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# 'Picking up the pieces': austerity urbanism, California and fiscal crisis

Mark Davidson[a] and Kevin Ward[b]

[a]*Department of Geography, Clark University, 950 Main Street, Worcester, MA 01610, USA, MDavidson@clarku.edu*
[b]*School of Environment, Education and Development, The University of Manchester, Manchester M13 9PL, UK, kevin.ward@manchester.ac.uk*

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**California continues to be at the epicentre of the current Great Recession. Cities around the state are facing a multiple-fronted assault on their fiscal situation. Although not new—the state's precarious financial situation is the stuff of legends—the cutting in federal revenues, together with the decline in property taxes stemming from the drop in house prices and the rising costs of servicing debt incurred through years of speculative growth strategies have left a number of city governments in the state horribly exposed. This paper explores the place of a number of Californian cities in the context of the wider onset of US austerity urbanism. This constitutes a deepening and widening of some aspects of earlier neo-liberalisation.**

*Keywords:* austerity urbanism, California, crisis, finance, redevelopment
*JEL Classifications:* R38, R58

## Introduction

> … the austerity war is now raging. States are cutting funds for programmes such as health care for the poor, home care for the infirm, and support for education at the elementary, high school and college levels (Crotty, 2012, 97)

> California is in a state of permanent crisis (Bardhan and Walker, 2011, 317)

> [San Bernardino] is a living laboratory for how a Chapter 9 municipal bankruptcy works in California (MacDuff, 2013, np)

> What happens in Stockton will be a bell-wether for other cities that are in financial distress … Stockton has already taken the center stage in a long line of cities in crisis… *Everyone is following it because it does have implications for how the game gets played beyond Stockton* (Smith, 2013, np, emphasis added)

The title of this paper paraphrases Steve Duran, the Hercules city manager. Located north east of San Francisco, this city of just under 30,000 has been left with an annual debt repayment of $20 million with the winding down of its Redevelopment Agency (RDA). The city was already struggling financially, due to federal budget cuts and a sharp decline in the value of its housing stock and thus in its property

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tax base. Its general fund had dwindled from $18 to $10.5 million over the last few years, for example. The statewide closure of 425 RDAs on 1 February 2012 by Governor Jerry Brown only made matters worse, and led the city of Hercules to lay off one hundred of its workers, about 40% of its total workforce. The city has also had to generate various reports to document how it has spent the revenue generated by the RDA, as the state has sought to claim unspent funds and those who had provided financial guarantees for the Agency's bonds have sought repayment reassurances. These revealed, amongst other things, that in April 2012 the RDA sold a four-storey apartment for $425,000, having spent over $38 million on it over the years, while it also had to cease a $20 million youth stadium project when the drop in property values meant that the project was no longer financially viable. More generally, the State Controller, John Chiang, commented that "During my time in office, this could be the worst set of city accounting records I have seen. The City's books were so poorly managed, that I must question their use of every single federal and state dollar granted to the City". In the context of a wider regime of 'light touch' accounting and record keeping this is some claim! As of late 2013 Hercules hovers on the brink of bankruptcy, seeking out new ways of delivering basic services while managing the repayment of various general fund and redevelopment bonds. The RDA successor agency, that is the city government of Hercules, meanwhile struggles to manage the legacy of bad debts and projects bequeathed to it.

Hercules is not alone, of course. Other cities, including, Lincoln, Milpitas, San Bernardino, Stockton and Vallejo are at various stages of fiscal distress. Table 1 outlines some general characteristics of these cities and their current precarious situation.

Each has either filed for bankruptcy—through Chapter 9—or is actively pursuing austerity strategies just short of bankruptcy. While there are elements of mismanagement in each case, there are also strong shared systemic features. Post Proposition 13 many Californian cities used RDAs to speculate on future growth. Speculative urbanism was system wide. Large amounts of money were borrowed against future revenue streams. Bonds were issued against these streams, to add to the General Obligation Bonds. Consequently, these cities found themselves with unserviceable levels of debt when the 2008 financial crisis struck and the decision was made to close down RDAs in 2012. There is evidence to suggest they are not alone in either California (California Public Policy Center, 2013; Walters, 2013) or the rest of the USA (Hujer, 2013; Plummer, 2013).

Figure 1 reveals that California's RDAs had generated over $30 billion of debt when they were closed down on 1 February 2012.

While this was the end of the RDAs in California, it was not the end of their consequences. Organisationally, cities and counties continue to wrestle with the succession plans. In most cases the debts, liabilities and projects of RDAs were taken over by city governments. Not in all cases however. Los Angeles was a noticeable exception. The city government declined the offer from Governor Jerry Brown, with the LA's City Administrative Officer, Miguel Santana, claiming that "we can't afford it" (Zahniser and Garrison, 2012, np). Instead the RDA's 192 employees were laid off and a Designated Local Authority was appointed. Moreover, around the state the disentangling of RDAs from the various financial and legal arrangements and entanglements they had with other city, county, state, federal and international private and public economic and financial actors is likely to continue to exercise many stakeholders for the next decade or so. Financially, the fallout of their cessation also continues to reverberate around California. The State's financial team has gone from city to city auditing the books of the RDAs, looking for revenue it can claw back to offset its own precarious financial situation. For despite announcing a 'balanced budget' for 2013–2014

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**Table 1.** *The start of the great California muni bankruptcy run?*

| | Hercules | Lincoln | Milpitas | San Bernardino | Stockton | Vallejo |
|---|---|---|---|---|---|---|
| Population | 26,000 | 43,428 | 66,790 | 213,012 | 290,000 | 116,829 |
| Median household income ($) (US median is 51,017) | 87,869 | 60,883 | 92,964 | 61,632 | 47,946 | 61,632 |
| Budget deficit ($) | 1 million | 2 million | 5.2 million | 22–32 million | 20–38 million | 16 million |
| Percent budget for salaries & benefits | 50–60% | 83% | 84% | 75% | 82% | 78% |
| Percent median home value decline | 62% | 50% | 33% | 55% | 65% | 66% |
| Main deficit drivers | City government took on $20 million debt from redevelopment agency | New library created $16 million deficit | City government took on $39 million debt from redevelopment agency | Closure of redevelopment agency, generating loss in general operating income | Lost $2.3 million in property taxes and retiree costs increased from $8.5 to $16.8 million over 3 years | Lost $4.9 million in revenues and $5.2 million increase in compensation related expenditures in 2008 |
| Deficit reduction strategies | Reduce 40% of city government employees | Consultant hired to reduce costs | Declare 'fiscal emergency' prior to poll to raise taxes or file for bankruptcy | Enter into bankruptcy | Enter into bankruptcy | Enter into bankruptcy |

*Source*: Adapted from Lusvardi (2012).



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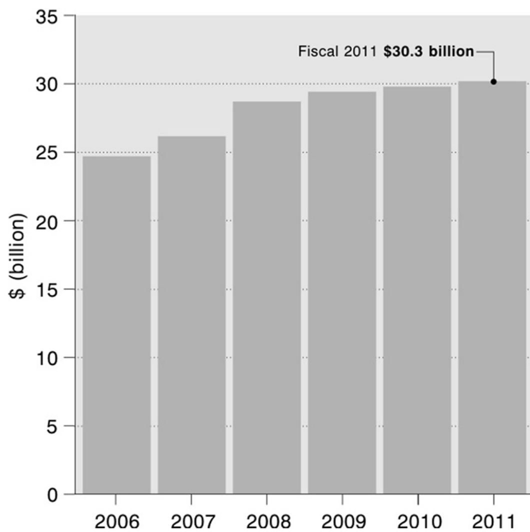


**Figure 1.** *The long-term debt of California's redevelopment agencies.*

(Luhby, 2013), California continues to be 'fiscally dysfunctional' (Bardhan and Walker, 2011, 317). Indeed, according to Oliff et al. (2012, 5), California's shortfall is 16.2% of its 2013 financial year budget, or $15 billion and hence why emptying the accounts of the state's 400-plus RDAs was attractive to Governor Jerry Brown.

This paper explores the current plight of a number of Californian cities in the context of the systemic emergence of speculative urbanism as the *modus operandi* since the early 1980s. Our argument is two-fold. First, that the last four decades have seen US city governments in general become ever more entrepreneurial and innovative with regard to economic development (Harvey, 1989). Cities have had to indulge in ever more risky forms of *speculative urbanism,* understood here as the ways in which cities speculate on future economic growth by borrowing against predicted future revenue streams to make this growth more likely. They thus seek to make a particular future realizable by borrowing against it. This has occurred in the context of the broader emergence and extension of neo-liberal urbanism. This emphasised "an always-contradictory process … [of] … evolving/rolling programme of restructuring" (Peck and Theodore, 2012, 179).

Our second argument is, however, that as the wave of recent bankruptcies reveal, Californian cities were at the forefront of this speculative urbanism. Afforded very little fiscal wiggle room due to the introduction of Proposition 13 in 1978—"which capped local property taxes and required a two-third of vote of the legislature or the citizenry to increase taxes" (Bardhan and Walker, 2011, 316)—it was here—through the ardent stimulation of development and consumption, oftentimes via the use of RDAs and Tax Increment Financing (TIF)—that cities speculated on future growth, borrowing against possible but not guaranteed future revenue streams (Weber, 2002, 2010). As a consequence, cities were gambling on, and eventually became habituated to, endless growth (or at least growth for 20–25 years, which is the length of the bonds that were taken out to instigate economic development). As the last 5 years have demonstrated this over-reaching has come at a high cost.

The next section of this paper turns to outline the general contours of speculative urbanism, paying particular attention to the increasing use by cities of revenue bonds—those not backed by the 'full faith and credit' of a municipality's tax base (Hackworth, 2002). The third section turns to the example of California. We outline the ways in which the state's city governments speculated on future growth, using consequent revenues to fund a number of schemes. Some bankrolled redevelopment projects which met the statewide 'blight' and 'but for' criteria. That is, 'but for' the redevelopment project the property taxes would not rise, there would be no increment that could then be captured, partly used to pay down the bond and partly used to finance other schemes. Revenues were also used to other ends, which did not comply with the statewide legislation.

Put simply, in an age where the scope for Californian cities to increase revenues was increasingly constrained, they turned to



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speculative mechanisms in order to generate funds for both local services and discretionary spending. In some cases this included paying for services that might normally have been expected to have been covered by the general tax base, such as the pensions and salaries of public employees. The final section of the paper examines institutional and financial restructuring in Vallejo, California, as an exemplar of today's speculative urbanism under conditions of austerity. In conclusion the paper makes three arguments. First, municipal bankruptcies in California are redefining the stakes of US urban politics, creating a political landscape where *just the threat of going broke* can be used to impose draconian neo-liberal reforms. Second, as the federally mediated urban crisis rolls out, city services and operations once thought beyond the reach of neo-liberalisation are now becoming fair game. Third, after years of speculative urbanism a number of cities appear ill-prepared financially to deal with the current urban (fiscal) crisis.

## Entrepreneurial speculative urbanism

Just for a moment it looked like neo-liberal urbanism would be no more. "The free market project is on the ropes" declared Peck et al. (2009a, 94). The financial crisis that struck first towards the end of 2007 appeared to signal the end of the "belief that open, competitive and unregulated markets, liberated from state interference and the actions of social collectivities, represent the optimal mechanism for socioeconomic development" (Peck et al., 2009b, 50). Yet this moment was relatively short lived. Talk of alternatives proved to be just that: talk. Quickly neo-liberal business as usual was restored. Over the last 5 years what has been witnessed across the cities of the global north is nothing short of extreme austerity urbanism (Gray, 2012; Mayer, 2013; Peck, 2012), or what Peck (2012, 631) refers to as the "urbanisation of neoliberal austerity". This has involved "state and local governments and cities in particular … being exposed to the full force of austerity's 'extreme economy" (Peck, 2012, 628). Echoing the argument of Peck et al. (2009b, 57, original emphasis) that "*cities* have become strategically important arenas in which neo-liberalising forms of creative destruction have been unfolding", our argument is that the speculative component of this neo-liberalising of cities left many of them horribly exposed to the vagaries of the financial and housing markets. This exposure—which allowed cities a degree of financial flexibility, as they took risks with as yet unrealised revenue streams—can be summarised along four *restructuring* features of entrepreneurial speculative urbanism. These general tendencies are just that, general. They are not constituted or expressed uniformly across space but are rather mediated across a range of geographical scales through various institutional and organisational prisms. However, their defining and DNA-like characteristics can be summarised as follows:

*Restructuring of inter-governmental relations*: In this the federal level has 'downloaded' a number of responsibilities, governing at a distance through the establishment of various indicators, at the same time as the limited federal and state level monies were used to 'incentivise' partnerships with the private sector. This has meant a number of cities have become more dependent "on own-source revenues" (Weber, 2002, 190).

*Restructuring of the logics of governmental decision-making*: In this, many cities have developed more speculative mechanisms to finance current expenditure through borrowing against predicted future income revenues. In the process this has changed the calculations, logics and rationalities of city government and other private and public actors involved.

*Restructuring of public finance:* In this the federal support for local activities and services as part of a wider commitment to redistribution has been dismantled—slowly and unevenly across space—with localities establishing new mechanisms for generating and retaining current and predicted revenue streams.

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*Restructuring of risk allocation*: In this, the 'risk' and its associated management has been 'downloaded' to localities, with the withdrawal of a federal 'safety net' exposing localities to a range of forces and pressures.

The outcome of these general tendencies has been that a number of US cities have been left teetering on the brink of financial crisis (Plummer, 2013). Unevenness in capacity—which has always been present in the country's federalised fiscal system—has been rendered more pronounced, as those cities that have faced the greatest pressure to downsize their workforce are also those that face the greatest challenges in terms of populations disadvantaged by the fiscal crisis. Some cities have even gone as far as to file for bankruptcy. These include Central Falls, Rhode Island, Harrisburg, Pennsylvania, Jefferson County, Alabama, and more recently and perhaps infamously, the city of Detroit. However, California has seen the most bankruptcy filings, is the state with the second worst credit rating in the nation and is where the debt almost trebled in the 6 years prior to the financial crisis (Summers and Randazzo, 2008). It is to this state that the paper now turns.

## Contours of Californian speculative urbanism

> Luck, now, as well as idleness or inadequacy, can lose you a job. Luck can wipe out a lifetime's savings, can double or halve the cost of a holiday abroad, can bankrupt a business because of some unpredictable change in interest rates or commodity prices or some other factor that used to be regarded as more or less stable and reliable (Strange, 1986, 2)

> Investors beware. Armageddon for muni bond holder lies ahead, and it could hit you like an iceberg (Zamansky, 2013, np)

The mantras of free and unfettered markets and the small state became engrained in California state and municipal politics from the late 1970s onwards (Lustig, 2010). To a large extent, the neo-liberal reforms imposed in California mirror those in other places (Bardhan and Walker, 2011). Cities became less reliant on funds redistributed from federal and state governments and, consequently, had to devise revenue generating mechanisms themselves (Harvey, 1989). As responsibilities were 'downloaded' from federal and state levels, cities were required to fund more local services and to find innovative ways of supporting their vulnerable communities (Peck and Tickell, 2002). In this section we briefly describe the contours of this neo-liberalised urban governance landscape, outlining the conditions that led to a number of Californian cities becoming avid gamblers and speculators.

### Revenues

Since Reagan's federal reforms in the 1980s (some of the impulse for which came from the Californian Proposition 13 reforms in the late 1970s), federal government transfers to municipalities have halved (Wildasin, 2010) and many states have sought to do no more than maintain funding levels, generating significant gaps in city budgets. In California this reliance on state funding was made more severe by the passing of Proposition 13 in 1978. The capping of general purpose property tax rates at 1% and the requirement for two-thirds of the voting citizenry or legislature to increase property taxes effectively took away from city government one of its most important ways of increasing revenue. The effects were immediate. State revenues were cut by 57% in 1979, leading to 100,000 public sector layoffs (Keil, 1998; Goldberg, 2010). Coupled with declining federal resources, cities around the state were faced with a systemic fiscal crisis, and began to explore other ways of generating revenues (Bardhan and Walker, 2011). 'Pay as you use' replaced 'pay as you go', as cities turned increasingly to the capital markets (Kirkpatrick and Smith, 2011), to the point that some have recently claimed that the state is 'drowning in debt' (Summers and Randazzo,

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2008). Subsequent revenue-restricting reforms at the state level have meant Californian cities have been impelled to pursue revenue-raising activities in order both to meet the most basic needs of its communities and to pursue related economic development strategies. The latter include, for example, the granting of franchise rights, permits and local sales taxes to produce new and/or enhanced revenue streams. Many of these revenue streams are tied to levels of consumption, making them particularly sensitive to economic cycles.

The two revenue sources that became widely used across the state and that were tied to the development-focused speculative actions of municipalities were RDAs, their use of TIF and their circumventing of any increase in property taxes that would need to be agreed by a two-thirds voting majority. However, as our study of Vallejo's bankruptcy illustrates, these institutionalised development mechanisms, and their particular uses, were derivative of a speculation-driven form of urban governance; as opposed to them alone encouraging speculative forms of governance.

RDAs grew out of the post-Second World War federal urban renewal program. The aim of the post-Second World War Community Redevelopment Act (1945) was to give state agencies the ability to address urban 'blight' by offering state assistance and government-backed financial incentives to stimulate development. In 1951 the state voted to allow TIF. This was unique at the time to California, although it has subsequently been introduced into every US state bar Arizona. This allowed an RDA to designate an area as 'blighted', using eminent domain if required. It could then speculate on what 'extra' or 'incremental' property taxes and sales taxes could be generated if it spent some money up-front on various types of infrastructure. This could include brownfield clean-up, land purchase, new roads, new sewerage systems for example. The up-front expenditure would be financed through a bond issue, not against the general fund but rather against the projected incremental future revenue stream that would be generated post the investment. One consequence of TIF was, however, that special districts, such as schools, which received a proportion of local property taxes, did not receive a proportion of the increment for the duration of the TIF, which would often be between 20 and 25 years (see Figure 2)

While California's cities were able to use (and where deemed necessary, increase) local property taxes to support the delivery of everyday services there was little use of TIF in the state, and very few RDAs were established. For example in 1977—the year before Proposition 13 was passed—there were only a couple of hundred RDAs and they received less than 2% of statewide property taxes. Ten years later in 1988 the number of RDAs had doubled and they were receiving approximately 6% of statewide property taxes. By 1998—20 years after Proposition 13—8% of all statewide property taxes were being collected not by city governments but by the 400 or so RDAs. Unable to increase local property taxes, for many cities RDAs and TIF was the only economic development game in town. It was certainly the one over which there was the least political or public accountability and oversight. The kinds of projects that RDAs undertook also changed over the decades. Definitions of 'blight' became stretched in the state, reflecting a US-wide redefinition of the term (Weber, 2002), as in many cases the RDAs turned their attention away from downtown and out to the suburbs. The projects also grew in size, as city governments worked in tandem with their RDAs to max-out on development and the revenue streams it promised.

In practice, then, RDAs played the simple—but not uncontroversial—role of providing cheap funding to property developers in order to direct development into designated districts. Using eminent domain powers, they became significant political actors, kick-starting economic development by issuing bonds against predicted future revenue streams and using this

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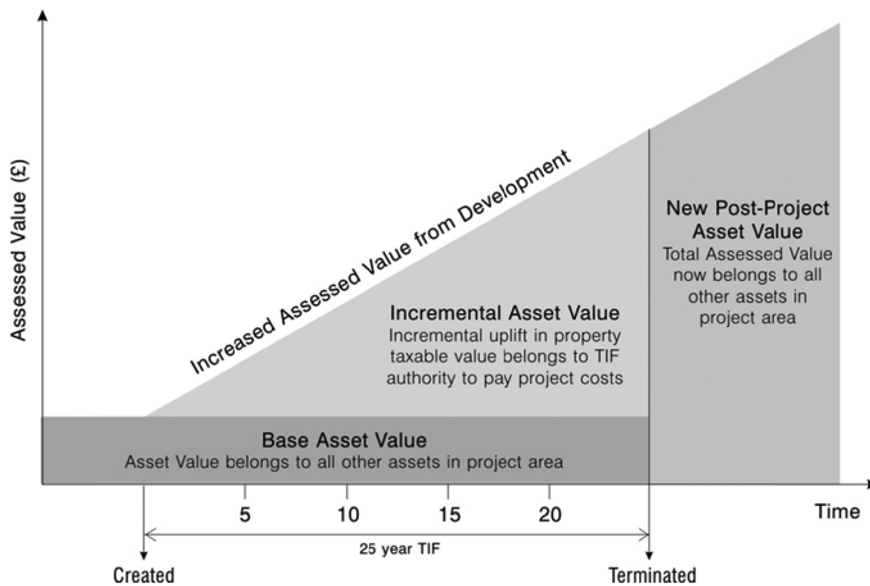


**Figure 2.** *Tax increment financing.*

capital to encourage and financially incentivise developers and others with a stake in this particular model of growth. The revalorisation of commercial and residential project areas via RDAs had a central role in making cities function in times of reduced redistributed funds. By reinvigorating urban districts the city could restore and/or increase property values and occupancy levels, therefore boosting total property tax revenues. Furthermore, a successful RDA could use funds accrued through revenue-raising project for the production of yet more (re)development.

The success of many RDAs—although not all were successful (Jonas and McCarthy, 2009; Kirkpatrick and Smith, 2011)—led them to become central contributors to city budgets. They subsidised activities and services that could not be funded out of the general tax base. In Oakland—the city over which the now Governor Jerry Brown presided between 1999 and 2007—for example, RDA income was funnelled into central city funds in order to support, by 2012, the salaries of approximately 200 employees, including those in the mayor's office and public works (Lee, 2012). The speculative activities of RDAs therefore became an important and normalised aspect to Californian municipal governance, as did the generation of debt—in the form of issued revenue bonds—which required a buoyant economy in order to generate the 'increment' which would allow them to be paid down.

This redevelopment-led revenue raising was paired with a more general reliance on property tax revenues. With Proposition 13 limiting any raises in property taxes to 1% of the value of properties, many cities were left with little option but to produce more (sub)urban development in order to increase the property tax base and collect construction-related revenues (for example, permit fees). In the context of California's economic boom, this strategy proved effective in many cities. As demand for housing grew, particularly in and around the state's largest cities, the Californian economy supported more and more employment (O'Keefe, 2004) and property prices inflated to staggering levels (Glaeser et al., 2005), as cities were able to collect growing amounts



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of property related revenues. The speculative housing boom in California therefore propped up municipal government and, as such, Californian municipalities had little interest in putting the brakes on property development and/or house price inflation (Goldberg, 2010).

## Expenditures

In the post-crisis period, the expenditures of indebted Californian municipalities have come under much scrutiny, both inside and outside of bankruptcy courts. This scrutiny has brought to light some of the ambiguities of municipal finance. When the city of Vallejo declared bankruptcy in 2008, it had a total budget of approximately $220 million. However, the city's bankruptcy only concerned its $80 million General Fund. This fund is primarily responsible for paying public employees and supporting local services. Most of its revenues come from property taxes (23%), property transfer taxes (7%) local sales taxes (20%), utility user tax (16%) and vehicle license fees (12%). Other parts of the city's $220 million budget include 'Enterprise Funds', 'Water, Transportation, Marina Golf Funds', 'Community Development Funds', 'Housing, Redevelopment', and 'Mare Island', 'Public Works Funds', 'Fleet Maintenance/Replacement, Gas Tax' and 'Capital Projects'. These funds have their own dedicated revenue and expenditures and, for the main, are separate financial entities from the General Fund. However, during the recent bankruptcy court proceedings of Vallejo, San Bernardino and Stockton, it has become evident that the practice of allocating city funds across various accounts differs between municipalities (Table 1). In Vallejo, the city's General Fund revenues had for decades subsidised failing redevelopment projects (Mialocq, 2008), even though the city had been a relative conservative user of TIF. However, in San Bernardino it has been the General Fund (that is, public services) that has been drawing on redevelopment funds to maintain the city's basic functions (Mulvihill, 2013).

The breakdown of Vallejo's general fund demonstrates the ways in which its local services became bound up with the economic performance of the municipality. When urban redevelopment and consumption continue to grow, the city's coffers are boosted (Hoene, 2004). Consequently the city is able to improve the compensation of its employees and improve its local services. In some Californian cities these growing city revenues became tied to its major expenditure: wages and benefits in the form of collective bargaining agreements (CBAs) with public employee unions. Many Californian cities have seen employee compensation expenditures track at around 70–80% of total General Fund revenues. As Californian cities enjoyed years of rapid economic growth, their employees therefore collected higher salaries and generous benefits. This arrangement was facilitated by binding arbitration and compensation formulas that grouped proximate cities in order to provide adjudicators with a benchmarking mechanism. Public sector employees therefore saw their salaries and benefits track together according to regional conditions. For example, Vallejo's CBAs were based on a comparison group of 14 cities in northern San Francisco Bay region. Consequently, California cities relied on continued economic growth to fulfil the obligations of 3–5 year CBAs.

As expenditures became linked to speculative revenues in many Californian cities, the business of urban governance therefore become focused upon ensuring local growth via financial mechanisms 'based on tenuous promises of future value generation (Weber 2002, 190; Bardhan and Walker, 2011; also see Harvey, 1989). Although not unique—there is evidence that this was a systemic feature of US neo-liberal urbanisation (Kirkpatrick and Smith, 2011)—in California this speculative urbanism took an acute form due to strict statewide fiscal restrictions, regional geographies of economic growth, rampant housing speculation and strong public sector labour unions (Sowell, 2009; Walters, 2010; Bardhan and Walker, 2011).

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These conditions went some way to produce a municipal governance landscape where city councils and planners took part in speculative activities in order to maintain basic levels of service. In this context, where the line between hedge fund gamblers and city managers sometimes became blurred (Jorion, 1995), a sudden economic downturn created a fiscal and governmental crisis of great severity. Consequent attempts by municipalities and the state to resolve this fiscal have been equally sobering.

## Recalibrating for austerity in California

The austerity reforms that continue to be rolled out across California represent a frontier of neo-liberal recalibration, we would claim. Others have argued that it is the "fountainhead of the Great Recession" (Bardhan and Walker, 2011, 303). Our claims are lighter on superlatives, perhaps, but are potentially no less pronounced. Collectively the reforms demonstrate changes to the urban political landscape that, if introduced into other states and jurisdictions, look set to extend—if not fundamentally remake—neo-liberal urbanisation. This is an extended landscape of austerity urbanism in which the "dumping of risks, responsibilities, debts and deficits, to the local scale" (Peck, 2012, 650) produce an increasingly unequal and unstable urban landscape, in which those who govern cities find themselves with fewer levers to pull and under the ever more disciplining effects of the financial markets. In this new Californian normal, established institutional notions of 'mutual independence' have begun to be recalibrated, with states squeezing the ability of city governments to generate revenue streams, through for example the abolition of RDAs and their use of TIF, at the same as cities themselves have begun to redefine the notion of 'municipal failure'.

Speculative risk can be managed in numerous ways by city governments, given their fiscal powers and ability to reform city programmes and services. The management of risk is also built into municipal accounting practices, whereby the separation of revenue streams and expenditures within city budgets allocates risk into defined accounting spaces (Gauthier, 2005). Post-crisis austerity reforms in California are changing how this municipal finance matrix operates and the consequent allocations of speculative risk. In this section we outline the ways in which Chapter 9 bankruptcies are pivotal to this regressive reorganisation, paying particular attention to the example of the city of Vallejo.

Under Chapter 9, Title 11 of the United States Code, cities are permitted to declare bankruptcy if states allow. At present only 28 US states allow their municipal governments to seek Chapter 9 protection (Spiotto, 2012). This number includes a variety of authorisations: 12 specifically authorise, 12 conditionally authorise, three provide limited authorisation, and one state (Iowa) allows certain exceptions to a general prohibition. The remaining 22 states either prohibit or have no specific instructions relating to Chapter 9 (ibid.) Due to the depths of its current municipal crisis, California has seen the nation's most Chapter 9 bankruptcy applications. As these bankruptcies are unfolding, we are witnessing new interpretations of Chapter 9 law being implemented, a consequent redistribution of municipal debt burdens (and consequent state responses), an increased politicisation of municipal finance and new depths to municipal financial failure.

In May 2008 the City of Vallejo became the first post-crisis Chapter 9 applicant. Its filing was unprecedented. Chapter 9 bankruptcy legislation had been originally designed as a mediation process, whereby any debt readjustment had to be agreed with the city's major creditors (Patterson, 1942). The legislation therefore provided no basis for cities to remove or restructure debt obligations without creditor approval. As a consequence Chapter 9 was rarely used by municipalities to deal with structural financial problems. For the most part Chapter 9 has been

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used to restructure special enterprise zones or utility projects where dedicated revenue streams had not delivered forecast incomes. Vallejo challenged this reading of bankruptcy law since it did not gain the approval of its creditors (Trotter, 2011). Instead it claimed its major creditors were making unreasonable demands on it, leaving the city with no option but to restructure without their consent. In this case, as with all cities in the US, the major creditors to general operating expenses are its current and previous employees, in the form of their wages, health benefits and pensions.

On the 13th of March 2009, a District Court judge granted Vallejo Chapter 9 bankruptcy protections based on the criteria that its cash flow situation did not allow it to pay its creditors and good faith negotiations with unions had failed to produce a reasonable solution. The significance of this decision extended far beyond Vallejo, since it created the opportunity, pending court approval, for cities to unilaterally restructure debts, including the voiding of CBAs and bond repayments. The Vallejo judgment therefore radically changed the prevailing interpretation of Chapter 9 bankruptcy law. The consequences of this judgment are still reverberating around the state and further afield. In California, Stockton and San Bernardino are both currently pursuing Chapter 9 readjustment plans that are poised to shake the foundations of California's pension schemes, municipal bond markets and organised labour.

In Vallejo the impacts of Chapter 9 restructuring are still unfolding. Post-bankruptcy the city continues to run deficits (City of Vallejo, 2012). Interim CBAs have served to push labour negotiations down the road, although the efforts the city went to in order that it could restructure its CBAs did not stop it from overlooking CBA renegotiation deadlines in 2012, resulting in the automatic extension of the generous interim agreements. However the city has removed binding arbitration from its City Charter, ensuring that pending contract renegotiations with unions will likely result in industrial action. In the course of Chapter 9 restructuring, Vallejo did cap health benefits to retirees at $300 per month per capita (Walsh, 2011). These benefits had previously been costing the city approximately $1500 per retiree, per month (ibid.). It also established a series of concessions from bond holders and labour unions, the latter limiting wage increases and cutting mandatory staff and service levels.

It is therefore unsurprising that the Californian state government and related agencies have begun to assert their sovereign powers as municipal fiscal collapse threatens to cause significant unrest and/or remake higher levels of government. The Californian state pension agency, CalPERS, has been active in attempting to protect itself from municipalities reneging on payments. When Vallejo entered bankruptcy and had the opportunity to renege on its pension obligations, the city's then finance director, Robert Stout, was informed by CalPERS that any such move would result in endless legal action (Walsh, 2012). No small threat for a cash strapped city, coming as it did from a $200 billion pension fund (Malanga, 2013).

The state government has also legislated to temper potential disruptions emanating from Chapter 9 filings. In 2012, state legislators voted positively on Assembly Bill 506. The bill requires a municipality to participate in a 60-day 'neutral evaluation process' or declare a fiscal emergency that jeopardises the health and well-being of its citizens before seeking protection under Chapter 9. Although some have suggested the bill does little to alter the existing Chapter 9 process (that is, it already requires 'good faith' negotiations with creditors), the legislation is indicative of the concern in Sacramento over the extreme austerity measures being formulated in cities such as Vallejo, Stockton and San Bernardino.

Concerns about the fallout of California's municipal bankruptcies are also present in municipal bond markets. Although Vallejo did not seek to stop bond repayments, fearing

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that credit downgrades would impact its future borrowing options, others have been less concerned about such implications. While a few Californian cities stopping bond repayments is insignificant in terms of the total $2.7 trillion municipal bond market, such actions are nevertheless causing significant concern in financial markets. Municipal bonds have long been considered a safe investment tool, given the predictable revenues and expenditures of cities and implicit state backing. Yet recent non-payments by fiscally beleaguered cites like Stockton and San Bernardino have the municipal bond market asking whether levels of risk should be rated much more highly, with some going as far as to claim that investors could face potential 'municipal bond Armageddon' (Zamansky, 2013).

With many cities reliant on bond markets, there has been a requirement within city government to designate and allocate revenue streams in order that investments can be rated and offered to the market (Hackworth, 2002). Yet, just as the closure of RDAs has redistributed risk within municipalities, Chapter 9 bankruptcies have undermined prevailing understandings of municipal accounting and, consequently, the financial risks associated with municipal debt. Municipal bonds are considered conservative, low risk investments not only because they have largely predictable revenues and expenditures, but also because the legal structures of municipal finance restrict the transfer for monies between funds to situations where a return of borrowed monies can be assured within the fiscal year (Mayer, 2008). As Vallejo's bankruptcy claim was contested in the courts, this understanding of municipal financial regulations was much debated.

For the fiscal year ending in June 2007, Vallejo had a total cash balance of $211 million in reserves. Only a proportion of this was in the soon-to-be-bankrupt General Fund. Some $61 million was administered by legally separate authorities, such as the Vallejo Sanitation and Flood Control District, and the Marine World Joint Powers Agency (Tanner et al. 2008: 12). Restricted trust accounts—primarily subject to debt covenants—accounted for $48 million. An additional $13 million was held as fiduciary funds for the city's five improvement districts. The remaining $89 million in revenue was allocated to the General Fund (ibid.). When the city filed for bankruptcy, it was specifically filing for the bankruptcy of the General Fund.

During bankruptcy hearings, the unions' representatives argued that the city could find monies to cover General Fund shortfalls from other accounts in the city budget, just as it had done in previous years (Mialocq, 2008). This was challenged by the city's financial manager, who argued that any such transfers would be illegal if the city could not demonstrate an ability to repay transferred funds (Mayer, 2008). This issue also drew the attention of the city's major bond holders, who refused to renegotiate debt repayments in the absence of an assurance that the General Fund could become solvent without continual draw-downs from other funds. So, Vallejo's biggest bond-related creditor, Union Bank, agreed to restructure its debts during the course of the city's bankruptcy, taking a 40% reduction in repayments (York, 2011).

Bond markets, via their rating of risk, act on the presumption that different municipal accounts remain largely independent (McGee, 2011). So, for example, when they finance a sewer project the assumption is that sufficient revenues associated with the project will be held within that account. The prospect of moving funds across accounts therefore changes calculations of risk. This 'political' problem has only intensified in many cities as RDAs have become incorporated with general city budgeting.

The closure of the Vallejo RDA—along with over 400 others across the state—on the 1st of February 2012 further worsened the city's already ailing financial situation. However, the impact of RDA closure was less severe in Vallejo than it was in, for example, San Bernardino. Why? Well, because as we have noted earlier, the city had been a relatively conservative user of TIF and property values had grown modestly

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in recent years compared to other areas of the state (Interview 65, April 2012). Vallejo city government and the RDA also had a strained relationship. Unlike the majority of cases across the state, the city retained its proportion of the relatively small 'increment' that had been generated (Interview 73, April 2012). Indeed, the city government regularly subsidised the RDA (Mialocq, 2008). Not only did this reduce the budget of the RDA; it also signalled to potential investors a lack of unity in terms of economic redevelopment strategy. This is perhaps best reflected in the failure of the RDA to deliver the redevelopment of the Mare Island naval yard. Closed in 1996, the RDA had overseen various attempts to redevelop the land. All failed. As a result the TIF revenue stream was just over $2 million per annum when the RDA was wound-down.

Vallejo therefore failed to utilise TIF and RDAs for significant speculative gains and, as such, could not incorporate these prospective incomes into its budgeting. Indeed, the opposite was true; the highly speculative activities of its RDA, such that they were, cost the city money. The factional local political context therefore forced the city government to rely on other sources of speculative income, such as property development fees and local consumption taxes, to boost revenues and support local services. When Vallejo's property market crashed and housing construction abruptly slowed in 2008, the past 'failures' of the city's RDA may well have served to (relatively) limit the immediate budgetary impact of economic recession. However, the city found itself in the same place as many others: facing a curtailing of speculation-fuelled revenue growth and escalating long-term spending and debt repayment obligations.

As many cities in California face fiscal collapse, they are therefore being drawn to political decision-making that requires them to identify winners and losers. In Vallejo's case, the city government reduced health benefits and left pension and bond obligations largely in place. However more dramatic changes are being made in Stockton and San Bernardino. In both these cities, places where RDAs have subsidised General Fund operating expenses, city councils have voted to stop payments to bondholders. In what are being described as "test cases in the titanic battle over whether municipal bondholders or current and retired employees will absorb most of the pain when a state or local government goes broke" (Reid, 2013) these cities are deciding who pays for speculative failure. This, as it occurs within newly minted post-Chapter 9, post-RDA closure budgets, is recasting the financial landscape of urban governance in California.

Whilst places like Vallejo, Stockton and San Bernardino formulate austerity budgets, the consequences of failure within the system of speculative urbanism appear to be reaching greater depths. When Vallejo entered bankruptcy during 2008, the following 2 years featured a host of news articles describing the city's failures. Storylines focused on the growing problem of prostitution and the increasing number of medical marijuana dispensaries dotted around the city's downtown. On the 22nd of August 2011, Bloomberg news ran the headline "Prostitutes Flood Vallejo as Bankrupt City Slashes Police Force by a Third". The headline reflected the city police's austerity-led decision to only respond to emergency calls and dramatically cut regular patrols. Indeed, throughout 2008–9 residents complained that calls to the Police Department regularly went to voicemail (Interview 28A, October 2012). Similar cutbacks have been implemented in the fire department, where stations have been closed and the number of firefighters significantly reduced (Interview 3, July 2010).

With local emergency services stretched and residents increasingly uneasy with levels of service, community relations have become tense. During 2012 Vallejo police shot and killed six people in the city. On each occasion police officers claimed that the use of deadly force was justified. The deaths have highlighted the racial divides within the town. When residents packed

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into city hall on 11 September 2012 to protest the conduct of Vallejo's police, the majority of attendees were racial minorities. The sister, Cindy Mitchell, of one of the shooting victims, Romero Mitchell (killed 2 September 2012, reaching for a pellet gun in his car), spoke at the meeting about the mischaracterisations of her brother that had circulated after his death: "…you guys are slandering my brother's name, calling him a parolee when he was never on parole, never been to prison, never sold drugs, never, okay!" Other residents interviewed complained that their working class neighbourhoods had become policed by "shoot happy cops" who only cared about "protecting each other and their big paychecks" (Interview 34B, September 2012).

Middle-class residents have not been exempt from austerity, however. On Mare Island, residents who bought houses in new bourgeois residential districts constructed in the early 2000s saw two fire houses close in 2010 as the city implemented bankruptcy-related cutbacks. The closing of Station 28 on Nimitz Avenue, located on Mare Island, meant the new residents of the peninsula development now have no local emergency services and face much longer response times. Although the fire unions challenged the legality of these cutbacks, they have remained in place leaving middle-class residents in Mare Island without previously mandated levels of emergency services. Residents complained that they still pay a supplemental local tax that was intended to support these services (Interview 2C, September 2012). This situation will become more precarious when a local bridge is closed for repairs, leaving the emergency services an additional two miles to travel to Mare Island.

Vallejo's descent into bankruptcy has therefore redefined levels of service provision. Police and fire services are run at bare minimums, answering only emergency calls. The resulting situation has witnessed growing intra- and inter-community tensions across the city, as residents blame the city's financial failures for shootings, high crime rates and house fires. Vallejo's fiscal crisis is therefore redrawing the depths of speculative failure: fire and police services are being reduced to levels previously thought unsafe; local services, such as libraries and community programmes have been reduced or removed. The costs of being a failed entrepreneurial and speculative city appear greater than ever before.

## Conclusion

> Cities are … where austerity bites (Peck, 2012, 629)

According to Gelinas (2010, np) "[t]he uncomfortable truth is that as municipal debt grows, the risk mounts that someday it will be politically, economically and financially worthwhile for borrowers to escape it." Writing after the bankruptcy of Vallejo and before San Bernardino and Stockton followed suit, this piece in the *City Journal* at the Manhattan Institute criticised investors who continue to value municipal bonds despite the evidence that many cities and counties have overstretched themselves. The argument was a simple one. Investors are kidding themselves if they think that states and cities can't fail. They can and they do. A growing number of Californian cities have either declaring bankruptcy or have threatened to do so as a means of gaining leverage over debt holders, labour unions and state officials. This is a high stakes game. "The deficit crisis created an opportunity for conservative state governments to both slash government spending and seriously weaken or destroy public sector unions", according to Crotty (2012, 97).

While it is likely that few on either the left or the right would argue that California is a 'conservative' state, nevertheless, what we are witnessing currently within it are city governments "implementing locally what was defeated nationally" (Davis 2013, 10). So, the services that are now being targeted, in places such as Vallejo and San Bernardino, in

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the name of austerity are those that remained largely untouched by past waves of neo-liberal outsourcing and privatisation. Fire and police professions—and their associated pay and pension—have been targeted by city officials in order to cut public expenditure to the point where it balances out with shrinking property tax revenues. Meanwhile, a range of services are being cut: lights being turned off, schools being closed and streets being left uncleaned.

As the costs of the financial crisis are divided between different levels of government (see Peck, 2012), many cities are ill-prepared to deal with any newly imposed responsibilities. When the Californian state government closed its RDAs, a number of the state's cities faced fiscal failure. Already addicted to growth and burdened with high levels of debt, they have found themselves with few reform options. When Vallejo was granted Chapter 9 eligibility in 2008, it offered a way forward for beleaguered cities: bankruptcy protected reforms to CBAs and bond debt. As the subsequent Chapter 9 filings of San Bernardino and Stockton are demonstrating, this combination of urban fiscal crisis and new legislative context has created a new regime of action.

Speculative urbanism under austerity is creating a turbulent and insecure political landscape. Whilst those cities that have pursued bankruptcy have brought crisis to retirees in ill-health (that is, Vallejo) and slashed the value of bond holdings (that is, San Bernardino and Stockton), these cases are also changing the stakes of municipal politics. What were once sacred cows are now fair game, enabling cities in fiscal crisis to threaten creditors with unilateral changes that would, a short time ago, have been unthinkable. This has not gone unnoticed to the purveyors of neoliberal ideology such as the Manhattan Institute (Gelinas, 2013) and Heritage Foundation (Tucker, 2013), both of whom have cast municipal bankruptcy as an indicator of liberal governmental failure and have made the case for further neoliberal reform. City hall has therefore once again become a key venue of class politics in the age of austerity, the place where attempts to resolve a structural economic crisis are playing out, but where 'local' decisions are informed, if not sometimes determined, but a legacy of fiscal calculations make in reference to 'global' financial markets.

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