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Struggling California Cities Vallejo and Richmond Take Different Financial Tacks

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By [Andrew Ward](#)

SAN FRANCISCO - Vallejo, Calif., and nearby Richmond are both old industrial towns in the San Francisco Bay Area. Both suffer high jobless rates. Both are working-class towns in a region that is better known for its wealth and high technology industry. And both want to attract outside capital to redevelop their waterfronts.

But the similarities end when it comes to how each city has handled its finances as of late.

Vallejo announced it would file for bankruptcy last week - the city had not filed as of yesterday - and saw the ratings for various city-related bond issues slashed. Richmond last week earned an upgrade from Standard & Poor's to A-plus from A, just four years after a financial crisis of its own in 2004.

"The difference in Richmond is management," said Gabe Petek, an analyst for Standard & Poor's in San Francisco. "Very strong management over the past few years has really paid off."

The story of these two cities shows how differing strategies for development and financial management can yield drastically different outcomes despite seemingly similar starting points. The results matter because they'll decide which of the two cities will be able to attract the investments and workers that will allow them to develop, grow and provide essential government services.

"It's certainly going to make it very, very difficult to go ahead with our waterfront and our downtown project," said Vallejo Mayor Osby Davis in an interview. He said he hopes to garner economic development through private investment even if the city itself can't tap the bond market.

His city, with a population of 116,800, is slightly larger and wealthier than Richmond. The city's median family income was \$67,000 in 2006, according to the U.S. Census Bureau. Richmond, with 102,120 residents, had a median family income of about \$55,000.

Both cities face a sharp contraction in their housing markets, and above-average unemployment rates. Again, Richmond's data is weaker. Vallejo's jobless rate averaged 6.7% in 2007, while Richmond averaged 7.9%.

A key difference between the two cities is how they have reacted to economic weakness. The Vallejo City Council voted unanimously last week to declare bankruptcy in an attempt to get out from under union contracts that current policymakers say the city can't afford. Davis, who has been in office for about six months, readily admits that the city's woes are of its own making.

"It's a policy problem," Davis said. "It's not an economic problem and it never has been."

The Vallejo Finance Department projects that it will deplete its general fund reserves by the end of this

fiscal year and spend \$16.6 million more than it brings in next year. Vallejo's most recent certified annual financial report showed that it spent \$13 million more than it took in on an all-funds budget of \$308.2 million.

Richmond projects a balanced budget next year. Its 2007 CAFR showed a \$37.3 million surplus on a \$246.9 million all-funds budget.

In 2004, Richmond faced its own financial crisis and cut its budget "to the bone," closing its recreation department and some libraries, said city manager Bill Lindsay.

"The City Council made some really difficult decisions back in 2004 in terms of devastating service cuts," Lindsay said. "We really had kind of hit bottom."

The council implemented a policy of keeping a reserve of at least 15% of general fund spending, renegotiated labor agreements, and boosted both taxes and fees.

"At least it had stabilized - it was not a situation where we had to worry about making payroll, and so it was a matter of putting financial policies in place" that would prevent a repeat of the crisis, Lindsay said. "And the City Council has stuck with them."

Vallejo, by comparison, has made serious cuts, including firing its police narcotics squad and youth outreach unit, but it's only willing to cut so far. For instance, it refused to shut libraries when its crisis erupted earlier this year.

At this week's City Council meeting, Crystal Odum Ford, head of the local transit agency, told councilors that Vallejo would have to hike fares for its buses and ferries to cover rising fuel costs.

Council members told her that wasn't acceptable and suggested she look for creative ways to lower fuel costs, such as buying fuel in advance or buying new ferries that are more fuel efficient.

"As a city, as a community, we need to decide if public transportation is important, and if it is, then we need to find ways to help subsidize it," said Councilwoman Stephanie Gomes, who led the charge for bankruptcy in Vallejo.

Gomes said the council should consider asking voters to approve a sales tax for transportation at some point, but she was hesitant to support a fare increase even in the face of the city's impending bankruptcy.

The council votes on the proposed fare hike next week.

Gomes has been a tough critic of the city's public safety unions, pointing out that public safety salaries eat up about three-quarters of the general fund budget, compared to about 50% in other cities. She's advocated bankruptcy to escape the contracts previous councils negotiated with the public safety workers.

There's truth to the contention that Vallejo's public safety workers are very well paid, but police and firefighter unions say the general fund percentage is not a fair benchmark because Vallejo's budget includes 100 funds, often segregating expenses that would be in the general fund in other jurisdictions. The city admits it can't keep track of how much money it has lent to one fund from the next.

Richmond and Vallejo report their public safety spending differently, but as a percentage of the all funds budget Vallejo spends less for police and fire than Richmond spends on "public safety," according to the cities' 2007 CAFRs.

On a per-capita basis, Richmond spends \$677 a year, while Vallejo spends \$610. The average Richmond firefighter makes about \$150,000 a year in salary and benefits, Lindsay said. A Vallejo firefighter makes \$171,250, according to the city Finance Department.

Vallejo's unions last week offered to close most of next year's \$16 million budget gap by accepting \$10.6 million in pay cuts. It also commissioned a report by the outside auditing firm to assess the city's claims that it is bankrupt.

"They've basically operated with a very low level of reserves for at least 11 years. That just reflects the financial decisions and policies that the city has made," said Roger Mialocq, a principal at Harvey M. Rose & Associates, a well-known government consulting firm in the Bay Area that serves as the independent budget analysts for the San Francisco Board of Supervisors.

Mialocq said the city could avoid bankruptcy with a series of one-time cuts and fee increases that would give it a \$6 million general-fund surplus next year. Some of his suggestions included delaying replacement of city vehicles, applying for state funds the city is eligible for but doesn't receive, and transferring money from the city's redevelopment fund to its general fund to repay loans made in past years.

"Clearly, they've been spending more money than they could afford and pouring extra money into redevelopment," Mialocq said. "They definitely don't need to go into bankruptcy - there's no question about that."

Vallejo has rejected both the union's pay reduction offer and the Rose report's suggestions. Mayor Davis said the city isn't interested in any quick fixes to keep it out of bankruptcy. It's holding out for a permanent solution.

"Even if you came up with an agreement that gets you through this year, what are you going to do, face this battle again next year?" he said. "Why put it off? There's a structural problem in our finances. We need to fix it."

It will fix that problem by reducing its labor costs, whatever it takes to do that, he said. "The contracts cost more than we can afford to pay."

The differences between Richmond and Vallejo are not just managerial, said Cynthia Kroll, a senior regional economist at the Fisher Center for Real Estate and Urban Economy at the University of California-Berkeley Walter A. Haas School of Business.

Richmond has a more diverse tax base because it has pursued a development strategy that included industry and retail in addition to housing, she said. It has much more retail, including big box retailers like Costco WholesaleCorp. and Wal-Mart StoresInc.

Housing-dependent Vallejo is particularly susceptible to the current economic downturn because it depends heavily on property taxes on new homes and development fees to fund services, whereas Richmond gets more revenue from utility taxes, sales taxes, and commercial property taxes, including taxes on a large ChevronCorp. refinery.

Under California's Proposition 13 property tax limits, properties are only reassessed when they change hands. That means that cities with more mature housing stocks, like Richmond, don't benefit as much from the housing boom as cities with lots of new homes, but it also means that they don't suffer as much when housing weakens.

"Vallejo is heavily depending on property taxes and other revenue related to housing growth," Kroll said. "So the housing crisis has hit them very hard."

That said, budget math is not hard, said Lindsay, Richmond's city manager. "The choices are not simple sometimes, but the math is easy."

Richmond has a balanced budget for the coming year because its spending will stay flat, like its income, he said. It cut back on other programs so that it could afford the pay hikes it had promised.

Vallejo said it has to increase spending 6.9% to pay the raises it has agreed to. Officials there said there's nothing more they can cut.

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