

# Success Stories of Cities that Turned Crises into Opportunities

**CALIFORNIA SOCIETY OF MUNICIPAL FINANCE OFFICERS  
2015 Annual Conference / “The Changing Tides of California Finance”  
Monterey, California**

**February 19, 2015, 8:30 - 9:45 am**



## Session Overview

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### Join the speakers to:

- Learn how California cities of Los Angeles, Vallejo and Mammoth Lakes have been able to turn fiscal crises into opportunities.
- Find out what methods and tools these cities have utilized, what alliances and partnerships they have found to be essential, what mistakes they have made, and what lessons they have learned.
- Engage in a dialogue on what makes a city strong, and how cities can best survive and thrive in today's challenging economic, demographic and political environment.
- Share your own stories, ask questions, challenge assumptions.

### Speakers include:

- Miguel Santana, City Administrative Officer – Los Angeles.
- Craig Whittom, Assistant City Manager – Vallejo.
- Marianna Marysheva-Martinez, Managing Director – FTI Consulting / Public Sector Solutions.

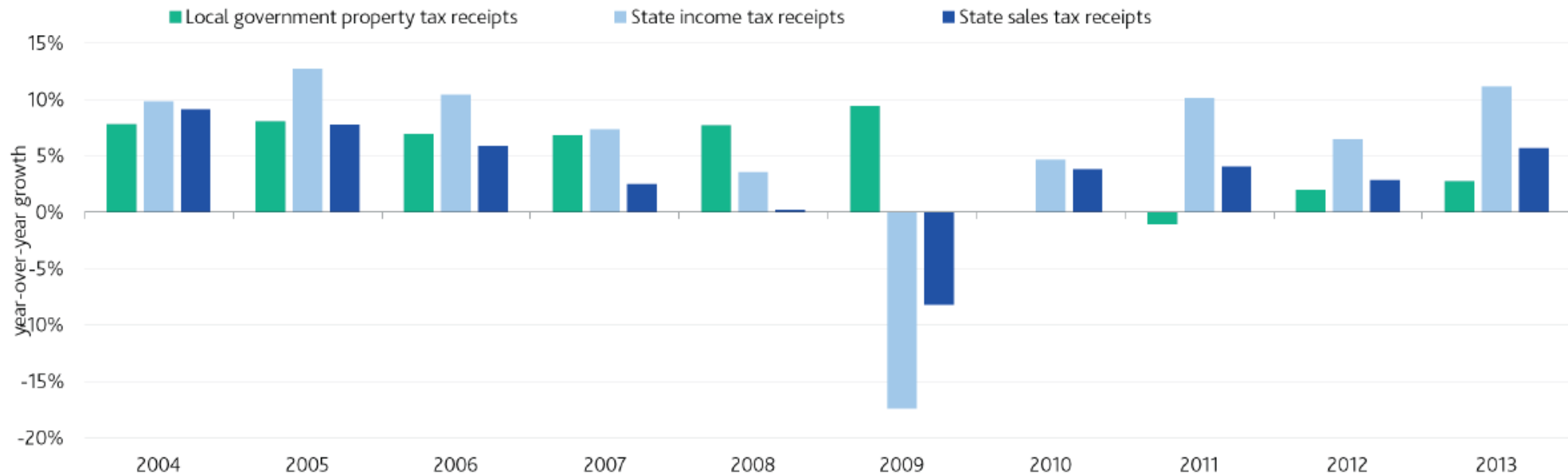
See bios in your packets.

# Why Is Today's Conversation Important?

■ Many public agencies continue to be challenged by:

■ **Weak economic conditions** impacting revenue growth.

*Nationwide, state and local governments rely on income, property and sales taxes as major sources of revenue. All three experienced declines during the downturn and are still recovering.*



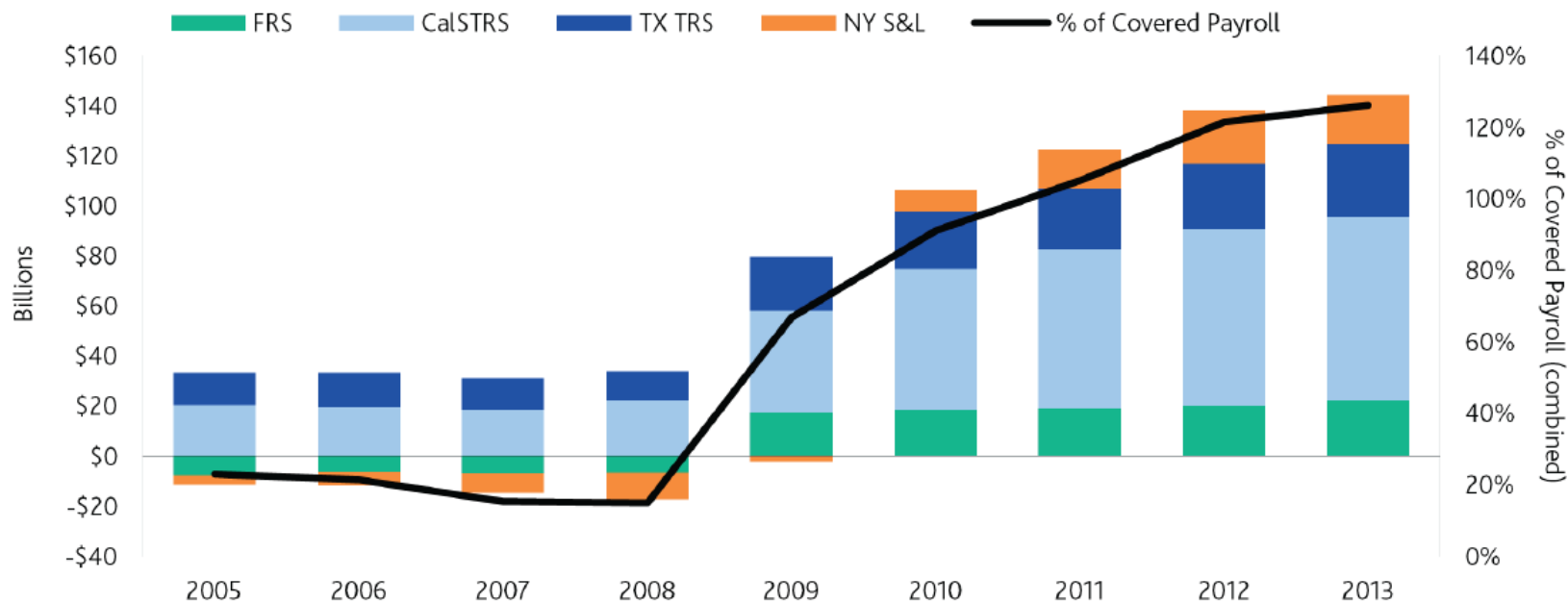
Source: Moody's Investors Service, U.S. Public Finance Outlook, December 3, 2014.

## Why Is Today's Conversation Important? (Continued)

■ Many public agencies continue to be challenged by:

■ Increasing pension and retiree medical (OPEB) liabilities.

*Nationwide, pensions continue to be an issue, with unfunded pension liabilities growing, particularly for the California State Teachers' Retirement System (CalSTRS).*



Source: Moody's Investors Service, U.S. Public Finance Outlook, December 3, 2014; Plan CAFRs and actuarial valuations.

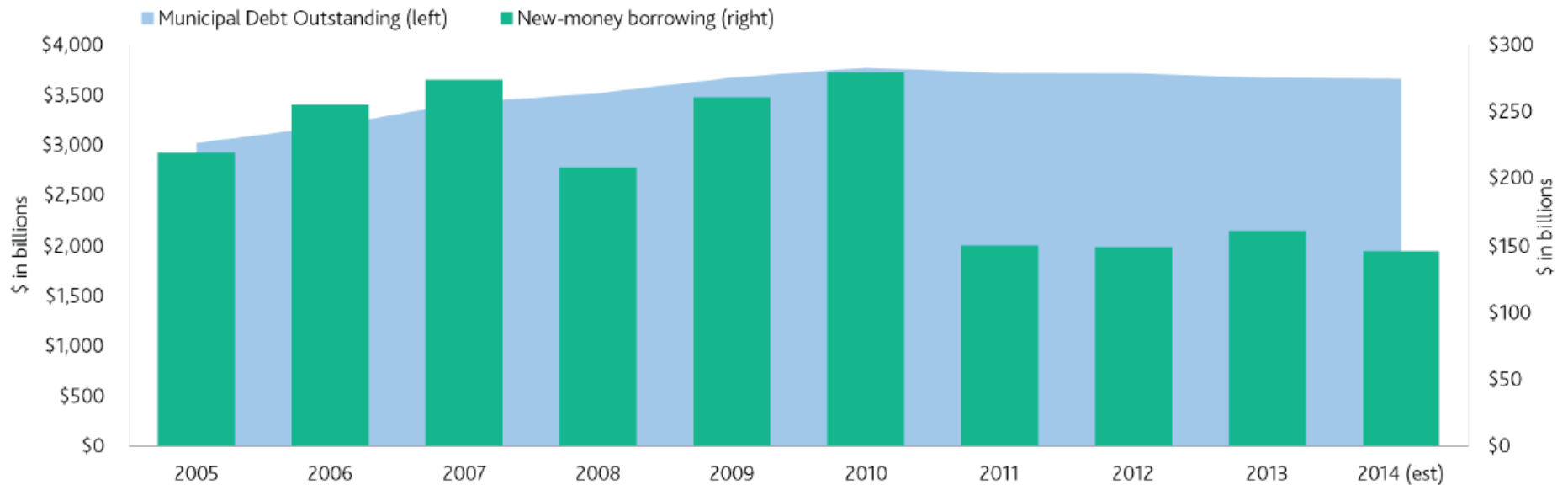
Includes the California State Teachers' Retirement System (CalSTRS), the New York State and Local Retirement System (NY S&L), the Florida Retirement System (FRS), and the Teacher Retirement System of Texas (TX TRS).

## Why Is Today's Conversation Important? (Continued)

■ Many public agencies continue to be challenged by:

■ **Aging infrastructure** (buildings, roads, sidewalks) and unfunded deferred maintenance.

*Inability to issue new debt further constrains government's options to fund infrastructure investments.*



Source: Moody's Investors Service, U.S. Public Finance Outlook, December 3, 2014.

## Why Is Today's Conversation Important? (Continued)

- Many agencies struggle to find sustainable solutions to adequately and fully address these challenges.
- Some have been able to effectively tackle serious challenges.
- Let us hear stories of Los Angeles, Vallejo and Mammoth Lakes.



## The Fiscal Crisis

- Brought on by the Great Recession
  - Unemployment in Los Angeles over 14%
  - Housing market crashed
  - As a result, in 2010 City had a drop in revenues of close to 5%
- Exacerbated by our own structural imbalance and inflexibility
  - Large and growing workforce prior to Great Recession (37,000 employees)
  - Employee costs approximately  $\frac{3}{4}$  of General Fund Expenditures
  - Civil service structure that made layoffs and terminations very difficult
  - High and growing pension obligation – 15% of General fund in 2009-10, increasing to over 21% in this year's budget
  - Labor contracts entered into immediately prior to recession with five-year term and continuous raises
- Aging infrastructure heavily reliant on General Fund
  - 38% of City streets receive a “poor” or “failed” grade
  - Sidewalks in places impassable due to tree roots and lack of maintenance
  - Underfunded and aging Information Technology infrastructure

## Two-Pronged Response

### ■ Immediate Efforts to Reduce Expenditures

- Early Retirement Incentive Program, through which thousands of employees left the City
- Instituted furloughs, reducing costs up to 10%
- Implemented layoffs, although difficult and lengthy process
- General Funded employees transferred to proprietary departments and special funded positions
- Asked contractors to take 10% cuts – some success, but could not impose

### ■ Developed a three-year plan for fiscal sustainability, updated each year since, based around five guiding principles:

- Responsible Fiscal Management, including increasing reserves
- Focus on Core Services, through prioritization, efficiencies, and eliminating redundancies
- Pursue Alternative Service Delivery Models, to enhance services at lower costs
- Maintain a Sustainable Workforce, by controlling compensation and benefit costs
- Strengthen Revenues, by pursuing new sources, improving collections processes

## Where We Are Now

### ■ Accomplishments

- City Reserves at 8.7% to start the fiscal year, more than double since before the recession
- If we control expenditures, we project elimination of the structural deficit by 2018-19
- Revenues have been gradually recovering, finally topping pre-recession levels in 2013-14
- Controlled employee costs:
  - Workforce size is over 14% below pre-recession levels
  - New pension tiers
  - Employee contributions to retiree healthcare
  - Reduced healthcare premiums
  - Compensation restructuring
- Recognition from rating agencies, with recent ratings bumps, and investors, with low cost of borrowing

### ■ Challenges

- Pressures to improve services from departments, elected officials, and residents
- Potential liabilities from pending lawsuits
- Infrastructure investment, while improved, is still inadequate



# City of Los Angeles, California



## Proof of Concept

- In 2010 and 2011, our debt was downgraded and ratings agencies made the following statements:
  - Fitch: “The downgrade reflects the anticipated draw-down of general fund reserves to a very low level and the likelihood that it will take the city some years to rebuild these reserves....Even with revenues returning to growth mode, greater political willingness will be needed to adhere to adopted and prudent fiscal policies to create meaningful results....This year’s budget deliberations...have shown the balancing process to be hindered by political considerations, impeding management’s ability to respond swiftly and effectively to economic contraction.”
  - Moody’s: “The downgrade primarily reflects the city’s increasingly limited general fund flexibility and likely continued pressure....Currently scheduled labor compensation adjustments and projected retiree cost increases will continue to put pressure on the city’s general fund budget for the foreseeable future.”
- In 2014, after implementing the reforms discussed above, ratings agencies were much more positive:
  - Kroll: “KRBA views the financial condition of Los Angeles as strong based on its management of its General Fund budget, increased levels of reserves and its strong liquidity over the last several years. KRBA considers the City’s improved finances from FY 2009 through FY 2013 to be largely the result of the City’s pro-active budgeting and strict fiscal monitoring practices.”
  - Moody’s: “[Los Angeles] is well positioned to strengthen its strong credit profile given a resilient and growing tax base, a highly diverse economy, and gradually growing reserves. The city’s strong financial management has curtailed expense growth, including significant pension cost in the wake of the Great Recession; prudently positioned the city to grow reserves with an expanding economy; and ultimately reversed the four-year budget outlook from growing deficits to a declining trend with a small surplus in 2019.”



# City of Vallejo: Community Overview

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North Bay Area community located 30 miles from San Francisco

Incorporated - 1867

Population – 116,000

Average Household Income - \$75,000

Former home to Mare Island Naval Shipyard (undergoing redevelopment)

Home to Cal State California Maritime Academy, Touro University, Six Flags Discovery Kingdom and corporate headquarters of Meyer Cookware and Blu Homes



# City of Vallejo: Why is Vallejo represented on this Panel?

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First City to file bankruptcy due to labor contract issues

City labor force fully unionized. Labor agreements through 1990s were top of market. Minimum staffing provisions in fire and police contracts.

Largely residential tax base impacted by recession. Little business to business sales tax. Land use development had assumed Mare Island Naval Shipyard would always provide for City.

Ebbs and flows of tax revenue from 1990 to 2008 resulted in contract extensions and COLA deferrals.

Recession and inability to re-negotiate labor agreements led to Chapter 9 filing in May 2008.

Exited bankruptcy on November 1, 2011



# City of Vallejo: Bankruptcy Experience in 2008-2011

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Being first was hard and expensive. Labor unions and retirees challenged City during all proceedings.

- Eligibility for Chapter Nine
- Ability to Reject contracts
- Impact of modified contracts on retirees medical benefits

Renegotiated police, management and fire contracts and City Council imposed new compensation/benefits on department heads.

Bankruptcy Court rejected the final labor contract (IBEW). Rejection withstood appeal.

Bankruptcy Plan of Adjustment approved by Court and Vallejo exited Bankruptcy on November 1, 2011.



# City of Vallejo: How did Vallejo Emerge Stronger from BK?

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Five primary reasons

1. Commitment to full cost recognition / five year financial planning
2. Voter approved structural changes
3. Commitment to communication
4. Willingness to empower residents with financial decision-making
5. Improving Economy

## *1. Commitment to solid financial planning*

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A. Confidence in data provided by Finance Department staff is highest priority. Invest resources that preserves, or if needed, enhances accuracy.

B. Provide financial data to help ensure ongoing financial solvency

1. Accurate year to date / projected year-end expenditures / revenues
2. Minimum five year forecast in budget including payment for unfunded liabilities.
3. Institutionalize quarterly City Council budget updates v. crisis returns to City Council.
4. Know your actuary.

C. Relationship with labor greatly improved.

1. Briefing before every City Council budget action
2. FY 2013-14 CAFR approved by City Council in December 2014

City Council asked voters to approve critical structural and financial measures

- A. Reauthorization of Utility Users Tax – Nov 2009
- B. Remove binding arbitration from the City Charter – June 2010
- C. 10% medical marijuana business tax – November 2011
- D. One Percent general sales tax with 10 year term – November 2011



## City of Vallejo:

### 3. *Commitment to Communication*

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Prior to BK City had not invested in communicating with its residents. During BK, City realized that we needed to fully invest in engaging with our residents.

Communication with our residents is now a key organizational value.

Here's what we do:

- A. Vallejo News – weekly newsletter (8,500 recipients)
- B. City Manager's Bi-Weekly Report (1,800 recipients)
- C. Facebook (2,200 likes)
- D. Open City Hall (42 topics closed / 560+ subscribers)
- E. See Click Fix (3,500+ issues resolved)
- F. Promote Nextdoor (6,000 participants)

[www.cityofvallejo.net](http://www.cityofvallejo.net)

Participatory Budgeting (PB) provides residents with an opportunity to vote for expenditure plan of budgeted General Fund Allocation.

Program was advocated by one City Councilmember in 2011. Staff recommended against it. City Council approved program on a split vote.

Process includes Steering Committee, Rulebook for voting and eligible expenditures, budget assemblies, development of project proposals and vote of residents. Now entering the Cycle 3 of funding.

### Highlights:

A. \$5.6 million invested on projects

B. 20 projects approved in Cycles 1 and 2.

Street repair, security cameras, student loans, park improvements, spay neuter procedures, homeless services

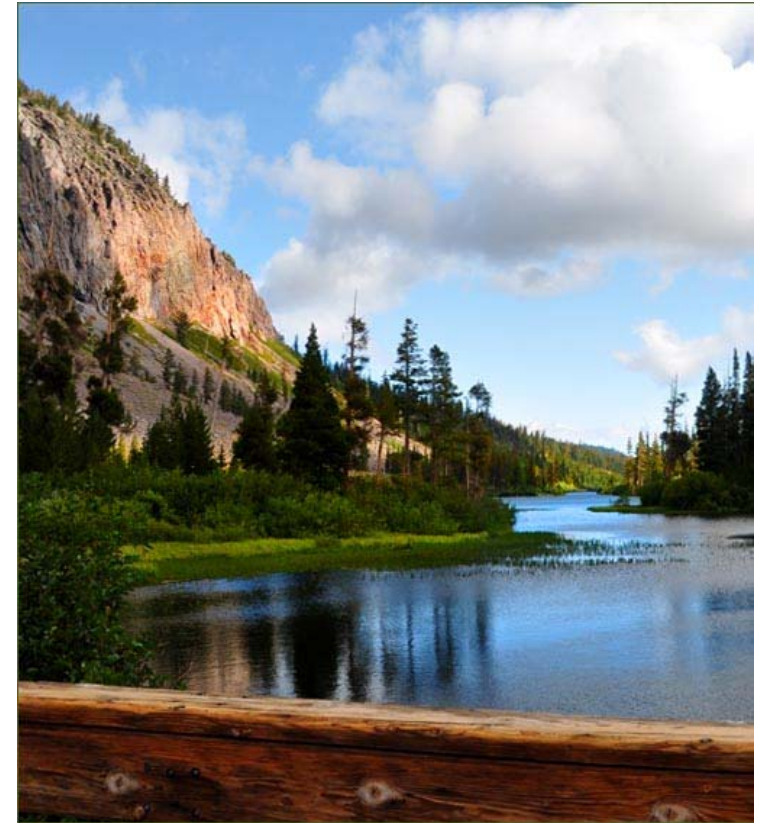
# Town of Mammoth Lakes, California

## About Mammoth Lakes:

- Small Mountain Resort Community of 8,000 people (35,000 including tourists).
- Known best for its skiing, snowboarding, fishing and proximity to Yosemite.

## Background:

- A \$30 million judgment awarded to a developer in 2007 for a breach-of-contract lawsuit. The court found the Town had not lived up to its end of the bargain.
- A state appellate court in December 2010 confirmed the judgment and chastised the town for trying to back out of the agreement it signed in 1997 with the developer.
- In early 2011 the California Supreme Court also ruled in favor of the developer, and ordered the Town to pay **\$43 million**.
- The City Council would not negotiate and wanted to dismiss the lawsuit.
- The developer would not negotiate.
- The community was angry at the City Council, and held them responsible for the lawsuit and the ultimate \$43 million judgment. They requested an apology from the City Council.



# Town of Mammoth Lakes, California

## Mammoth Lakes was forced to file for bankruptcy in 2012:

- Renegotiated the development judgment to \$29.5 million; incorporated all land and various other airport issues.
- Also used bankruptcy as an opportunity to address other challenges:
  - Financial: Successfully negotiated with all of its other creditors (employees, banks, contractors, vendors), for concessions of 10-15%.
  - Organizational: Changed organizational structure to reduce layers of management, streamlined operations, combined departments, reviewed key position qualifications, added new positions to increase tax collections.
  - Operational: Outsourced IT, introduced reserve officers to police, implemented a Town-wide volunteer program.

## Post-bankruptcy:

- Town residents, political leaders and employees were all emotionally impacted by the bankruptcy.
- Town residents needed an apology from the political leaders; then leadership.
- It was as important to repair morale as addressing financial issues. Trust had to be re-established.






# Common Thread: Leadership in Action

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Leadership is essential in challenging times in order to:



Understand how  
bad the  
challenges are

Develop a  
plan to  
address  
them

Implement the plan in  
collaboration with the  
impacted parties (e.g.,  
elected boards; employees  
and unions; business  
leaders; contractors and  
vendors; banks; etc.)

Stay focused, determined and inspiring throughout



## Discussion

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Let us all talk:

- Tell us what you think makes a city strong.
- How can cities best survive and thrive in today's challenging economic, demographic and political environment?
- Share your own stories, ask questions, challenge assumptions.