this 26th day of May 2005.

Michael A. Smith
Foreperson

References

Documents

1. City Council Policy entitled "Independent Judgment Policy" dated August 23, 1993
2. Political Action Committee & Officeholder Files for Mayor and Councilmembers, maintained by San Jose City Clerk, between 1998 and the present.
3. San Jose's Request for Proposal No. 003-00, dated May 2, 2000
4. Mayor's recommendation to City Council, dated June 26, 2000
5. Director of Environmental Service's (DES) Recommendation dated September 22, 2000
6. Norcal letter to DES, dated September 28, 2000
7. Norcal letter to Mayor of San Jose, dated October 4, 2000
8. Norcal letter to Teamsters Local 350, dated October 4, 2000
9. CWS letter to Mayor, dated October 4, 2000
10. DES memorandum to Mayor and City Council, dated October 6, 2000
11. Mayor's recommendation to City Council, dated October 8, 2000
12. Addendum to Agreement between Norcal and CWS, dated October 9, 2000
13. Minutes of October 10, 2000 City Council meeting, plus attachments thereto
14. DES memorandum to Mayor and City Council, dated October 30, 2000
15. Minutes of December 12, 2000 City Council meeting, plus attachments thereto
16. DES memorandum to 2002 Recycle Plus Follow-up, dated December 3, 2000
17. Mayor's recommendation to City Council, dated December 8, 2000
18. City Auditor's report to City Council, dated December 8, 2000
19. DES memorandum to Mayor and City Council, dated December 12, 2000
20. City Attorney's memorandum to Mayor and City Council, dated October 27, 2000
21. Minutes of March 27, 2001 City Council meeting, plus attachments thereto
22. Contract between San Jose and Norcal, dated March 21, 2001
23. DES memorandum dated November 25, 2002
24. Minutes of December 17, 2002 City Council meeting
25. CWS letter to Norcal, dated January 22, 2003
26. Second Amendment to Subcontract between Norcal and CWS, dated March 11, 2004
27. Norcal letter to DES, dated April 6, 2004
28. DES letter to Norcal, dated April 30, 2004

Documents (cont'd.)

29. Minutes of June 15, 2004 City Council meeting
30. Norcal letter to DES, dated June 16, 2004
31. DES letter to Norcal, dated June 25, 2004
32. Norcal letter to City Manager, dated July 2, 2004
33. Norcal letter to City Manager, dated July 22, 2004
34. Agenda item for September 7, 2004 City Council meeting
35. Recommendation by Mayor to City Council, dated September 16, 2004
36. Deputy City Manager's memorandum to Mayor and City Council, dated September 16, 2004
37. Agenda item for September 21, 2004 City Council meeting
38. Memorandum from two Councilmembers to Mayor and City Council, dated September 20, 2004
39. Minutes of September 21, 2004 City Council meeting
40. Videotape of September 21, 2004 City Council meeting
41. DES and Deputy City Manager recommendation to Mayor and City Council, dated December 14, 2004
42. Videotape of December 14, 2004 City Council meeting

Interviews

1. District 8 Member of City Council, 23 Feb. 2005
2. District 1 Member of City Council, 28 Feb. 2005
3. District 4 Member of City Council, 4 March 2005
4. Director of Environmental Services Department and Deputy City Manager, 16 Mar. 2005
5. San Jose Mayor's Director of Budget and Policy, 2 March 2005, 20 April 2005, and 26 April 2005
6. Mayor of San Jose, 14 March 2005 and 22 April 2005
7. District 2 and 9 Members of City Council, 30 March 2005
8. Norcal, Inc. President and Norcal, Inc. General Manager of Norcal's San Jose facility, 4 April 2005
9. District 3, 5, 6 Members of City Council, 11 April 2005
10. San Jose City Attorney, 11 April 2005
11. President of California Waste Solutions, Inc., 14 April 2005
12. Secretary-Treasurer of Teamsters Local 350, 14 April 2005
13. Former Norcal General Manager of Norcal San Jose, 25 April 2005

Correspondence

1. Document request from Grand Jury to City Clerk, e-mail 14 February 2005
2. Document request from Grand Jury to County of San Bernardino, 22 March 2005
3. County of San Bernardino letter to Grand Jury, 24 March 2005