

AB 506 Process Frequently Asked Questions (FAQs) and Answers for City of Stockton Employees

Q. What's happened?

- The City has embarked on a process designed to *avoid* bankruptcy.
- The City has not declared bankruptcy. However, our situation is serious, and requires urgent action.
- City staff and outside experts have determined that more service reductions and further cuts to employee pay and benefits will not be enough to get us through this crisis.
- Therefore, the City has extended our fiscal emergency, and has begun what's called an AB 506 Confidential Neutral Mediation Process (AB 506 Process).

Q. What is the AB 506 Process?

- The State of California passed Assembly Bill 506, which provides a clear path for cities facing imminent fiscal emergencies.
- The law, which was sponsored by organized labor, went into effect on January 1, 2012.
- The AB 506 Process allows cities that have declared a fiscal emergency to enter into a period of restructuring debt with major creditors and "interested parties." These are parties with whom the City has \$5 million or more in obligations or debt.
- The AB 506 Process is similar to the restructuring process used by private sector companies, as a way to avoid bankruptcy.
- The City and the interested parties will select a neutral mediator with the goal of reaching an agreement on how to manage Stockton's debt obligations.
- By law, the process must remain confidential until an agreement is reached by all parties, at which time the City Council will vote on the final agreement in open session.
- The process lasts 60-90 days, once the mediator is selected.

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Q. Who is involved in the AB 506 Process?

- Working with the neutral mediator, the City will seek to address our debt obligations by engaging our largest creditors – for example, employees, retirees, bond insurers and trustees.
- We have provided notice to our largest creditors of our current fiscal status.
- The mediation process itself and interactions with creditors will be, by law, confidential.

Q. How did we get here?

- The sources of our fiscal situation include unsustainable retiree health insurance that was not properly funded since its inception in the 1990's; some unsustainable labor contracts that still remain; an extreme amount of debt issued in the first decade of this century; constant State raids on City resources; the protracted Valley recession; and decades of poor fiscal management practices.
- When Stockton was booming in the years before the recession, the City's finances were handled as if the good times would go on forever and revenues would keep growing.
- As a result, the City made financial obligations that relied on continuous revenue growth.
- Making matters worse, years of weak accounting controls and lax financial practices obscured problems that have been uncovered by current City management. As a result, we now know that our situation is worse than we thought.
- While other California cities have faced problems during the economic downturn, Stockton's significant level of unfunded financial obligations makes our situation more dire than most others in the state.
- The City made financial commitments to employees and retirees and there was no long-term structure put in place to maintain these commitments.
- For example, Stockton faces an enormous, unfunded retiree healthcare liability of \$417 million. In fact, starting next year, the City will be paying more for *retirees* than for *current* employees – an unsustainable fiscal path. We expect these retiree health costs to double in the next ten years.

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Q. How did we get here? (continued)

- The City also borrowed money to pay for buildings and facilities, counting on continuously growing revenues to pay down the debt. With the financial crash, those revenues have now evaporated.
- Despite four years of austerity – including \$60 million in cuts to programs, services, pay and benefits over the past two years alone – the City has struggled to keep revenues and expenditures in balance.
- Despite past cuts, the General Fund is expecting increased deficits in the foreseeable future.
- The City manager and City Council feel the employees have borne the brunt of the cuts and now it's time for others to share in the pain.

Q. How does this affect me?

- *Employees will continue to get paid* – you will receive your paychecks and your benefits.
- There will be a temporary suspension of cashing-out of annual, sick and other leave balances – to avoid a large dollar value of payouts occurring at once. If many employees sought cash-outs, it would deplete City cash available resources and push us back into insolvency and uncontrolled default.
- The leave payoff suspension is temporary. The City is looking at possible solutions to the suspension of these payoffs without jeopardizing the City ability to pay its employees and vendors.
- We ask that you remain committed to the City of Stockton and continue to focus on providing the highest level of service while we work through this restructuring process.
- Given that retiree health insurance has to be on the table to resolve our fiscal situation, we do not see any benefit in premature retirement.
- Employees have already been doing their part. In recent years, employees have helped the City begin to tackle its fiscal problems by taking pay cuts, absorbing work furloughs and paying a greater share of healthcare costs.
- We will now ask our creditors to participate in the solution to this crisis.

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Q. How does this affect me? (continued)

- We ask that you help us minimize confusion about this situation by directing anyone who has questions about the AB 506 Process to our website or to the City's Public Information Officer.

Q. What does this mean for our citizens?

- Citizens, too, have participated by absorbing unfortunate service reductions.
- We will now ask our creditors to participate in the solution to this crisis.
- The AB 506 Process will not have any immediate, discernible effect on residents or visitors, as services will continue to be provided and bills will continue to be paid.
- We as a City must remain committed to the safety and well-being of our citizens, and to providing the highest levels of service.
- The AB 506 Process allows the City to continue to provide everyday services to the people of Stockton.
- The AB 506 Process allows us to conduct business and pay our bills to businesses and vendors. In fact, you can tell everyone whom we conduct business with, that we will pay all our bills. Only 3 bond payments and employee buy outs are affected.

Q. What is the City Council's Role?

- This City Council has been faced with a series of difficult decisions, and has made tough choices in the best interests of the City of Stockton.
- By adopting a 10-point plan for fiscal sustainability, the Council has managed to rein in costs, control spending and begin the enormous task of tackling Stockton long-term structural problems.
- The Council has closed huge budget deficits over the last four consecutive fiscal years.
- The Council will continue to do everything in its power to maintain fiscal solvency, by focusing on current spending decisions while the AB 506 Process proceeds.

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Q. What is the City Council's Role? (continued)

- The Council will ultimately decide on any final agreement reached through the neutral mediation process.

Q. What is city management doing about it?

- Our staff's analysis of the financial situation was so dire that we contracted with outside experts to give us a second opinion.
- Outside experts, Management Partners, Inc., validated staff's assessment and confirmed that restructuring is urgent because, if we continue on our current course, the City will run out of money soon.
- We have made progress in the last year with a 10-point plan for fiscal sustainability – highlighted by restructuring employee compensation and bringing our employee pay and benefits more in line with cities that are comparable in size, location and demographics.
- We know these changes have been tough on everyone, and we're grateful for our employees' participation.
- We have cut services to the bone, reducing programs and services. These were painful cuts, felt throughout the community, but necessary to maintain the City's solvency.
- We will use a new process established by state law, AB 506, to renegotiate our financial commitments to stabilize the City and help us rebuild a financially sustainable municipal government.
- As a result, cost reductions will be spread across a larger base, so that employees, and services to the public, will no longer bear the full impact of balancing the budget.
- We will work through the restructuring process with your labor representatives to achieve long-term employment stability, with pay and benefits consistent with the market.