

MANUFACTURING

9.0%

HOSPITALITY & LEISURE

1.9%

RETAIL SALES

0.7%

WHOLESALE TRADE

9.7%

GOVERNMENT SERVICES

1.9%

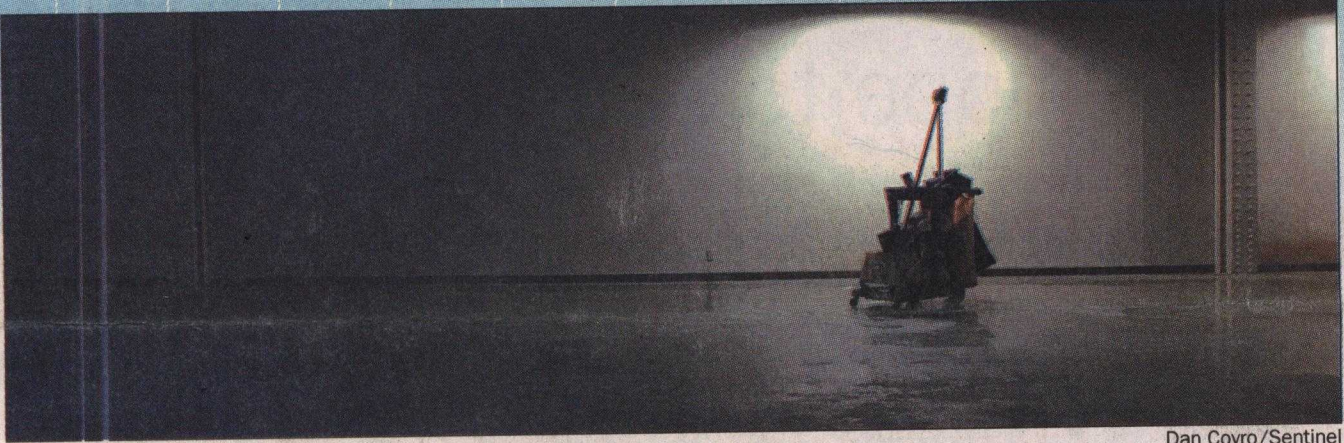
CRUNCH TIME



Cities cope with life in the red

County labor force
Traditionally-strong sectors of the county economy continued to take hits over the past year, resulting in declines in the labor force. (Top)
SOURCE: State Employee Development Department.

County unemployment
(Above)
SOURCE: State Employee Development Department.



Dan Coyro/Sentinel

Space where the county's manufacturing industry once thrived is now vacant, and city budgets are feeling the effects.

S.C. officials debate economic future



WHEN EVERY DOLLAR COUNTS

An ongoing look at tight budgets and tough decisions

Budget
EDITOR'S NOTE: This is the first part of a series exploring the economic downturn in Santa Cruz County. The Sentinel this week examines the factors that contributed to budget deficits in cities like Santa Cruz and looks at ways lost revenues may return to city coffers.

By DAN WHITE
SENTINEL STAFF WRITER

SANTA CRUZ — City officials were in a panic. Facing worker layoffs and a budget crisis worsened by state take-aways, city leaders were forced to sock residents with new utility fees. They entered into money-making talks with UC Santa Cruz about a new, state-of-the-art research park and argued over revenue-building plans to put a hotel and conference

center in Beach Flats. While this scenario might sound strangely familiar, it unfolded 20 years ago. It was the early '80s. The economy was soft, and Proposition 13's rollback of property tax revenues left the city scrambling for dollars. Today, the situation is even worse, officials say. City Finance Director David Culver, commenting on how so many fiscal problems are hitting at once, calls it "the perfect storm." Santa Cruz, with a \$48 million general fund budget, is saddled with a \$1.8 million deficit. And the loss of its manufacturing base and a drop in tourist dollars probably won't boost city coffers anytime soon. Weak city revenues, combined with the state's possible takeaway of vehicle license fees and a multi-

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Next Sunday
The Sentinel, on March 16, looks at how individuals are getting by on smaller budgets. There may be a lesson in store for you. If you have any advice on how to survive during tough economic times or, perhaps, a story to tell about scraping pennies, please send your thoughts to kalexander@santa-cruz.com. Please include your name, hometown and a contact number.

million dollar increase in employee pension costs, could bring the city's deficit to an unprecedented \$6 million-\$8 million within the next three years. Numbers aside, this means the

Budget

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possible shutdown of the Santa Cruz Civic Center and teen center, slashing social programs for the poor, cutting police positions and more.

So, what's a city to do?

On the table are any number of ideas — some old and some new, but all bound to create controversy in an outspoken community where, according to a former council member, Keith Sugar, "the very air elicits an opinion."

For starters, city officials are in the process of tightening their budget by cutting employees and services, adding a few fees and thinking about asking voters to approve a parcel tax.

But budget taming alone won't solve the long-term issue of declining tax revenues in traditionally strong sectors like manufacturing and tourism.

Hoping to draw new revenues to the city, some people want plans for a beach hotel and conference center and UC partnership revisited. Others want a cultural arts center, complete with shops and concert venues.

A few are looking at retail giants like Costco that have funneled cash into the city budget but prompted the so-called "big-box" controversy.

City Councilman Tim Fitzmaurice expressed optimism that the right combination of plans would eventually lift the city out of its current financial doldrums.

"Our gap is not impossible," he said. "We can do it by wise management of our resources, with a little good faith from the state and federal government."

The fall of manufacturing

The loss of so many manufacturers, from gum-makers to electronics manufacturers, is a major reason why the city cash flow is in decline.

In the past two years, annual tax revenues from manufacturers were down more than \$2 million, according to city officials.

During this time, Santa Cruz saw the loss of Lipton Tea, Salz Tannery and the city's largest manufacturer, Texas Instruments. The loss of Texas Instruments alone cost the city \$2 million a year in property and utility taxes, nearly 5 percent of the city's general fund budget.

While depleting the city's coffers, the shutdown of manufacturing heavyweights also cost the city 835 jobs — not including 300 jobs eliminated when Wm. Wrigley Jr. Co. closed its plant on the Westside of Santa Cruz in 1996.

The job losses are even greater than the numbers suggest because most manufacturers were downsizing many years before shutting down completely.

The pull-outs led to accusations from the business community that the city's "anti-business" climate, and the left-leaning politics of the

ager Dick Wilson pointed out that there are allegations that Santa Cruz officials have courted business too forcefully.

He acknowledged a longtime "conflict between the fact that we want and demand social services but want to be a 'low-revenue environment.'"

"There's a high level of opposition to things that produce a lot of tax return," he said.

While the bulk of manufacturers and their tax revenues are gone, a small number of manufacturing facilities remain. Among them: Harmony Foods Corp. with 220 employees, Raytek Corp. with 141 employees and Plantronics with 420 employees.

But Wilson said the city can't expect large-scale manufacturing to ever return.

"Nationally, that sector has been shrinking for decades," Wilson said. "The U.S. economy has long been becoming a service economy, not a manufacturing economy."

He said the lack of a rail or air network in Santa Cruz as well as shipping limitations didn't help.

"They go where labor and property costs are going to be a lot less, either overseas or elsewhere in the United States," he explained.

Courting R&D

One hot topic of conversation, amid cold budget talk, is a city partnership with UC Santa Cruz. The goal — joint revenue-building projects.

"After all this time, Santa Cruz should start thinking about UCSC as a local business," said Primack.

Some may remember bitter opposition in 1985 to UC's proposal to put a research park on campus, under Chancellor Robert Sinshemer. In light of the uproar, critics may wonder why city officials are now discussing the similar idea of off-campus research offices.

Many say there's more to gain this time.

State Assemblyman John Laird, D-Santa Cruz, who was Santa Cruz mayor when the idea arose, said the project then "would have required city contributions without revenue coming back to us. It was an economic loser and unfair."

Students and City Council members also shared traffic and housing concerns about the initial proposal, and some complained that the city would have too little say over the project.

But since the nearly 20-year-old debate, UC has pumped up its research facilities with the creation of an engineering school, a much larger computer engineering program and new resources for natural science students.

A by-product of this expansion, some say, could be a handful of new high-tech spin-offs and small-scale manufacturers that create high-paying, stable jobs and possibly new tax revenues.

Though officials know that this alone won't make up for manufacturing losses, they say new research start-ups would help boost city coffers.



Dan Coyro/Sentinel

Texas Instruments shut its Santa Cruz plant down in 2001.

But ambivalence toward tourists is the least of the visitors council's worries now. Its problem is the tourism cash cow is in bad shape.

Santa Cruz had the second highest decline in hotel occupancy rates last year than any other area in California, according to the state Travel and Tourism Commission.

Accordingly, Santa Cruz's room tax revenues fell 25 percent last fiscal year, the first slip since 1993-94. Over the past five years, the hotel tax brought the city an average of \$3.3 million each year.

The recent drop in Santa Cruz mirrors what is going on in the rest of the county, where room tax collections fell an average of 21 percent.

The unincorporated areas of the county fared worse, falling 27 percent. Scotts Valley dropped 31 percent. Capitola fell only 9 percent. Watsonville bucked the trend with tax receipts climbing 24 percent.

Traditionally, tourism in Santa Cruz County has been somewhat recession-proof because it depends heavily on a "drive" market, meaning more than 80 percent of people who visit here get here by car instead of more costly forms of transportation, said Raneë Ruble, visitors council spokeswoman.

This year, though, this hasn't been true and experts are wondering why.

"I don't have one clean answer for you, but I have several theories," said Ruble.

One certain factor, she said, is that the Holiday Inn was leased to UC Santa Cruz for student dorms in the fall of 2001, eliminating hotel tax revenues to the city estimated at \$500,000 annually.

A sharp decline in business travel to such locations as the Santa Cruz Coast Hotel was another reason for slipping tax revenues for the city, Ruble said.

She explained that a dramatic increase in the number of relatively low-cost lodgings in South County, luring travelers south from hotels in Santa Cruz, played into the occupancy trends.

The new Holiday Inn Express in Watsonville became a popular option, for example. So did other modestly-priced motels like the Red Roof Inn which charges about \$125 a night during the peak season as compared to more than \$200 a night at places like the Comfort

looming question: if there was a conference hotel, where would it go?"

The initial location, the aging La Bahia facility on Beach Street, may be out of bounds now because of a proposal to develop a 100-room "boutique" hotel.

Kennedy has gone so far as to say he'll oppose the smaller hotel unless the council gives him some guarantee that approving the project at La Bahia won't preclude the city from developing a much larger hotel elsewhere — or perhaps one day incorporating La Bahia into that larger plan.

Rotkin hasn't gone so far as to say he'd try to block a smaller La Bahia plan, though he'll say, flat out, that he hopes the boutique hotel plan falls by the wayside.

Reports by developer Barry Swenson Builder show that the smaller hotel plan may in fact be stalled because of financing problems. Nonetheless, the firm is still planning to seek approval from the City Council this summer.

Kennedy said a new conference hotel should have at least 275 rooms to be cost effective.

The size is what has troubled critics, who claim the project is too big for Santa Cruz.

"A conference center doesn't have to be on that scale because of neighbors and major traffic," said ex-Mayor Christopher Krohn.

Another topic of discussion is the creation of a proposed \$42 million arts complex at the defunct Salz Leather plant along the San Lorenzo River. The complex would have performing and visual arts space and places for artists to sell their wares.

The project has been dubbed, by Redevelopment Director Ceil Cirillo, as Santa Cruz's answer to Fort Mason in San Francisco with its string of historic buildings in the city's marina district, now converted to a performing arts center, and featuring world-renowned vegetarian restaurant Greens.

Supporters hail the Salz project as a way to beef up revenue. Others denounce it as a waste of money.

Mayor Emily Reilly is a vocal supporter.

She said the project could make Santa Cruz a "cultural tourism" hot spot: "This project could put us on the map as an arts destina-

tion across the street.

The city does not have an estimated time frame for construction.

Assemblyman Laird recognized the dilemma between wanting tax revenues from giant retailers and not wanting to dramatically change the retail landscape.

"The people of Santa Cruz shouldn't do something they wouldn't do otherwise just because of money," he said.

Costco does not disclose its local sales revenues, but city officials say the retailer "far exceeded" its projections to do more than \$100 million a year. This means that sales taxes to the city exceed \$650,000 a year.

Vice Mayor Kennedy, who was criticized by some for supporting Costco's construction seven years ago, said the business's success is testament to its public support.

"If it's totally against the character of Santa Cruz, then who are all the people who are shopping there?" he asked.

Mayor Reilly said she's cautious about chain-store proposals.

"Some of these box stores are really predatory and would hurt local businesses," she said.

A closer look at the budget

Aside from flashy prospects of money-making hotels, cultural centers and new retail outlets, city officials are moving forward with the basics of trimming a budget: fee increases and service cuts.

City leaders plan to impose a surcharge on all local phone bills to raise an annual \$1.3 million for the 9-1-1 emergency system. Officials don't have an exact figure but say the surcharge will be "less than \$2 per bill."

The council has also imposed a plan to jack up parking meter costs in the Beach Area, from 50-75 cents to a uniform \$1 per hour. On top of this, the city is considering a "smart" parking system that would erase any left-over time on a meter when a car leaves, maximizing income.

Additionally, the City Council has spoken informally about imposing a parcel tax on property owners. Such a tax requires a two-thirds approval from voters.

"It's certainly not something

jobs eliminated when Wrigley Jr. Co. closed its plant on the Westside of Santa Cruz in 1996.

The job losses are even greater than the numbers suggest because most manufacturers were downsizing many years before shutting down completely.

The pull-outs led to accusations from the business community that the city's "anti-business" climate, and the left-leaning politics of the City Council worsened the problems.

Fair or undeserved, the image is pervasive.

When bike manufacturer Giro moved its plant out of state in the late '90s, resulting in more than 100 layoffs, a national bicycle industry trade publication blamed the City Council and claimed that Santa Cruz "scares manufacturing away."

City Councilman Mark Primack sees some truth in arguments about the city's "institutional ambivalence" toward business reflected in laws and attitudes.

"It's the 'Welcome to Santa Cruz, now leave' bumper sticker ... that ambivalence at every level," he said.

"Yes, we want your business but we don't want to give you a building or water to set it up," he said, describing the Santa Cruz sentiment. "We have to come to grips with what it means to be a community that supports services."

Others like Councilman Fitzmaurice deny any anti-business bent.

Fitzmaurice insists the city has a "good record of supporting businesses who come here."

He said that city officials courted Texas Instruments and worked hard to persuade such manufacturers to stay.

"We lost that business not because of any poor practice on our part but because of reversals in their business environment," he explained.

The reasons cited by many corporations for leaving were competition with overseas markets, business consolidation and the high cost of doing business in Santa Cruz — or, for that matter, most anywhere in California.

Contrary to claims of city leaders opposing business, City Man-

ufacturers, many say, could be a handful of new high-tech spin-offs and small-scale manufacturers that create high-paying, stable jobs and possibly new tax revenues.

Though officials know that this alone won't make up for manufacturing losses, they say new research start-ups would help boost city coffers.

UC and city officials have been holding informal talks about partnership possibilities.

One option, advocated by UCSC vice chancellor for research Robert C. Miller, is to develop a research park in some of the city's vacant industrial space on the Westside.

The Harvey West industrial park, which also has a number of vacancies, is considered a likely spot as well.

These proposals are bound to generate controversy among residents, many who want to see industrial space set aside for affordable housing and are suspicious of UCSC's growth.

But city administrators plan to consider the ideas anyway.

"We have lost over 1,000 jobs on the Westside in the last few years," said Joe Hall of the city Redevelopment Agency. "R and D would be at least a way to start replacing what we lost."

Revisiting tourism

City residents have a relationship with tourism that ranges from warm to prickly.

While tourism generates more than \$3 million in hotel tax for the city each year, residents are wary. They think of summertime traffic snarls and crowded Pacific Avenue hot spots.

Look no further than the controversy surrounding last year's Measure Q, the initiative that would have boosted hotel room taxes to help pay for the Santa Cruz County Conference and Visitors Council, the county's publicly-supported tourism promoter.

The pro-tourist industry measure failed, with opponents like property owner Gordon Pusser going as far as calling the plan "corporate welfare."

County, luring travelers south from hotels in Santa Cruz, played into the occupancy trends.

The new Holiday Inn Express in Watsonville became a popular option, for example. So did other modestly-priced motels like the Red Roof Inn which charges about \$125 a night during the peak season as compared to more than \$200 a night at places like the Comfort Inn Santa Cruz.

Ted Burke, who owns the Shadowbrook Restaurant in Capitola, and sits on the state's Travel and Tourism Commission, said one reason for Santa Cruz's tourism decline is "we don't have the facilities we used to."

Burke said the city needs to address the needs of the business market.

One proposal lingering in recent years, with a track record of creating controversy, is a plan to put a hotel and conference center in the Beach Flats area, potentially twice as large as any hotel in town.

Backers of the hotel say it will beef up tourism by drawing more visitors, including well-heeled executives with more spending money, during the off-peak season.

There has been no formal discussion of the conference hotel plan recently, but Councilman Mike Rotkin said he'd like to revive the idea.

A hotel proposal was part of a Beach Area development plan that went down in flames three years ago because opponents declared it an expensive, sprawling boondoggle that would displace low-income residents currently living in the area.

Opponents also didn't like the idea of a partnership between the city and Beach Flats landowner Seaside Co., the city's biggest private employer.

While Vice Mayor Scott Kennedy vocally supports a conference hotel, saying it would be an answer to weak tourist revenue in off-peak seasons, he isn't holding his breath.

"I don't see anything on the horizon," he said. "There is also the

etarian restaurant Greens. Supporters hail the Salz project as a way to beef up revenue. Others denounce it as a waste of money.

Mayor Emily Reilly is a vocal supporter. She said the project could make Santa Cruz a "cultural tourism" hot spot: "This project could put us on the map as an arts destination."

The city has made no firm commitments to the proposal but has taken it seriously enough to spend \$175,000, in redevelopment funds, to study the idea.

Minnesota-based Artspace — the consultant and potential investor — has said the vast majority of funds would come from federal and philanthropic sources. Cirillo said it's unclear what the local portion of the costs would be.

The local cost is what concerns critics of the plan.

"Surely when the city cannot perform basic services like street maintenance and keeping schools open you would not even think of spending money on a plan for an arts studio and performing space," wrote resident Mary Lopez in a letter to City Council.

Rekindling retail

Costco and the Gateway Plaza not only brought thousands of feet of retail to Santa Cruz with tens of thousands of dollars in ensuing tax revenues, but the retail projects brought the polarizing issue of "big box" development to town.

Currently, there are no proposals for retail giants like Costco before the City Council, and Wilson doesn't expect any soon. "They aren't knocking on our doors," he said.

But at least one box store is about to get bigger.

The City Council, in December, approved Costco's plan to demolish the tire center and replace it with a slightly larger tire center and add almost 13,000 square feet to the warehouse. Also, the plan calls for a new four-island gas sta-

tion to a uniform \$1 per hour. On top of this, the city is considering a "smart" parking system that would erase any left-over time on a meter when a car leaves, maximizing income.

Additionally, the City Council has spoken informally about imposing a parcel tax on property owners. Such a tax requires a two-thirds approval from voters.

"It's certainly not something that is imminent, but we are talking about it," Mayor Reilly said. "We'd have to do polling first."

She said she hoped a parcel tax could be geared to a specific purpose such as preserving greenbelt lands, fixing sidewalks and maintaining park services.

Unfortunately, it is unlikely that revenue-builders will prevent city leaders from having to make major cuts to the city budget.

Consequently, the community is likely to lose services ranging from park rangers to maintenance staff, and less funding will be available for programs like homeless services.

Already city officials have eliminated 13 positions from the payroll, resulting in two layoffs, and could lay off more than 100 of its current 850 employees over the next few years.

That number is down from a 2000-01 high of 882 employees before city officials had started their belt tightening.

City Manager Wilson said the government is not likely to be as big anytime soon.

"I believe we'll have far fewer city employees in the future, I think for decades," he said.

"We think we'll limp through the rest of this year, take another million out, hold our breath and see what the state does," he added. "If the state visits more new cuts on us, all bets are off."

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