Infomail

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How Stockton Went Broke

Before the turn of the millennium things looked very different in California. In the last two weeks, three cities in California filed for bankruptcy. The largest was Stockton with a population of 300,000 which is just a bit smaller than London, Ontario (keep that in mind as you read along).

In the mid 1990's, the US stock market was booming, bolstering Stockton's pension funds. Real Estate values were beginning to soar, all of which brought a flood of new tax revenue to the once quiet farming town located about 85 miles east of San Francisco.

It was then that a series of bad political and administration fiscal mismanagement decisions began the downward spiral. In 1996, in a move that seemed cheaper than giving in to pay raises demanded by unions, city officials gave fire fighters full healthcare coverage in retirement. Of course, other Stockton public employees soon demanded, and received, the same healthcare deal. So to counter demands for wage hikes from the union, Stockton offered to extend their health care insurance in retirement past age 65. A benefit the union embraced and assured to be rock solid until city officials put it on the chopping block when they declared bankruptcy.

As the 2000's advanced, Stockton continued to spend freely with the support of voters, politicians (from both parties), employees, and bond holders. Rating agencies only started to downgrade the city's credit ratings two years ago.

Then in the early 2000's, generous pension deals were added.

That was followed by spending on large projects, trying to transform the bedroom community for San Francisco. Home building went on steroids and median prices, which were $110,000 in 2000, rose to nearly $400,000 in 2006.

City revenues did rise too. The general fund, which pays the city's operating costs, soared from $139M in 2001 to $186M in 2007.

Like other cities in California, Stockton chose to offer many public safety workers the same benefits as those mandated by a state law for highway patrol officers. The change allowed police officers to retire at age 50 with pensions based on 3% of final pay for each year of service (up from 2% before). City employees in other unions also received more generous pensions as well. This is in contrast to the vast majority of private sector workers who cannot receive Social Security payments before they are at least 62 years of age.

By the mid 2000's, Stockton's full time employees were also entitled to free healthcare for life. Police and firefighters continued to win further concessions, including allowances for uniforms, bonuses for years of service, and cash payments for unused vacation days. Of course, city officials miscalculated the rate of inflation for the soon to be rocketing medical expenses. Stockton city officials soon burned through their reserves and began planning new construction projects hoping to attract new residents. I suppose a "build it and they will come" mentality. They didn't come.

In 2004, the city issued $47 million in bonds to finance construction of a sports and concert arena to revitalize the city's downtown. The arena was built, but bled money for years.

A new downtown high rise building was acquired for a new city hall. A revamp of Stockton's downtown/riverfront was financed, by more than $100 million in debt between 2004-2006 by the city's redevelopment agency.

In 2007, the city issued a $125 million pension obligation bond, which also backfired. Stockton passed the proceeds to the California Public Employees Retirement System (Calpers) to pay down unfunded liabilities at the pension fund. Then when financial markets plummeted in 2008-09, the fund suffered steep losses. (23%).

In the end, when Stockton filed for bankruptcy, the city was left with a whopping $417 million liability.

The worst damage was done by the housing crash. Median home prices were back to $110,000 by 2009, wiping out a decade's gain. General fund revenues for 2011 were $155 million, just above 2001 levels. The real estate bust made Stockton one of the foreclosure capitals in the USA. Property tax revenue collapsed and the number of city employees are down 25% in numbers, in just three years.

Debt servicing costs that were $3 million six years ago, now stand at just over $17 million per year. Stockton has already defaulted on $2 million in bond payments this year.

Bondholders, employees and retirees will all be hurt in the process. Axing medical benefits is now central to the restructuring. One city clerk, retired at age 56, with a monthly pension of about $1900, now faces a $576 monthly premium for health care coverage.

Vallejo, Stockton and last week San Bernardino are just early in the process, there will be many more. If California was a nation on its own, it would be the 6th largest economy in the world. The tax and spend mentality in this historically liberal Democrat State has come home to roost.

Our own city of London has mentioned a wish list of spending projects including revitalizing downtown, a new city hall, and waterfront developments. Sound familiar???

So next time President Obama keeps blaming the banks, or Wall Street, or the "rich" for all of today's problems, remember the story of Stockton, California brought to its knees by terrible policies by politicians who simply wanted to get re-elected, greedy unions and public servants, and just simple living beyond one's means.

The free spending socialist mentality has already come home to roost in Greece, Portugal, Spain and Italy. Among others: the USA and even the Province of Ontario need to pay heed, or follow a similar course as Stockton. And if it gets that far it will be extremely painful for everyone.

Stay Tuned,

Vito Finucci
Vice President & Director
Private Client Division

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