Avoiding the Fiscal Cliff: Lessons from the Stockton Bankruptcy

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The Stockton Case

• Stockton, California, filed Chapter 9 on June 28, 2012. citing:
  – Prior poor fiscal management
  – Overspending on downtown improvement projects,
  – The general economic turndown of 2008,
  – The resulting decline in real estate transactions and values,
  – High unemployment rates,
  – Lower collections of tax revenues and user fees
At the September 2013 Meeting of the California League of Cities, Vice Mayor Kathy Miller added to the list:

- Unsustainable and Unsupported Labor Contracts (including pensions and add-ons)
- State Raids on City Finances
But this catalogue of woes describes many of California’s 482 cities; why does Stockton capitulate to them?

• Unique history of neglect by state government
• Unique location on rim of two world cities, San Francisco and San Jose
• Unique struggle to right municipal government and to fulfill a dream to be a recognized as a player in the Bay Region
Viewing Stockton's Tsunami through three lenses?

I. Stockton as a supplicant of the state
II. Stockton as a vassal of two world cities
III. Stockton as an immature political system
   A. A political culture seeking respect
   B. A political structure limiting dissent
   C. Oscillation in political leadership between activists and caretakers
“Proposition 13 marks the beginning of a new era in California fiscal governance. This 1978 initiative has profound significance for the fiscal relations between the state and its local governments”. Mark Baldassare, When Government Fails: The Orange County Bankruptcy
Supplicants Negotiate after 1978
Examples of Stockton As Supplicant

• **Revenue**: property and sales taxes are 60% of General Fund revenues as against 43% for the average city (2009); lack of diversity creates vulnerability to market forces.

• **Expenditures**: Budget heavily weighted toward public safety: 35% in comparison to 27% for average city (2009); reflects state preference for public safety support.

• **Uneven state support of public works and facilities**: mental health and prison closures, freeways slow, university not provided. marina development is one of few grants.

• **Regulation**: General Plan oversight and settlement agreement

• **Redevelopment Agency**: terminated 2011-12; state requests $1,361,531 in repayment
Supplicant Survival

• “State and local governments have employed a range of tactics to replace the money seized by the tax revolutionaries: these include the passage of special taxes, especially parcel taxes, fees and charges for a wide range of services, lease backs, and bond financing”

Jack Citrin, “Proposition 13 and the Transformation of California Government” in After the Tax Revolt: California’s Proposition 13 Turns Thirty.
Stockton adopts Survival Skills

- **Lease backs** on Planned City Hall Building, Fire, Police and Library buildings, an Arena, parking structures, two golf courses and a park
- **Hiring of lobbyist, grants writers**
- **Bond Financing** for pension increases
- **Fees/taxes** on business licenses, utility use, transient occupancy (hotels), franchise fees for use of streets, fines
Worries of a Supplicant

- **Limited flexibility** in generating general fund revenue
- **Uncertainty** concerning revenue streams over time; limited planning opportunities
- **Complex financial instruments** become attractive, often leading to borrowing from the future to pay for current expenditures
- Many revenue sources **fluctuate with markets** that the city does not control
- State not a reliable partner **regarding facilities**
- Lines of representation to legislature often confused by gerrymandering.
VASSELS OF WORLD CITIES I
Northern California MSAs, per capita income 1969-2012

- Stockton per capita personal income
- San Francisco per capita personal income
- San Jose per capita personal income
- Sacramento per capita personal income
- Modesto personal income
Commuting to and from San Joaquin County (Stockton), 2006-2010
(Source: US Census, Table 2. Residence County to Workplace County Flows for the United States and Puerto Rico Sorted by Workplace Geography: 2006-2010)

<table>
<thead>
<tr>
<th>Commutes from Stockton to</th>
<th>Number Daily</th>
<th>Margin of Error</th>
<th>Number of Commutes to Stockton</th>
<th>Margin of Error</th>
<th>Ratio to/from Stockton</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alameda County (Oakland)</td>
<td>26,121</td>
<td>1,276</td>
<td>1,856</td>
<td>287</td>
<td>1/14.1</td>
</tr>
<tr>
<td>Santa Clara County (San Jose)</td>
<td>7,954</td>
<td>590</td>
<td>497</td>
<td>150</td>
<td>1/16</td>
</tr>
<tr>
<td>Contra Costa County</td>
<td>5,377</td>
<td>633</td>
<td>1,903</td>
<td>360</td>
<td>1/2.8</td>
</tr>
<tr>
<td>San Francisco County</td>
<td>2,582</td>
<td>413</td>
<td>82</td>
<td>68</td>
<td>1/31</td>
</tr>
<tr>
<td>Total to West</td>
<td>42,034</td>
<td>4,338</td>
<td></td>
<td></td>
<td>1/10</td>
</tr>
<tr>
<td>Stanislaus County (Modesto)</td>
<td>10,040</td>
<td>674</td>
<td>17,140</td>
<td>1,087</td>
<td>1.7/1</td>
</tr>
<tr>
<td>Sacramento County</td>
<td>7,805</td>
<td>970</td>
<td>8,151</td>
<td>660</td>
<td>1.04/1</td>
</tr>
<tr>
<td>Total North and South</td>
<td>17,845</td>
<td>25,291</td>
<td></td>
<td></td>
<td>1.4/1</td>
</tr>
<tr>
<td>Internal (San Joaquin County) commuting</td>
<td>193,718</td>
<td>2,627</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>External/Internal commute ratio</td>
<td>1/3.2</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Vassel as “staging area”

- Due to the centralized location of San Joaquin County, it has cultivated extensive transportation facilities: Interstate 5 and 99, railroads, and the Stockton Airport. With this transportation system in place, San Joaquin County is a central staging area and meeting place in California.”
  Colliers International, 2012

- “…the thing about Stockton…{is}…that Stockton is a hub for narcotics trafficking, in particular methamphetamine. You’ve got Interstate 5, which is a major corridor for narcotics, so you’re coming through this town to get a source of methamphetamine, and then you’re shipping it somewhere else….Drugs and violence go hand in hand.”
  AFT agents after a 2013 bust reported by Jason Anderson, Stockton Record, 8.26.13.
### Employment by Industry, Stockton MSA/California

California Employment Development Department
(Stockton MSA covers all of San Joaquin County)

<table>
<thead>
<tr>
<th>Industry</th>
<th>Stockton MSA 2000</th>
<th>Stockton MSA 2008</th>
<th>% increase</th>
<th>California 2000</th>
<th>California 2008</th>
<th>% increase</th>
</tr>
</thead>
<tbody>
<tr>
<td>Labor Force</td>
<td>258,000</td>
<td>297,200</td>
<td>15%</td>
<td>16,857,500</td>
<td>18,391,800</td>
<td>9%</td>
</tr>
<tr>
<td>Transport, warehousing, utilities</td>
<td>11,700</td>
<td>14,300</td>
<td>22%</td>
<td>518,300</td>
<td>505,800</td>
<td>-2%</td>
</tr>
<tr>
<td>Education, health services</td>
<td>22,000</td>
<td>28,500</td>
<td>30%</td>
<td>1,401,000</td>
<td>1,725,300</td>
<td>23%</td>
</tr>
<tr>
<td>Farm</td>
<td>16,700</td>
<td>14,900</td>
<td>-11%</td>
<td>408,500</td>
<td>390,900</td>
<td>-4%</td>
</tr>
<tr>
<td>Wholesale trade</td>
<td>6,400</td>
<td>10,500</td>
<td>64%</td>
<td>646,200</td>
<td>706,600</td>
<td>9%</td>
</tr>
<tr>
<td>Government</td>
<td>37,000</td>
<td>40,300</td>
<td>9%</td>
<td>2,318,100</td>
<td>2,519,300</td>
<td>9%</td>
</tr>
</tbody>
</table>
Comparison of Stockton and Modesto's rankings with rankings of the largest 100 Metropolitan Areas with attention to Northern California and Central Valley Metros

<table>
<thead>
<tr>
<th></th>
<th>Stockton</th>
<th>Modesto</th>
<th>San Francisco</th>
<th>San Jose</th>
<th>Sacramento</th>
<th>Fresno</th>
<th>Bakersfield</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Magnitude of Recession: Peak to Trough</strong></td>
<td>95th</td>
<td>93th</td>
<td>75th</td>
<td>72th</td>
<td>89th</td>
<td>84th</td>
<td>81th</td>
</tr>
<tr>
<td><strong>Employment</strong></td>
<td>90th</td>
<td>76th</td>
<td>61th</td>
<td>72th</td>
<td>87th</td>
<td>78th</td>
<td>73rd</td>
</tr>
<tr>
<td><strong>Unemployment</strong></td>
<td>99th</td>
<td>96th</td>
<td>69th</td>
<td>82nd</td>
<td>86th</td>
<td>94th</td>
<td>90th</td>
</tr>
<tr>
<td><strong>Gross Domestic Product</strong></td>
<td>83rd</td>
<td>81rd</td>
<td>72th</td>
<td>58th</td>
<td>85th</td>
<td>67th</td>
<td>11th</td>
</tr>
<tr>
<td><strong>Housing Prices</strong></td>
<td>98th</td>
<td>100th</td>
<td>78th</td>
<td>70th</td>
<td>90th</td>
<td>91st</td>
<td>95th</td>
</tr>
<tr>
<td><strong>Size of Recovery, Peak to 2013</strong></td>
<td>97th</td>
<td>93th</td>
<td>14th</td>
<td>1st</td>
<td>28th</td>
<td>44th</td>
<td>57th</td>
</tr>
<tr>
<td><strong>Employment</strong></td>
<td>90th</td>
<td>80th</td>
<td>41st</td>
<td>22nd</td>
<td>89th</td>
<td>84th</td>
<td>9th</td>
</tr>
<tr>
<td><strong>Unemployment</strong></td>
<td>97th</td>
<td>94th</td>
<td>21st</td>
<td>18th</td>
<td>66th</td>
<td>96th</td>
<td>79th</td>
</tr>
<tr>
<td><strong>Gross Domestic Product</strong></td>
<td>87th</td>
<td>88th</td>
<td>64th</td>
<td>6th</td>
<td>89th</td>
<td>78th</td>
<td>17th</td>
</tr>
<tr>
<td><strong>Housing Prices</strong></td>
<td>98th</td>
<td>100th</td>
<td>72nd</td>
<td>51st</td>
<td>88th</td>
<td>94th</td>
<td>93th</td>
</tr>
</tbody>
</table>

(Source: Metro Monitor, Brookings Institution, September, 2013)
### New Housing Units Based on Finalized Building Permits 2000-2011

<table>
<thead>
<tr>
<th>Year</th>
<th>Total</th>
<th>Single-Family</th>
<th>2-4 Units</th>
<th>5+ Units</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>1,163</td>
<td>1,135</td>
<td>12</td>
<td>16</td>
</tr>
<tr>
<td>2001</td>
<td>1,534</td>
<td>1,534</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>2002</td>
<td>1,750</td>
<td>1,675</td>
<td>3</td>
<td>72</td>
</tr>
<tr>
<td>2003</td>
<td>2,866</td>
<td>2,555</td>
<td>11</td>
<td>300</td>
</tr>
<tr>
<td>2004</td>
<td>2,945</td>
<td>2,640</td>
<td>39</td>
<td>266</td>
</tr>
<tr>
<td>2005</td>
<td>2,706</td>
<td>2,571</td>
<td>22</td>
<td>113</td>
</tr>
<tr>
<td>2006</td>
<td>1,507</td>
<td>1,392</td>
<td>29</td>
<td>86</td>
</tr>
<tr>
<td>2007</td>
<td>836</td>
<td>750</td>
<td>16</td>
<td>70</td>
</tr>
<tr>
<td>2008</td>
<td>342</td>
<td>311</td>
<td>10</td>
<td>21</td>
</tr>
<tr>
<td>2009</td>
<td>257</td>
<td>196</td>
<td>6</td>
<td>55</td>
</tr>
<tr>
<td>2010</td>
<td>162</td>
<td>162</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>2011</td>
<td>182</td>
<td>131</td>
<td>1</td>
<td>50</td>
</tr>
</tbody>
</table>

**Total**

<table>
<thead>
<tr>
<th>Total</th>
<th>16,250</th>
<th>15,052</th>
<th>149</th>
<th>1,049</th>
</tr>
</thead>
</table>

**Annual Avg.**

<p>| | | | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Total</td>
<td>1,354</td>
<td>1,254</td>
<td>12</td>
<td>87</td>
</tr>
</tbody>
</table>

Source: City of Stockton Community Development Department, 2011
What Does “Vassal hood” mean?

- **Functional Specialization**: Transit Center, Exurban Location (warehouse people and goods, legal and illegal)
- **Limited control** over demography and economic growth or flexibility
- **Middle and Lower Classes**: limited resources
- **Limited Participation** in regional planning or defining regional identity
- **Difficulty** attracting private capital
- **Domination** by national/international capital
Stockton: Immature Politics I

• Political Culture
  – Inferiority complex; tends to accept definition as evolving ex-urb, transit hub
  – Approach/Avoidance attitude toward Bay Region
  – Resistance to identification with agriculture and Delta
  – Tolerant of development, construction
  – Vulnerability to public safety challenges: fire and police.
  – Skeptical of government; distrust of federal government in particular
I. Structure with few Checks and Balances

- At Large General Elections (Primaries in Districts)
- Dual Executive System (strengthened Mayor and City Manager, but in practice, Mayor guides the appointment of manager)
- Non-Partisan elections
- Only two interest groups actively engaged: developers and union; both are pro-growth
- One outlet for local news: Stockton Record
- Failure to incorporate poor, people of color
Stockton: Immature Politics III

• Leadership
  – Darrah/Milnes Administration, 1990-96
    • Professionalize with good salaries and benefits
  – Podesto/Lewis Administration, 1996-04
    • Public/Private Partnerships with financial instruments
  – Chavez/Palmer Administration, 2005-08
    • General Planning without fiscal oversight
  – Johnston/Deis Administration, 2009-12
    • Fiscal Contraction, then Bankruptcy
  – Silva/Wilson Administration, 2013-Present
    • Crime fighting and anti-elite rhetoric
Stockton Leadership Styles

– Darrah/ Milnes Administration, 1990-96
  • Alex Smith; 49er: a “game manager”
– Podesto/Lewis Administration, 1996-04
  • Tony Romo;: Dallas: a “high risk/high rewards” guy
– Chavez/Palmer Administration, 2005-08
  • Kyle Orton; Dallas backup: low-key, conservative
– Johnston/Deis Administration, 2009-12
  • Brett Favre/Aaron Rogers; Packers: brash, calculating
– Silva/Wilson Administration, 2013-Present
  • Too soon (Mike Klocke, Stockton Record, 1/12/14)
Challenge of Data Driven Government: Expertise

Figure 5. DoF and BFC Population Projections, 2010-2040
The new interim projection by the Dept. of Finance falls between our 2008 and 2012 baseline projections.

Tendency to Predict Future from Past

- Curve Tracing Revenues
CALPRES and Ballooning Pensions

1. Total General Fund Retirement Costs as a Percent of Total Expenditures
Stockton Leadership Lapses

• Reliance on expert opinion
  – Demographics
  – Financial Instruments
• Limited transparency with public and council
  – Control of fiscal agendas
• Preference for consensus over conflict
  – Most votes unanimous on compensation, facilities
• Narrow community networks
• Problem-solving over Strategic Planning
<table>
<thead>
<tr>
<th>Actors ➔ Causes of Bankruptcy ➙</th>
<th>World Cities</th>
<th>State of California</th>
<th>Local Structure</th>
<th>Local Political Culture</th>
<th>Local Patterns of Leadership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Poor Fiscal Management</td>
<td>Low oversight</td>
<td>Weak Checks and Balances</td>
<td>Eyes on a Prize, not the process</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Downtown Improvements</td>
<td>Sale of Complex Instruments</td>
<td>Re-development Authorization</td>
<td>Obscure Fiscal Decisions</td>
<td>Few reserves</td>
<td></td>
</tr>
<tr>
<td>Economic Downturn</td>
<td>Financial Meltdown</td>
<td>Slow mortgage assistance</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Drop in Real Estate Values</td>
<td>Exporting of the financially weak</td>
<td>Little assistance</td>
<td>Wants single family homes</td>
<td>Dream of suburbia and warehousing</td>
<td></td>
</tr>
<tr>
<td>High Unemployment</td>
<td>Expendable jobs</td>
<td>Limited infrastructure projects</td>
<td>Dream of suburbia and warehousing</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Low tax and user fees</td>
<td></td>
<td>Power of interest groups</td>
<td>Anti tax</td>
<td>Unwilling to tax</td>
<td></td>
</tr>
<tr>
<td>Labor Contracts</td>
<td>Bay Area examples, competition</td>
<td>CALPERS encourages</td>
<td>Low oversight; union power</td>
<td>Desire for professionals without fiscal planning</td>
<td></td>
</tr>
<tr>
<td>Debts</td>
<td>Investors encourage</td>
<td>Low oversight</td>
<td></td>
<td>Desire to be an entrepreneur</td>
<td></td>
</tr>
<tr>
<td>State Raids on Funding</td>
<td>Poor state fiscal management; centralized funding</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Lessons from Application of First Lens: Relationship with State

• Stockton as Supplicant
  – Press for fiscal home rule whereby cities gain control of portion of income tax or value added tax.
  – Resist provision of human resource services by the state (CALPERS)
  – Improve coordination between City Hall and legislative representatives
  – Participate in regional compacts in preference to statewide policies
Lessons from Second Lens: Relationship with World Cities

• Stockton as Vassal
  – Need to self-define future independent of the World Cities (embrace Delta and Agriculture)
  – Need to be included in regional planning (new census computation should help)
  – Dramatically improve educational mix to attract diverse businesses
  – Value of home grown leaders who value Stockton as place (reclaim the young)
Lessons from Application of Third Lens: Immature Political System

• Stockton as Immature
  – Encourage increase media attention to local politics
  – “Incorporate” of poverty/minority communities
  – Recruit mayors with diverse networks
  – Help Stockton identify and value its unique qualities
  – Incorporate difference into policy process
    • Encourage greater interest group participation
    • Reconsider power of mayor to nominate managers
    • Engage in transparent strategic fiscal planning