REMAPPING DEBATE
Asking "Why" and "Why Not"

Deep-rooted dysfunction

Original Reporting | By David Noriega | Government services, Taxes

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March 5, 2014 — San Jose, perhaps surprisingly, is bigger than any other city for 300 miles. At one million people, it is the Bay Area's forgotten metropolis, defined far less by its own characteristics than by the smaller cities nearby. A 20-minute drive northwest of downtown, in good traffic, will wind through the zip codes of the world's most profitable tech corporations: Cupertino (Apple), Mountain View (Google), Santa Clara (Intel), Palo Alto (the historical ground zero of tech innovation), and on and on. "The Capital of Silicon Valley" is the self-anointed title San Jose has long strained to live up to; but, more bedroom community than capital, the city doesn't much feel like the center of anything.

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Still, as the de facto suburb of one of the most economically powerful regions on the planet, San Jose is awash with money. It regularly tops the list of richest big American cities, with a median income of $80,090 in 2012. That's almost twice as much as Dallas, which is approximately 25 percent more populous, and about $7,000 more than San Francisco. San Jose is also headquarters to several big tech names of its own, including Cisco Systems and eBay.

In spite of this, the city has been on shaky fiscal footing for the last three decades. After periodic budget squeezes in the 1980s and '90s, San Jose inaugurated the new millennium with a decade of chronic shortfalls. The dot-com bust had decimated tech jobs in the region and sapped revenues with it, but while the rest of the Valley restarted its engines, San Jose sputtered. Then the 2008 crash plunged it deep into the red.

Since then, San Jose has been mired in a protracted fiscal and political crisis. Services have been cut so far that discontent is widespread among residents. After initial rounds of layoffs, city workers have responded to cuts in pay and benefits, both real and threatened, by leaving in droves. The shrinking of the city is felt in many places: lagging repairs to infrastructure, reduced hours for libraries and community centers, a perilously understaffed sewage treatment plant.

Most conspicuously, public and political attention has been captured by a steep loss in police officers and firefighters. For a long time, San Jose's great pride was its status as America's Safest Big City. Then, in 2012, crime rates surpassed the state and national averages for the first time. This has only sharpened a general malaise, said Terry Christensen, a retired professor of political science at San Jose State University. "People are a little paranoid about it," he said, "because we hear about it a lot. It's still a very safe city. It's just not as safe as it was — you didn't used to hear that there was a burglary down the block."

To make matters worse, 2014 opened with a serial arsonist. Over the course of a week in early January, he set 12 fires, eluding police and causing more than $5.5 million in damage. One fire destroyed a massive warehouse and paralyzed surrounding traffic for hours. “It just heightened the fear and paranoia,” Christensen said.

Rising crime became a focal point for the city’s wider dysfunction — the compounded years of budget quarrels, the threadbare service levels, the shrill tenor of political hostility. The city’s officials, workers, and residents are locked in a triangle of resentment and mistrust, much of it, Christensen said, caused by successful efforts to place the blame for budget problems entirely on city employees. “People are worried about the rising crime, but at the same time they’re resentful of public employees. And public employees are pissed off that they’re resented,” Christensen said. “We’ve started to get divisions and hostility that we’d never seen before.”

A lopsided solution to a lopsided problem

In many ways, San Jose is alone in its suffering. Its neighbors were hit by the financial crash and the recession, too, but in the interim they have managed to ride the wave of Silicon Valley’s extraordinary recovery, the sharp rise in tech wealth and tech jobs applauded by economists — and many politicians — nationwide. Take Palo Alto. Its revenues since the recession have gone up by almost 10 percent (inflation- and population-adjusted); San Jose’s have gone down 12.5 percent.

This is because San Jose’s problems are part of a larger fiscal imbalance in Silicon Valley. The region could reasonably be said to function as an integrated economy, with a shared pool of capital and labor: there certainly is no such thing as “the Palo Alto economy” or “the Mountain View economy,” as distinct from the economy of the Valley or the larger Bay Area. Yet the region remains divided into numerous municipal jurisdictions that alternately benefit and suffer from the uneven distribution of industry and housing. While Palo Alto and Mountain View ingest waves of revenue from concentrated tech-industry activity, San Jose is stuck being the bloated suburb.

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And being a chiefly residential suburb is not sustainable in California. “Except for maybe at the absolute peak of the housing boom, residential development is basically a loser,” said Bob Brownstein, who was San Jose’s budget director in the mid-’90s and is now research director for the labor-backed think tank Working Partnerships USA. “That is, the taxes that are generated by housing don’t generate enough money to pay for the public services that the residents require.”

Over the last three decades or so, San Jose has gone to great lengths to attract industrial and commercial activity. The question of how the city ought to find the resources it needs has been almost entirely subsumed under the rubric of “economic development,” following a fairly strict neoliberal logic: private sector growth, induced by low taxes and heavy subsidies along with low expenditures, is the only real route to increasing revenue. The paradox: the efforts to induce growth have, to a significant extent, been successful, and yet the city remains cash-strapped.

As such, it would not seem difficult to understand San Jose's predicament as one of inadequate revenues. Although there is plenty of wealth circulating through the regional economy, San Jose as a fiscal entity simply doesn't capture enough of it. In spite of this, the city's elected officials in recent years have taken a decidedly lopsided view of its fiscal imbalance, disproportionately going after the cost side of the ledger. This approach reached new levels of intensity under the current mayor, Chuck Reed, who came into office in 2007. Faced with the fallout of the financial crash and the recession, Reed did what many mayors did: laid off personnel, cut programs and services, and instituted pay cuts across the workforce. But then he went several steps further, embarking on the mission that has become his signature: finding ways to make deep, permanent cuts to the retirement benefits of current city workers.

A key expression of this campaign is Measure B, a referendum that Reed successfully persuaded city voters to adopt in 2012. The measure is designed to effectively force employees out of their current pension plans and into far smaller ones. It would also cut benefits by, among other things, lowering cost-of-living adjustments and making it much harder for injured workers to receive disability payments. As of now, Measure B has been prevented from achieving its intended transformative effect. While a Santa Clara County Court in December upheld some of the cuts (like the restrictions on disability benefits), it struck down many of the measure's central provisions. (The city is likely to appeal.)

But Measure B is a product of Reed's one-sided focus on expenses, specifically the cost of worker benefits. Reed has allowed some minor tax increases while in office, but these are dwarfed by the effort he has expended on cutting costs. "The central problem in the whole pension reform issue is that these benefits are too expensive," Reed told Remapping Debate.

Everyone agrees that the costs of retirement benefits have been rising since the early 2000s, and that the portion of the city's general fund dedicated to paying for basic services has dwindled as a result. Part of this, as Reed stresses, is due to substantial increases to benefits made in the late 1990s and early 2000s, the large majority for police and fire.

But those outside Reed's camp see the city's longstanding fiscal problems as deeper and more complex; even the portion of the problem related to pensions, they say, involves many more factors than what Reed and his allies describe as overly generous benefit levels. At the top of the list: the city's two pension funds lost $1 billion in the 2008 financial crash. While the recovery of the market has brought the funds back to nearly the values they had before the crash, the initial losses still mean that the funds are worth far less than they were projected to be today. "There are multiple factors" to the rising retirement costs, Brownstein said. "But of those, the 10,000-pound gorilla was the financial meltdown."

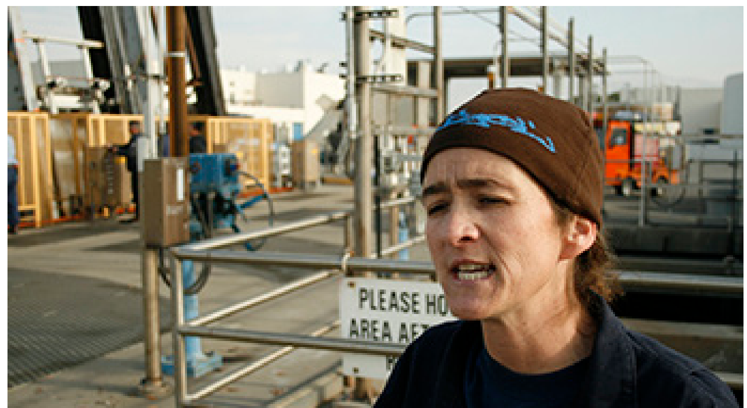
A structural problem — but which structure?

Reed's opponents point out that he and his allies on the council have declined to pursue tax measures that would have helped significantly in relieving the pressure. Most recently, in 2012, they voted against a quarter-percent rise in the city's sales tax. Other possibilities have received even less consideration, like rewriting rates for a business license tax that hasn't changed since 1984. The city currently pulls in only $40 million from the tax. "If you adjust for inflation," said Brownstein, "it's half what it used to be."

This is part of a deeper aversion in Reed's camp to raising taxes, said Ash Kalra, a city councilman opposed to the pension cuts. "They hesitate any time we talk about revenue generation," Kalra said. "This continues to put the onus of balancing the books on the employees and on the residents who suffer from service cuts."

A fundamental roadblock to San Jose (or any California locality) pursuing new revenues is traceable to Proposition 13, a 1978 statewide referendum that, along with a few successors, erected all sorts of constraints on the ability of cities to raise taxes. Any new tax requires a vote by the public, and some require two-thirds approval. The law also choked property taxes throughout the state at 1 percent and curtailed the government's ability to reassess property values; to a massive suburb like San Jose that had relied almost entirely on its residential tax base, this was especially ruinous.

But while Reed has no interest in removing the structural obstacles to raising more revenues, he is aggressively pushing for structural change on the cost side. Well before the court decision on Measure B, he had already launched a statewide ballot initiative to amend the California Constitution to allow cuts to existing contracts. The initiative has made him something of a national poster child for pension reform, gathering hundreds of thousands of dollars from prominent Republican donors and giving keynote speeches at Manhattan Institute for Policy Research panels.



Teresa Harris, a senior mechanic at the San Jose sewage treatment plant, said the facility is now seriously understaffed.

Reed acknowledges the significant limitations that constrained revenues imposed on the budget but treats those limitations as an inalterable reality. He is content to operate along the established routes, which mainly consist of subsidizing private growth. In explaining that he had done everything possible on the revenue side of the ledger, Reed said: "Trust me, it's a lot more fun to do economic development and get new revenues than it is to cut services."

Yet others point out that there is already a tremendous amount of economic activity in and around San Jose, and suggest that the city is simply not benefitting enough from it. "You're in San Jose, in the heart of the Silicon Valley, and the business tax rates are actually quite low," said Chris Hoene, executive director of the California Budget Project, a Sacramento-based research and advocacy group. "Which doesn't really make sense, right? The city can't even tap into the wealth that it has in the community."

One glaring example is the way that, through a particular quirk of Proposition 13, many large corporations pay extraordinarily low taxes on commercial property. Under the law, properties are only reassessed, thus generating more taxes, when they change hands. But some companies hold on to land for decades, while many others avoid reassessment by leasing land, buying it through limited liability companies (LLCs), or any number of other maneuvers.

"Commercial property assessment is a nightmare," said Lenny Goldberg, director of the California Tax Reform Association. "It's more loophole than tax." Thus, a company like IBM pays half a cent per square foot on a 200-acre campus in San Jose, according to a report by Goldberg's group. The report estimates that if the value of the land were made current in the books, IBM would pay around $6 million more per year on that property alone.

This, Hoene said, underscores how Reed's approach to the problem leaves its principal causes untouched. "What's really needed is for local governments to be given more space to maneuver on the revenue side," he said. "That would get them a lot further down the road towards controlling their own fiscal destiny, more than allowing them to scale back the benefits of current employees."

Rippling consequences

The San Jose-Santa Clara Regional Wastewater Facility is spread out across 2,600 acres in northern San Jose. Every day it processes 110 million gallons of sewage — enough, the plant's brochure tells us, to fill the hockey arena downtown.

During an interview at the treatment plant, Teresa Harris, a senior mechanic, pointed to a sort of gulley down which water, translucent blue and smelling faintly of chlorine, cascaded underground. A few hundred yards back, the same water had been thick and dark with waste. She explained the transformation by reference to the plant's clusters of machinery, the wards of her supervision and care. One allows solids to settle while skimming grease and debris off the surface. Another facilitates a biochemical cleansing: "The good bugs eat the bad bugs." Finally the water arrives at the chlorinated blue state it will preserve on its underground journey to the San Francisco Bay. "That water is so clean we could drink it," Harris said. "It's cleaner than the actual bay."

But the facility was one of the hardest hit by the budget crisis and subsequent political decisions, with 40 employees leaving over the course of two years. "A lot of them went to neighboring cities," Harris said. "They were afraid they were going to lose everything, so they quit. They locked in their pension and their medical and got the heck out."

To keep up basic operations, the city hired private contractors, which wound up costing more than the city workers. The plant is still around 25 percent understaffed. "We simply don't have the people that we need," Harris said.

A report from the city auditor in 2012 sounded alarms about the staffing shortage: the loss of senior mechanics and engineers left the plant in peril of failure, which could send raw sewage into the bay or overflowing into the streets.

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