

Jefferson County, Alabama: A Perfect Storm of Ethical, Financial, Political, and Market Failures

by

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A dissertation submitted to the Graduate Faculty of
Auburn University
in partial fulfillment of the
requirements for the Degree of
Doctor of Philosophy
Auburn, Alabama
August 6, 2011

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Abstract

This study details the ethical, financial, political, and market failures that have nearly caused the Jefferson County, Alabama to file what may become the largest municipal bankruptcy in the history of the nation.

Acknowledgments

Acknowledgements for a work of this nature are fraught with danger because so many people have had to listen to my rants and raves about the body politic in Jefferson County. However, a special thank you must go to Charles Ball, Executive Director of the Regional Planning Commission and the entire Board of Directors of the RPCGB who have supported me in this endeavor wholeheartedly. Also, my gratitude to the staff of the RPCGB, especially Yvonne Murray who has had to hear more than her fair share of ideas and thoughts on this topic than she would ever admit too, are more than I can repay. I especially wish to thank my committee who has never failed to provide the guidance I need to make this work a reality. A special debt of gratitude is owed to Jim Byram and Troy Post, both of these gentlemen gave me my start in public administration and have and continue to be mentors and friends. Last, but most importantly, I thank my wife Katharine and her family for all the moral support and prodding provided along the way. I could not have done it without you.

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List of Abbreviations

ADEM	Alabama Department of Environmental Management
ARS	Auction Rate Securities
BBA	Birmingham Business Alliance
BoB	Bureau of the Budget
CAO	Chief Administrative Officer
CD	Consent Decree
CDO	Collateralized Debt Obligation
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CIP	Capital Improvement Plan
CM	City/County Manager
CRS	Cahaba River Society
CWA	Clean Water Act
EPA	Environmental Protection Agency
ESD	Environmental Services Department
FBI	Federal Bureau of Investigation
ICMA	International City/County Management Association
IDB	Industrial Development Board

IRS	Internal Revenue Service
Jeffco	Jefferson County
LGC	Local Government Commission
LIBOR	London Interbank Offering Rate
NIH	National Institutes of Health
NINJA	No Income No Job or Assets
NPDES	National Pollution Discharge Elimination System
OCIP	Orange County Investment Pool
PARCA	Public Affairs Research Council of Alabama
PIMCO	Pacific Investment and Management Company
SEC	Securities and Exchange Commission
SIV	Special Investment Vehicle
UDC	Urban Development Corporation
VaR	Value at Risk
WTSCIP	Waste Treatment System Capital Improvement Plan
WWTP	Waste Water Treatment Plant

CHAPTER 1

Introduction

In 1996, the United States, in conjunction with Rodney Kipp, Edwin Angwin, and Betty Angwin, filed a lawsuit against Jefferson County, Alabama, in an effort to prevent further pollution of the Cahaba River via the sewer systems located within the jurisdiction of the county. The Cahaba River and more than half of its tributaries are considered impaired (Resources 2008). This has been cause for great alarm due to the fact that the Cahaba River also “supports 64 rare and imperiled plant and animal species, 13 of which are found nowhere else in the world. The river has more fish species, at 131, than any other river [its] size in North America” (Service n.d.). In an effort to end the lawsuit the County is currently under a consent decree, whereby it agreed to assume all of the sewer systems within its jurisdiction. This entailed acquiring twenty-one individual systems and thousands of miles of sewer line from other local governments (BE & K 2003, 1). In order to finance the necessary repairs, the county floated a large number of revenue bonds; however, due to bribery, corruption, and general mismanagement, the costs for rehabilitating the sewer skyrocketed. Then, due to complaints from ratepayers, the County entered into several risky financial transactions which were designed to keep rates from increasing, but because of the inherent risk, the County soon went from nearly 99% fixed interest rate bonds, to nearly 95% variable, which means that bond payments are based on ever-changing market conditions. Next, the County became the victim of macroeconomic factors which were brought about by the subprime crisis. Additionally, Jefferson County has suffered a loss of over

\$75 million dollars per year in general revenues due to an occupational tax levied on incomes and a business license fee being found unconstitutional by the Alabama Supreme Court (Wright and Chandler 2009). As a result of these machinations Jefferson County may have to declare Chapter 9 bankruptcy which will have ripple effects for scores of municipalities. Jefferson County has truly experienced a perfect storm of financial ineptitude, bribery and corruption, economic factors, a hostile public, and assaults from the legal community which have transpired to nearly ruin the most populous county in the State of Alabama.

Statement of the Problem

The county was not the first nor will it be the last to suffer from economic uncertainties, illegal activities, and lackluster administration. Other counties and jurisdictions could follow suit, perhaps this dissertation could be of some assistance in steering them clear of this path. Jefferson County's plight is certainly placing it squarely in the national spotlight as a warning for other jurisdictions, investment bankers, elected officials and public administrators alike.

Twenty-six people have been indicted or pled guilty to a variety of charges stemming from bribery and corruption. A recent article in the Birmingham News discussing the recent trial of the former County Commission President, and now former Mayor of the City of Birmingham, cites a former official with the Securities and Exchange Commission as saying, "Hanky-panky [under the table payments] between investment bankers and elected officials happens regularly." The News goes on to warn "[t]he blatantly illegal practice is still common enough that [SEC officials] expect[] the Langford trial to get widespread attention from nervous politicians and investment bankers nationwide" (Hubbard, al.com 2009). The problems of the County and the region are not limited to just those convicted. The public ultimately must pay for the repercussions of such malfeasance. This will come not just in the form of higher taxation, but

also in the form of lost economic development as the instability of Jefferson County ripples across the region and affects statewide economic development and financing as well. However, in order to address the potential backlash it is important to understand true underlying causes of such decline.

Research Question

“Almost all political theories seem to originate from a perception of disorder in the body politic” (Spragens 2007, 10). This work is certainly no exception as Jefferson County is definitely in the throes of disorder. Therefore, this dissertation seeks to answer the research question of why Jefferson County, Alabama, failed both financially and as a political body through a case study approach. Subsequent and related questions that will also be addressed include an examination of the after-effects of the crisis and an analysis based on the case study about what can/should be done to repair and prevent such failures in the future. Now seems like an appropriate point to stop and address the question of why not write this dissertation as a part of the public finance subfield? I feel that political science and public administration should still use political theory as a method and framework for addressing many of the ills our society and organizations face today. While quantitative studies have extreme value; the use of history, with prescriptive advice, can also yield tremendous dividends, especially to a larger public which may benefit from such advice. This is the situation with Jefferson County.

Theoretical Framework

“The core of any political theory is a broad descriptive account of what is going on beneath the surface, sound, and fury of human politics” (Spragens 2007, 3). Considering the breadth of the debacle created in Jefferson County a case study inquiry has been selected as the primary method of ascertaining what has transpired in the subsurface of the political system.

Further, methodologies employing process-tracing as well as selected elite interviews have been used to identify the actions or inactions that have taken place with the case.

Thomas A. Spragens offers a four step method for the use of political theory as a way to “understand a political situation that is causing real trouble and real pain to those caught in it” (Spragens 1976, 20). His four steps are: 1) the identification of a crisis and the perception of disorder, 2) diagnosis, 3) imaginative reconstruction, and 4) proscription of a remedy for the political ills that threaten the public (Spragens 1976). In the first step the identification of a crisis and the perception of disorder is established. Here the problems/crises in a political society are enumerated and examined in some depth. Once the symptoms of the disorder have been identified it is then possible to move to the second stage in the model which is diagnosis. In this stage there is but one goal and that is to “discover *why* the unsatisfactory state of affairs [] has come about” (emphasis in original) (Spragens 1976, 46). When the causes of the political ills have been identified, Spragen’s methodology calls for the proper ordering of political society. More specifically this requires the political theorist to “look [] closely at the disorders and crises of the body politic, and then imagine [] what it would look like if these afflictions could be overcome” (Spragens 1976, 78); therein leading to the final step in the methodology that is the development and presentation of prescriptive recommendations grounded in facts. In this phase the goal is to move toward the implementation of those necessary and possible actions that will allow for the creation of a rightly ordered political society as described in the imaginative reconstruction phase of the model. This deployment of political theory as a problem-solving model creates an ideal model for the creation of the planned dissertation.

“Political theories are like pearls: they are not produced without an irritant” (Spragens 1976, 20). While at this point in the research it is difficult to point specifically to any one irritant or

triggering event it is anticipated that the county's ills are due in large part to urban sprawl, followed by lawsuits, mismanagement, corruption, and poor administration (Parsons 1995). In order to determine the precise actions and decisions that have transpired the following methodology is offered.

Methodology

This work examines the case of Jefferson County through the lens of a single-case study. George and Bennett suggest that “studies of single ‘deviant’ cases and of single cases where a variable is at an extreme value can be very useful for heuristic purposes of identifying new theoretical variables or postulating new causal mechanisms” (Bennett 2005, 81). Jefferson County certainly qualifies as a “deviant” case due to the extreme nature of several variables including the amount of the potential bankruptcy, the exorbitant fees extracted by investment bankers, the amount and number of bribes received by elected and non-elected officials as well as the ridiculous sewer rates which are being pilfered from the ratepayers of the county.

Accordingly, to reach a conclusion on exactly what has transpired during the decision-making process of the county commission it is necessary to examine the failures of the county as a case-study using a single-case inquiry. This type inquiry is consistent both with qualitative methodology generally and the Spragen's framework specifically. Robert Yin, a specialist in case study methodologies writes:

“The case study is preferred in examining contemporary events, but when the relevant behaviors cannot be manipulated. The case study relies on many of the same techniques as history, but it adds two sources of evidence not usually included in the historian's repertoire: direct observation of events being studied and interviews of the persons involved in the events. Again, although case studies and histories can overlap, the case study's unique strength is its ability to deal with a full variety of evidence—documents, artifacts, interviews, and observations—beyond what might be available in a conventional historical study” (Yin 2009, 11).

Further, O'Sullivan et. al. posit that "[c]ase studies are the preferred research strategy if one wants to learn the details about how something happened and why it may have happened" (O'Sullivan, Rassel and Berner 2002, 39). It should also be noted that "that the case-study researcher often has a clinician's interest in developing theories that are useful for making discriminating diagnoses"; thus, solidifying the usefulness of the case-study and within case-study methodology and pointing to a complementary methodology for the Spragen's framework of theory development (Alexander and McKeown 1985, 21). Again, this is precisely the intent of this study, to understand how and why Jefferson County has placed itself in the current situation. The case study inquiry is further refined by the use of process-tracing and elite interviews.

Process-tracing is a methodology that "takes the form of a detailed narrative or story presented in the form of a chronicle that purports to throw light on how an event came about" (Bennett 2005, 210). Thus making process-tracing an integral tool in attempting to ascertain how the crisis ensued which is the ultimate goal of both the method of process tracing, but also to the Spragen's framework, both of which lend themselves to the single-case study. "Process-tracing is an indispensable tool for theory testing and theory development not only because it generates numerous observations within a case, but because these observations must be linked in particular ways to constitute an explanation of the case. It is the very lack of independence among these observations that makes them a powerful tool for inference" (Bennett 2005, 207). One of the main proponents of using the process-tracing methodology within case studies has been George L. Alexander, a prominent scholar of international relations. In one work, with Timothy McKeown, he states "that historical arguments about causal processes in studies of human and organizational decision-making often involve a 'process-tracing' procedure []." The authors go

on to explain that the process-tracing “procedure is intended to investigate and explain the decision process by which various initial conditions are translated into outcomes. A process-tracing approach entails abandonment of the strategy of ‘black-boxing’ the decision process; instead, this decision-making process is the center of investigation” (Alexander and McKeown 1985, 35). It is anticipated that the tracing of activities (and processes) that have contributed to the existing Jefferson county debacle will lead to the ultimate decisions that have brought about the existing chaos and disorder. Furthermore, “[t]he process-tracing approach attempts to uncover what stimuli the actors attend to; the decision process that makes use of these stimuli to arrive at decisions; the actual behavior that then occurs; the effect of various institutional arrangements or attention, processing, and behavior” (Alexander and McKeown 1985, 35). Therefore, the tracing of various activities and processes should provide a detailed examination of both the processes and instrumental decisions that have brought us to the current stage in the development of this crisis. “It attempts to uncover the micro-foundations of individual behavior that connect hypothesized causes and outcomes and to reduce the difficulties associated with unobserved contextual variables” (Falleti 2006, 1). However, it is also a method that lends itself to iterative hypothesizing and testing as well as the generation of hypotheses.

By retracing the events of recent history that have brought the county to the near-bankrupt state, I posit that select informal groups have influenced and co-opted the decision making process of the county’s legislative body for their own ends. Further, I believe the following analysis demonstrates that the elected officials and administrators that have been part of the sewer project and financing formed their own informal groups (also known as regimes) or were assimilated into existing regimes that sought to influence decisions of the Commission to supplement their own private gains. The qualitative method of process-tracing makes this

analysis feasible. Since process-tracing does allow for several observations within the case, it certain dependent variables in the form of regimes and their subsequent actions should be seen to be having significant impact on the independent variable of decision-making. Environmental groups, departments of the county, bankers, sewer contractors, and ratepayers all formed regimes that moved the county's legislative body toward the aforementioned decisions. Again, through the process-tracing method, several observations of these activities should be readily evident

Yet, "process tracing is not a panacea, eliminating all need for tough, informed judgments on the part of the researcher (Checkel 2005). To complement and validate the findings of the process-tracing efforts this study also makes extensive use of archival documents such as newspaper and magazine articles, public documents and records, Securities and Exchange Commission (SEC) filings, and court documents. Fortunately "[t]he social nature of decision making implies that actors must communicate with one another in making decisions; that the content of this communication will reveal much about the attention focus, the decision rules, and the behavior of actors (even if it cannot be taken at face value); and that this communication is often accessible to researchers (Alexander and McKeown 1985, 37). Additionally, to ensure its effectiveness "[p]rocess-tracing requires data collection on key political decision-making and activity, often at the highest political level, and elite interviews will frequently be a critical strategy for obtaining this required information" (Tansey 2007, 767).

"Elite interviews can shed light on the hidden elements of political action that are not clear from an analysis of political outcomes or other primary sources" (Tansey 2007, 767). Manheim, et. al. explain further that elite interviews "are used, not to obtain precise measures of concepts for testing theories, but as a means of gaining *in depth understanding* of a phenomenon and discovering aspects of that phenomenon that you did not anticipate" (emphasis in original)

(Manheim, et al. 2005, 355). Interviews were conducted with officials directly involved with the decision making process along with other public administrators that have firsthand knowledge of the crisis as well as other private sector actors such as bankers and engineers that were heavily involved in the issues surrounding Jefferson County. The combination of using case-study inquiry combined with in-case process-tracing and elite interviewing allowed the most flexible path of research while continuing to maintain the integrity of the Spragen's framework.

Chapter Summary

Chapter 2 serves as the literature review and the backdrop to theory development. This chapter draws upon various political and economic thinkers such as Adam Smith, Alexander Hamilton, Albert Gallatin and moves forward in time to more modern thinkers in hopes of gaining insight as to how debt undertaken by a government should be utilized and disposed of. This chapter also serves as a primer on public debt and provides an understanding not only of how governments finance projects, but also why governments borrow money at all. In the case of Jefferson County, it was partially due to urban sprawl that forced the county (and other municipalities) to finance infrastructure activities that in turn led to environmental problem such as are described in Chapter 3.

Chapters 3-6 essentially serve as the diagnosis of the predicament with Chapter 3, dealing with the impetus behind the current problems, namely the lawsuit brought by the Kipp et. al.. However, before delving straight into the lawsuit and its effects, the chapter presents a brief case of the environmental impacts of sprawl and how this causes municipalities to finance infrastructure activities, thereby providing a tie-in to the literature review of the previous chapter. The chapter then provides the backdrop to the question of how the lawsuit came about, the rulings and the consequences of the consent decree which brought the suit to conclusion.

This leads to Chapter 4 which examines in detail Jefferson County's initial reaction to the lawsuit and consent decree with particular emphasis on the explosion of debt that Jefferson County borrowed to undertake the rehabilitation of the sewer systems it acquired. The chapter further details the mismanagement and initial issues of corruption. The chapter then treats the dual issues of rising program costs and the passing of these costs on to the ratepayers, thus setting the stage for Chapter 5.

Chapter 5 addresses the problems brought about by the increased rates and the subsequent refinancing activities which ultimately led to the downfall and near bankruptcy of the county. This chapter is perhaps the most complicated of the entire work as it deals almost exclusively with the derivatives, collateralized debt obligations, and swap options agreements. All of which the county used in an attempt to lower the finance costs associated with the sewer refurbishment, albeit without success. These complicated, yet widely used financing vehicles actually caused just the opposite effect in light of the macroeconomic factors that are discussed in the next chapter.

The subprime crisis that has caused widespread economic havoc across the globe also had a major impact on Jefferson County. Briefly, the county bet that interest rates would go up, thus they entered into swap agreements whereby if interest rates did increase then interest rates on their existing bonds would remain low. They bet wrong. The subprime mortgage crisis swept across the nation and in an effort to prop up the economy interest rates were lowered almost across the entire financial spectrum. When that happened it triggered increased rates for Jefferson County. I liken this to waking up one morning and discovering that your mortgage doubled--overnight. Chapter 6 treats this subject with some depth as at this point not only were elected officials to blame, but also this is where public administrators failed to provide the proper

advice and may have had their own conflicts of interest. This chapter also includes a section that details yet another blow to Jefferson County's financial status--the invalidation of a 1% occupational tax that was applied disproportionately across various occupations. A local group of attorney's filed suit and in 2009 the tax was invalidated by the Alabama Supreme Court. The tax issue has been lingering in the courts for years, but after the ruling the State Legislature was forced to enter into a special session to adopt a new tax, simply because home rule does not exist in Alabama.

Here Chapter 7 begins the ideal political environment and the imaginative reconstruction that Spragens calls for in his methodology. In this chapter, the ideal setting for political activity in Alabama at the municipal level will be contemplated. It is, by necessity, prescriptive. Through this chapter I seek to inform how best to achieve solutions to the problems set forth in the previous chapters.

Chapter 8 is the conclusion and final thoughts. While it is my conclusion, unfortunately I feel that Jefferson County will long be a topic of public administration and policy. This will be for its policies regarding public finance, but also as an indictment against bribery, corruption, and a failed legislative body. However, the public are always the penultimate suffers when both governments and markets fail. Here the failures have collided, but the business of the world continues. The aftermath of this debacle will be felt for some time to come, but it is my earnest hope that this dissertation cuts through the fray to develop some understanding of why these events have befallen the Birmingham Region.

Before delving too deep into the intricacies of the county's woes it is necessary to briefly examine the nature of public debts and provide an overview of how and why governments choose to employ debt as a method of financing various projects. After this short overview of

governmental debt the next chapter looks even further back in time and examine what those political-economic scholars and practitioners of public finance thought and did in the wake of the financial crises of their times.

CHAPTER 2

Literature Review and Theory Development

Introduction

Public finance is not only about the economic activities of a particular jurisdiction or political body. Public finance is more about politics and politicians. It is my intent in the next few pages to demonstrate that throughout the history of the world in general and specifically in the United States that the financial wheel that runs our government is turned by the actors involved and not always about the monetary aspects.

In the following pages, I will provide a brief overview of municipal debt and the activities associated with financing projects. In addition, this review will seek to provide the historical background which has informed and formulated policy and policy-makers during very tenuous times. However, it would do the reader well to bear in mind that the overarching theme from the time of Adam Smith to present day is the presence and effect of the political sphere. This is more clearly seen in the latter years covered by this literature review, especially in the areas of growth and regime theory. It is these theories that build upon one another that have illuminated the methods and rationale of Jefferson County's financial transactions. The political will completely dominated the public finance arena. Economic factors largely played no part in any decision-making; an argument that is supported by the following theories presented. However, first it is necessary to briefly explore the methods of municipal finance.

Overview of Municipal Debt

“The flow and management of funds is the lifeblood of our system of public administration. No policy, however farsighted, no system of administrative performance, however well crafted, can function unless it is associated with the flow of funds that will make it possible” (Shafritz and Russell 2002, 429). The use of public dollars for policy purposes should be of utmost importance to the citizens of a government, although all too often we pay no heed until a crisis looms large on the horizon. In typical crisis fashion, rarely is just one aspect of a financial crunch isolated; rather, financial crises cause ripple effects throughout the economic and political spheres. Governments should invest wisely in projects governed by policies that support the wellbeing and quality of life its citizens; or more specifically “[t]he goal of public finance [] is, ideally, to bring about maximum social welfare” (Borna and Mantripragada 1989, 35).

Governments have a variety of methods they utilize to provide the various services and projects that are now considered required of most municipalities. Most expenditures of local governments fall into one of two categories, operating expenses or capital expenses. Operating expenses are typically those budgeted items that are utilized for maintaining an entity’s day-to-day operations. Conversely, most capital expenditures are for fixed-assets which can be utilized for much longer periods of time. These fixed assets are typically paid through two methods; the first is pay-as-you-go which is just as it sounds where the entity finances a project through its own cash flows and any reinvestments of earnings that may be derived from the project itself. The second method employed is the use of bonds. “Governments and corporations borrow money by selling bonds to investors. The money they collect when the bond is issued, or sold to the public, is the amount of the loan. In return, they agree to make specified loan payments to

the bondholders who are the lenders” (Brealey, Myers and Marcus 2007, 118). In turn, as part of the loan restrictions, “most jurisdictions are prohibited from using the proceeds of long-term bond issues to finance current expenditures, [therefore] virtually all long-term debt financing is used to fund capital improvements” (Leonard 2004, 391). These borrowers must also repay the loans, plus interest and closing costs, as well as continue to pay for other operating costs through various revenue streams.

There are basically three ways that governments raise revenues: “taxation, borrowing, and printing of money” (Borna and Mantripragada 1989, 36). For the purposes of studying the sub-national level the last one is not allowed by the U.S. Constitution leaving state and local jurisdictions to rely on taxation and debt as the primary methods to generate revenues. Although many politicians are reluctant to raise taxes as these decisions are widely scrutinized; while borrowing money is quite often done with little or no public knowledge. Even Thomas Jefferson, for whom Jefferson County is named, realized this. “In the long run, [Jefferson] proved quite prescient. An impecunious insolvent debtor most of his adult life, Jefferson knew the downside of debt from hard-lived personal experience. He also knew that most people in public office were politicians, not statesmen. They would, he realized, often find it easier to borrow than to raise taxes or slash expenditures” (R. E. Wright, *One Nation Under Debt: Jefferson, Hamilton and the History of What We Owe* 2008, 14). However, as time progressed and the role of cities changed, local jurisdictions provided additional services to its citizenry which gave rise to a fourth method of raising revenues: the user fee.

A local government may charge a fee for services, much like a business, as is the case with Jefferson County charging for sewer service. There are many examples of the user fees and their associated uses such as toll roads, water systems and the aforementioned sewer systems.

These user fees may then be used to borrow funds, generally in the form of revenue bonds or warrants. Robert Bland presents a very succinct definition of revenue bonds when he states:

“A revenue bond represents a limited pledge of revenue sources to the repayment of qualifying bonds. Usually, revenue bonds are used to finance a revenue producing project such as a public housing complex, public hospital, toll road, water or wastewater facilities and lines, or a parking garage. Only revenues earned from the project can be used to repay the bonds used to build the facility. The government does not pledge its full faith and credit to the repayment of these bonds, although it may subsidize the project with general tax revenues, especially during the development phase. Because of the more limited pledge, voter approval is usually not required, and the bonds incur slightly higher interest rates because of the higher risk of default. However, investor can see a clear link between the use of the debt and the repayment of the bonds, which normally increases their confidence that the government will repay the debt” (Bland 2007, 171).

Many economists and politicians widely disagree over the proper role of debt in public sector uses. However, during the last century, local government borrowing has seen enormous growth. According to the Census of Governments for 1992 and 2002, local debts increased over 35% from 1992 to 2007 while all revenues combined equated to a rise of just 11% for the same period¹. Normally, these debts would be helpful if the proceeds were all to be used for investment in infrastructure (well planned, of course) or capital projects that governments will be able to finance over the useful life of the asset. However, many governments utilize the proceeds for a variety of other reasons, including financing current operating expenditures as well as to cover deficits that may exist from previous years or accounting periods. Shafritz and Russell point out that public debt “is also a tool notoriously open to abuse” (Shafritz and Russell 2002, 459). They further point out six categories of abuse:

“1) Borrowing to finance operating (or ‘recurrent’) expenditure, 2) Borrowing beyond the level of repayments the community can meet, 3) Borrowing under poorly structured contracts that

¹ From this point on I shall attempt (where applicable) to confine the discussion to local governments, but due to the federal system in the U.S., this may not always be possible.

leave the borrower no protection against large interest rate hikes by the lender 4) Borrowing to finance projects that give no return or are highly speculative, 5) Borrowing where government lacks the administrative capacity to manage or implement the projects without major losses and 6) Borrowing where there is widespread corruption and where a high proportion of the funds borrowed will be creamed off in payments to corrupt politicians and administrators, rather than applied to the purpose for which the funds were ostensibly borrowed” (Shafritz and Russell 2002, 459-460).

If the Shafritz and Russell assumptions are correct Jefferson County has apparently committed every category of abuse.

Jefferson County utilized revenue bonds quite extensively along with complex financing methods in order to reduce the amount of fees charged to sewer ratepayers, a topic we will visit in some depth in subsequent chapters. However, before entering into the specifics of Jefferson County’s ordeal it is necessary to gain an understanding of how debt affects government policy and ultimately the social welfare that public finance is supposed to assist in providing. By all accounts “[t]here seems to be general agreement that substantial [] public debt is a burden to society. The logic behind this view is that when [] debt becomes due, the payments are used by creditors to obtain goods and services which would have otherwise been at the disposal of members of the debtor” (Borna and Mantripragada 1989, 36). Herein lays one of the fundamental questions to which there is no single answer: should governments borrow money? This topic has been debated for ages and no end appears in sight, although an exploration of the arguments is certainly worthwhile.

Historical View of Debt Policies

As stated previously, the issues surrounding Jefferson County can and certainly are considered a financial crisis, however, much of the debate about debt policies have been brought about by various other crises. The nature and occurrence of economic and political crises is nothing new. In fact, even a cursory glance back in history demonstrates that these types of

failures happen with frightening regularity and that they are largely intertwined with one another. Since 1618, the developed economies of the world have experienced at least 46 distinct and separate financial crises (Kindleberger and Aliber 2005). On average this equates to some sort of financial crisis every 8.5 years. This is to say nothing of the political crises of the same period which are so often related to one another. Many of the great political economists developed their greatest works during or in direct response to the crises for which they were either victims or witnesses of. However, some of the following individuals may not altogether be thought of as theoreticians. They were administrators who both developed and/or implemented the theories that they have come to represent. The theories developed are less important than the actions they took to place whatever institution for whom they were working on the path to financial (and often national) security. The following will provide a brief review of the pertinent philosophers and the events surrounding these works. At the conclusion of this analysis, it should become evident that the debt policies of Jefferson County could have been prevented by developing alternative theories of public finance and actually responding to the crisis rather than seeking absolution in the courts or salvation from the state and federal governments. Kindleberger and Aliber begin their seminal work on financial crises in 1618, however, in an effort to maintain a focus on modern government theory and practice we shall begin our study in 1776 with that Scottish philosopher Adam Smith who was so influential to the founding generation.

This was the year the American Revolution began, but also the year that Smith's seminal work *An Inquiry into the Nature and Causes of the Wealth of Nations* (hereinafter *Wealth of Nations*) was published. Many have hailed Smith as the "father of economics" and while this may be subject to debate, Smith's impact on liberal capitalism and our modern society is not (Cropsey 1987). "Smith's contribution to economics[] has the character of a description and

advocacy of the system now called liberal capitalism; and the ligaments between the economic order and the political system, close under any circumstances, are exceptionally broad and strong in the world” (Cropsey 1987, 635). So strong in fact that volumes have been written about Smith and his writings. For our purposes the focus will remain on his writings specific to the public debt, Book V, Chapter III of the *Wealth of Nations*.

Smith’s discussion of the public debt focuses primarily upon debt at the national level; however that need not be a concern as the principles are entirely applicable to the sub-national and local levels as well. In his discussion of Great Britain’s mounting debt Smith comes to a swift and startling conclusion when he states: “When national debts have once been accumulated to a certain degree, there is scarce, I believe, a single instance of their having been fairly and completely paid. The liberation of the public revenue, if it has ever been brought about at all, has always been brought about by a bankruptcy; sometimes by an avowed one, but always by a real one, though frequently by a pretended payment” (Smith 1994, 1008). The pretended payment that Smith goes on to describe relates to national governments and their ability to deflate the currency and cause the cost of the debt to decrease. Smith alludes to several governments especially Rome that followed this practice, although this practice ultimately failed and thus left taxation as the only method of retiring the public debt. Since debasement of the currency is not an option for a local government, it stands to reason then that the only permissible method of repaying any form of debt is through taxation, realizing that this may result in the collection of user fees which in the broadest sense can also be construed as a tax. Therefore, it is reasonable to deduct that public debt cannot exceed the ability of a government to tax its populace. “It might perhaps be more proper to lighten, than to aggravate, the burden of those unfortunate countries, and to endeavor to draw a revenue from them, not by imposing new

taxes, but by preventing the embezzlement and misapplication of the greater part of those which they already pay” (Smith 1994, 1027). This would certainly alleviate at least a portion of the burden of county taxpayers.

Writing in 1776, Smith indicated that the period was one of turmoil. The American Revolution was beginning to get underway with the issuance of the Declaration of Independence and Britain would undergo major change as she fought wars on two fronts. These wars would rage for nearly a decade in the U.S. but the French conflict would last even longer. However, once the American Revolution was complete and the independence of the United States fully secured, the nation’s first administration assumed the task of building an economic system.

“The financial revolution was a really quick and neat accomplishment of the first Federal administration in the early 1790s. []. Politically it was quite controversial at the time, and reverberations from the 1790s debates over it have continued throughout U.S. history” (Sylla 2002, 283). No other founding figure has been at the center of more of this controversy (and others) than Alexander Hamilton, the first Secretary of the Treasury.

Hamilton experienced a very tumultuous childhood in the West Indies, but soon migrated to the New York. He attended King’s College, but soon quit to serve in the Continental Army. After securing a commission Hamilton served nearly six years as George Washington’s primary aide-de-camp. After earning glory at Yorktown, Lieutenant Colonel Hamilton traded his sword for the quill of a lawyer. Although cramming for the bar exam and passing it in record time, Hamilton was soon selected to represent his adopted state of New York in the Constitutional Convention in Philadelphia (Chernow 2004). It was here that he and Washington renewed their friendship that would stand the test of time even though at times the relationship was strained. What transpired during and after the Continental Convention would be instrumental to the

formation and economic prosperity of the fledgling United States; the completion of what would soon become the U.S. Constitution and *The Federalist*, a product of Hamilton's famous collaboration with James Madison and John Jay. *The Federalist's* "authors also looked beyond the immediate struggle [for ratification of the Constitution] and wrote with a view to influencing later generations by making their work the authoritative commentary on the meaning of the Constitution" (Diamond 1987, 659). Although for the purpose of understanding Hamilton's theoretical underpinning of public debt, one must turn to a much shorter work, *The First Report on Public Credit* submitted to the House of Representatives in 1790 during which time Hamilton served in Washington's cabinet as the first Secretary of the Treasury.

For political and ideological reasons (which often overlap) Hamilton has been much maligned for his views on public debt. It is largely accepted in historical and economic circles that Hamilton was completely in favor of plunging the U.S. headlong into debt. Much of this has come from his detractors such as the Republicans led by Jefferson and Madison, but as we shall see they adopted many of Hamilton's measures for their own ends. The animosity toward Hamilton springs largely from his willingness to borrow money during times of national emergency. More specifically, he states "the necessity for borrowing in particular emergencies cannot be doubted;" although in the same sentence he advocates that a nation "be able to borrow upon good terms" (Hamilton 1790). Therefore, "it is essential that the credit of a nation should be well established" (Hamilton 1790).

Further, Hamilton makes the argument in his report that a national debt will allow the U.S. to grow economically through three measures. The first is the belief that trade will be increased through the amount of capital available. Secondly, agriculture and manufacturing would be increased due to the availability of additional capital. Third, Hamilton argued that

interest rates would be lowered, again due to more capital being available at lower pricing. With such support it is easy to see why Hamilton would urge the newly formed federal government's assumption of state debts which had been incurred by the individual states to finance the Revolution. What Hamilton was attempting to do was make the U.S. creditworthy. This could only be done in his estimation by federalizing the debts and levying taxes and import duties to pay the principal and interest on the notes.

Here is the key in which Hamilton's theory of public finance turns. Hamilton laid out his philosophy eloquently when he stated:

Persuaded as the Secretary is, that the proper funding of the present debt, will render it a national blessing: Yet he is so far from acceding to the position, in the latitude in which it is sometimes laid down, that 'public debts are public benefits,' a position inviting to prodigality, and liable to dangerous abuse,--that he ardently wishes to see it incorporated, as a fundamental maxim, in the system of public credit of the United States, that the creation of debt should always be accompanied with the means of extinguishment. This he regards as the true secret for rendering public credit immortal" (Hamilton 1790).

From this statement it is difficult to see how any interpretation of Hamiltonian fiscal policy regarding the willful taking on of debt would be complete without including provisions for repayment of said debt. Through these repayments which must occur regularly are vital for entities to be "respected and trusted: while the reverse is the fate of those, who pursue an opposite conduct" (Hamilton 1790).

"When Hamilton left office in 1795, his adopted homeland harbored six critical institutional components that characterize modern financial systems: stable public finances and debt management; stable money; an effective central bank; a functioning banking system; active securities markets; and a growing number of business corporations, financial and non-financial" (Richard Sylla 2009, 62). These institutions, so vital to the economic boom the United States was experiencing, were not to continue without controversy.

When the Thomas Jefferson took the office of president in 1801, he moved quickly to name the one person who had a demonstrated an ability to match Alexander Hamilton's enormous reputation as a financier to be his Secretary of the Treasury, Albert Gallatin. Gallatin is one of the most influential figures of American History that scarcely anyone has heard of, although he was a public servant of enormous impact. As Wright and Cowen state, "he served his country for *over sixty years* (emphasis in original), held a leadership position in Congress, was a confidante of Thomas Jefferson in his successful bid for the presidency, served as the Jeffersonian's money man, holding the position of Secretary of the Treasury for over twelve years (twice as long as Hamilton)" (Wright and Cowen, *Financial Founding Fathers: the Men Who Made America Rich* 2006, 87).

Astonishingly, there are only three biographies of Albert Gallatin available. The most important (and most recent), for our purposes, is by Raymond Walters, Jr. entitled *Albert Gallatin: Jeffersonian Financier and Diplomat* written in 1957. Through this work and by examining Gallatin's original papers, it is quite easy to identify a man of completely different philosophy from Hamilton. According to Walters, Gallatin had always been opposed to the policies of public debt of the previous Federalist administration. Gallatin's express purpose for assuming his role at the treasury was to extinguish the public debt. A sample of his philosophy is in evidence when Gallatin wrote, "Almost all the expenses of government, but especially that species which most usually engenders a public debt...are a destruction of the capital employed to defray them" (Gallatin 1967, 32). From this it is easy to see that Gallatin would prefer not to have any debt at all, but he goes on to say, "[T]he only evil which arises from a habit of recurring loans is that, by facilitating the means of raising capital, it tends to enlarge the scale of expenses, it encourages unnecessary ones; it thus indirectly promotes a greater destruction of capital than

would have otherwise taken place” (Gallatin 1967, 33). As we shall see later, this perpetual need for growth to pay for debt is an unintended yet dangerous consequence of acquiring public debts. Although Gallatin was not immune to taking on debt as he was ultimately responsible for financing the Louisiana Purchase which more than doubled the size of the U.S. Evidently, some deals are in fact too good to pass up². It is important to note that the overall resources made available to the U.S. through the Purchase contained plenty to offset the debt acquired for the acquisition (i.e. the Port of New Orleans). This was a completely unforeseen event which does occur with frightening regularity; however, it is possible for many governments to be more prepared for growth (although perhaps not as large as the Louisiana Purchase!). This preparation for growth-related expenditures can be made much more evident in the form of an accurate budget. Thus we fast-forward to the mid-1960s.

Public Budgeting

In 1964 Aaron B. Wildavsky wrote one of the seminal works of public administration. In *The Politics of the Budgetary Process*, he takes us on a journey, not of the process of creating and administering a budget, but rather he pulls back the curtain on the political machinery that is American budgeting. Specifically, Wildavsky focuses upon budgeting at the federal level, although much of his work is readily transferable to the local and state levels. He defines “the federal budget [as] a representation in monetary terms of governmental activity” (Wildavsky 1964, 4). Budgets serve as a record of the winners in the struggle for governmental resources. “In the most integral sense the budget lies at the heart of the political process (Wildavsky 1964, 5). He also asserts that in order to understand the budget one must understand the environmental conditions under which it was created.

² The true irony of the Louisiana Purchase is that the U.S. borrowed money from Britain to buy the territory from France which needed the capital to fight Britain. France was ultimately defeated in 1815 at the Battle of Waterloo, but the economic strain on Britain due to the war would be felt for decades.

While there are numerous types of budgets, there are three major decisions on which to base the budget: 1) how much to ask for, 2) how much to recommend, and 3) how much to give. Budgeting is incremental as many programs and decisions are made years in advance and only this current year's portion is included in the budget. Therefore, only a small portion of any budget is actually capable of being allocated by the governing body. Budgets are typically compared with previous year's activities and it becomes important not to ask for too much or too little. According to Wildavsky, appropriations committees have become extremely suspicious of agencies that continually ask for large sums of money. However, if one asks for too little, then the request may never be made because it is simply too small to warrant the time and effort necessary to secure the funding.

"Padding" is also an issue with budgets; however as it is a dangerous tactic. If it is done without proper thought it can inflate budget requests. Conversely, if it is not done then one can find themselves in deep trouble without enough funding to cover all expenses. Padding must be done with prudence and within an acceptable framework. As we shall discover, padding becomes a major factor for agencies/departments that become captured by regimes.

Another tricky part of the budget process is actually the prior year spending. If an agency comes in under budget, then they have asked for too much; if it's over-budget, then they do not conserve, if it comes in on-budget then it's too convenient and the agency has not sought economical ways of providing service(s). This is very much a damned if you do, damned if you don't scenario, because rarely are performance evaluations done to justify any levels of funding.

The second decision-making process, how much to recommend, is very daunting indeed. In Jefferson County's case the finance office is by its very nature put into a very precarious position itself being an agency that reports to the Commission and attempts at some level to

maintain the programs desired, while at the same time being funded by the Commission. Wildavsky illustrates the difficulty of how much to recommend by using the example of the National Institutes of Health (NIH). He points out that instead of using NIH's numbers the formerly federal Bureau of the Budget (BoB) personnel used various "rules of thumb" to determine the increases NIH would have over the course of the next ten-years. These were not done in a systematic or quantitative manner, rather they were done "off the cuff", with BoB staffers knowing full well that Congress would more than likely raise the percentages recommended by the BoB. This type of event places any budget-recommending clearinghouse in a very tough situation, whereas they cannot reduce the funding request as it may support or reject any particular policy and may be deemed to have lost its objectivity. Although, for Jefferson County the financial office was indeed compromised, along with various other public officials involved in the budget related process, thus adding an additional variable which confounds the crisis even further. Yet as Wildavsky explains there are several strategies for maintaining an agency's base and to achieve their fair share.

First a definition of terms is in order. An agency's base is the budget amount that includes all of its necessary expenditures to provide an adequate level of service. In many, but not all cases, this is the previous year's budget amount, minus any special programs. The amount set aside (or requested) for special programs or projects is the fair share. This is typically the residual amount of the budget that is fought over by each agency and that has not been allocated yet. The major point here that Wildavsky makes is that it is vitally important to protect the base amount. This is done by utilizing various strategies.

Wildavsky's large number of interviews left him with one maxim on budgeting. "It's not what's in your estimates but how good a politician you are that matters" (Wildavsky 1964, 64).

This is further expounded as Wildavsky explains how to be a good politician. It “requires essentially three things: cultivation of an active clientele, the development of confidence among other government officials, and skill in following strategies that exploit one’s opportunities to the maximum. Doing good work is viewed as part of being a good politician” (Wildavsky 1964, 64-65).

The cultivation of clientele can certainly be a difficult one for certain agencies such as Jefferson County’s Information Technology and Planning Departments, although it is fairly easy for others such as such as Environmental Services (which is responsible for sewer service). In any event, it is vitally important to be able to prove that each agency is actually providing a useful service to either special groups such as industries or the public as a whole. However, as Wildavsky points out, agencies wishing to protect their base should avoid capture at all costs. Although Wildavsky’s study focuses primarily on the federal system, local jurisdictions are also subject to capture as well. The Environmental Service and Finance Departments as well as the County Commission as a whole became captured by the contractor and development communities. The development community used its influence to spur the County into placing its funds into projects that increased the land values of various land owners. This is not a new trend or new theory rather it the practice has occurred for centuries, but the articulated theory is fairly recent. The view of an urbanize area controlled by the development community is presented most clearly by Growth Machine Theory.

Growth Machine Theory

Growth Machine Theory was first articulated by Harvey Molotch in 1976. However, he more recently revisited the theory in a chapter entitled, *The City as a Growth Machine*, co-authored with John Logan. They argue that the primary function of a city (or urbanized area) is

growth. “[I]t is not the only function of local government, but it is the key one” (Logan and Molotch 1996, 301). The authors continue by asserting that growth of a municipality is promulgated by a few elite actors such as landowners and developers. While they also point out that there are various other actors such as the media, utilities and universities, who all benefit directly and indirectly from local growth, it is those that actually see a transfer in economic rents from the many to the few that benefit the most from pro-growth policies. They also argue that much of the growth rhetoric is aimed at the creation of jobs and the greatness of the community in order to generally sway the usually idle professional and working class that efforts are being made on their behalf to make the community a better place to live. While this statesman like approach is pleasing to the ear of most, in reality the goal is to utilize public policy to foster private development. Further the authors posit that it is those politicians that give into the will of the developer faction that provide fuel for the growth machine. This good will is typically bought either through legitimate or illegitimate means. Legitimate means would be through campaign contributions whereas illegitimate means equals graft and corruption, both of which shall be discussed in future chapters.

Robert Fitch, author of the *Assassination of New York*, is another strong proponent of Growth Machine Theory. In his highly entertaining (and rather colorful) book Fitch demonstrates that financial, insurance, and real estate (FIRE) interests pushed for the creation of a redevelopment planning process (during the mid-1960s) that would in essence de-industrialize the city. This was done in hopes of creating higher land values. Fitch states that there is a “1000 percent spread between rent received for factory space and the rent landlords get for class A office space. Simply by changing the land use, one’s capital could increase in value many times.” He further argues the large glut of office space in New York City was brought about by

this change in land use. Fitch points out in 1992 “a long-term U.S. bond yield[ed] something on the order of 6 percent. An increase, say to 10 percent could probably draw capital from the outer planets. Imagine the incentive for increasing income by a factor of ten” (Fitch 1993, xii). Accordingly, the potential for growth was a major factor for the elected officials of New York. There has always been a need for elected officials to point to construction and pat themselves on the back, because they like to show the constituents that they are working hard on their behalf “creating jobs”. However, in order to finance much of the construction New York began borrowing massive sums in order to finance the redevelopment plans as urged by the development community.

By 1975, the New York was on the verge of bankruptcy. The city, in order to circumvent constitutional limitations on borrowing created an array of political subdivisions that were invested with borrowing authority. Essentially, this had the effect of creating off-balance sheet financing for the City, a similar tactic used by banks as we shall see in a subsequent chapter. The number of entities created was a staggering 230, with the largest being the Urban Development Corporation (UDC) (Weikart 2009). The corporation “had more functions than a Swiss Army Knife” (Fitch 1993, xiii). UDC borrowed vast sums, cleared out wide-swaths of the city with eminent domain, overrode zoning laws, built thousands of units of upper-middle class housing...and simply collapsed. The UDC financed most of its projects through poorly managed bond issues. “Instead of issuing twenty bond issues for twenty projects, [the UDC] issued nonspecific, non-project bonds starting twenty projects using 10 percent of the bonds revenues as a fast start-up (Weikart 2009, 33)” The UDC was created in 1967 by Governor Rockefeller, a member of the landed gentry, and was bankrupt by 1974.

Vojnovic, another growth machine theorist succinctly states that “growth policies are not necessarily viewed as rational, but rather, the outcome of elite influences on local governments that might produce benefits for some but that might also impose heavy burdens on others” (Vojnovic 2003, 598). Essentially, this is a case of wealth redistribution, from the lower and middle class to the rich. It is a case that will be repeated in Jefferson County, where the development community encouraged the county to borrow large sums of money, so that additional infrastructure may be added to the deteriorating sewer system in a desire to improve their land values. This push for development was facilitated not only by the development community, but also those ancillary entities that stood to benefit such as engineering and design firms. These elites helped propel Jefferson County to the brink of bankruptcy, but just as in New York, the financial crisis was only created in part by the development community and growth theory. Weikart, quoted above, does not expressly blame the politicians and the developers; rather as a regime theorist she turns her attention to financial elites.

Regime Theory

Regime Theory originally began as a school of thought in international relations. Since its development it has found new life in urban political thought. Namely, it may be thought of a subsystem of growth machine theory, but where growth machine theory purports that local governments are governed by those in that benefit from growth, regime theory posits that local governments may have an informal power structure that provides governance to the jurisdiction. One of the most influential proponents of Urban Regime Theory has been Clarence Stone. In his landmark work, *Regime Politics: Governing Atlanta 1946-1988*, Stone provides the following definition: “An urban regime may thus be defined as the *informal arrangements by which public bodies and private interests function together in order to be able to make and carry out*

governing decisions” (emphasis in original) (Stone 1989, 6). As part of an informal structure Regime Theory is largely concerned with networks of power. Cox argues “[u]rban regime theory seems much more concerned with the bottom-up construction of networks of relations between local governments and private sector actors than with the top down imposition of norms or the provision of conditions for some normative convergence at the microlevel” (Cox 1996, 105). He goes on to argue that what makes regime theory so enthralling is that the networks present in the regimes all have similar (although not identical) goals for growth and in this specific instance, economic development. Cox states, “[l]ocal governments have major interests in local economic development. To secure their own respective tax bases, they have to attract in new investment in the form of real estate developments, corporate headquarters, branch plants, and the like. What local government has to offer is important to those same capitalist interests” (Cox 1996, 120).

Fainstein and Fainstein in *Restructuring the City* lay the ground work for regime theory. In this edited work, Fainstein and Fainstein describe how urbanized areas, particularly cities, but appropriate to urban counties as well, began to see a major decline during the post-World War II era. They assert that due to federal policies, urban areas gave way to the suburbs and therefore left the core or central city derelict. They attribute this decline to federal policies in transportation whereby federal funding up to 90% was made available to states and cities to implement road projects. This was a part of the legislation that created the federal interstate system, but it also had a direct impact on urban areas as those areas became the focus of most projects and city leaders welcomed it because of the new road’s ability to reduce congestion (albeit temporarily) as more and more families owned and utilized cars. The second set of legislative initiatives that had a major impact on urban areas was policies that dealt with housing.

While the housing literature is vast, it shall suffice to say that the federal government's policy of providing mortgage guarantees to banks and other institutions would lead directly to reduced risk for lenders and greater demand for housing by consumers. Thus, with the ability to move relatively quickly between where people lived and where people worked, the suburban areas became even more popular. Of course this policy of supporting homeownership did not cease, but rather became the foundation for later fiscal distress.

The third policy that Fainstein and Fainstein argue lead indirectly to sprawl was the urban renewal legislation of the 1970s. Again, urban renewal literature is vast and has been studied for the better part of thirty years; however, a quick overview is in order. Urban renewal was essentially aimed at redeveloping cities. In many cases funding became available to urban areas through the Community Development Block Grant program and others. However, as successful as some of the local implementation may have been, it should be noted that they often times only accomplished part of the goal. For instance, the authors point out that in some cases money was only available for demolition which left many vacant or rubble strewn lots in the urban core. This has a definite effect on the psyche of an urban area's populace. Thus, urban areas experienced a continual decline in the amount of intergovernmental transfers they received for redevelopment efforts. Therefore it became increasingly difficult to attract private investment into the downtown areas. In order to combat this effect many urban areas developed various incentives as a way to attract private capital. One such example is the tax increment financing district, where a portion of the yearly tax increment is set aside to be spent within the district for improvements such as sewer, water, and other infrastructure. These districts had and do have some effect in attracting private capital, however, the incentive offerings would only increase as time passed as competition for private investment intensified. "Although legitimized as adding to

employment and producing multiplier effects on general commerce, they tend to encapsulate their return, since gains are pledged either for debt service or reinvestment” (Fainstein and Fainstein 1986, 20).

Furthermore, regime theory indicates that just as with Wildavsky’s base budgeting a certain amount of public funds, as mentioned above, are fought over by the development community. This in turn creates a situation where the public is almost completely isolated from the decision-making process. “Since private interests are the principal forces in redevelopment, most decisions concerning the location and type of investment are not subject to popular approval. Even the election of ‘people’s candidates’ cannot change the dependence of public officials on private financial power—consequently the ‘governing coalition’ differs in composition from the electoral coalition” (Fainstein and Fainstein 1986, 22).

In the final chapter of *Restructuring the City* Fainstein and Fainstein describe their view of regime theory in even more detail. They argue that there are three types of regimes that govern cities. Those regime types are “directive, concessionary, and conserving” (Fainstein and Fainstein 1986, 251). The authors point out that each of these regime types had specific time periods in which they were active in local politics.

During the post WWII period directive regimes were the most common, and “operated with little effective opposition” (Fainstein and Fainstein 1986, 258). The hallmark characteristic of the directive regime is that these regimes had grandiose plans for the urban area, specifically, the Central Business Districts of metropolitan areas. This was an effort to revitalize these areas that had long been neglected with the federal funds that were beginning to flow to urban areas. Many of these projects were large in scale and were designed to restore the urban core to its glory days, no matter how erroneous this vision of the past may have been. Rather, what

transpired were effectively the beginnings of what would become deep class divisions between urban minorities and suburban whites. This gave rise to the concessionary regime type.

Because of the urban turmoil and uprising the 1960s and 1970s, many of the directive regimes had to rethink their goals of redevelopment for the sake of merely making the urban area attractive for investment. The authors largely dismiss this regime type save to say that the concessionary regimes of the time were still beholden to the interests of capital, but gave more than lip service to programs that provided services to the “underclasses” (Fainstein and Fainstein 1986, 259). The concessionary regimes were short lived and were eventually replaced by the conserving regimes which the authors contend existed from 1975-1981, but I believe that this regime(s) still exists today albeit with some modifications.

Fainstein and Fainstein’s work indicates that conserving regimes were “conserving in the senses of being politically conservative, of trying to preserve the fiscal stability of the local state given stagnation in the national economy, and of keeping political arrangements which maintained social control without costing capital very much” (Fainstein and Fainstein 1986, 259-260). The upheaval of the previous decade most likely put quite a scare into the regimes and some of that fear is still evident in the existing regimes. However, what all three regimes were sufficiently able to secure was the need of cities and urban areas to feel that they were now responsible for the accumulation of capital and investment to their locales. In *Restructuring the City*, the authors cite five case studies of major urban areas, they determine that “[i]n all five cases a symbiotic relationship developed between the mayor’s office and the business community, cemented on the one side by the city’s access to federal funding and on the other by the commitment of business to invest if redevelopment plans conformed to its perceptions of an appropriate strategy” (Fainstein and Fainstein 1986, 250). Over and over we will see the

business community which makes up a large portion of the regimes that so often effect policy decisions instrumental in directing the redevelopment efforts of the metropolitan areas. More importantly, these regimes were able to convince elected officials of urban areas that their continued investment in making areas prime for development was critical for the sustainability of the jurisdiction. This placed a major strain on the fiscal abilities of local governments particularly when the federal government discontinued many of the intergovernmental transfer programs previously designated for urban redevelopment. Therefore, urban areas were solely on their own and as we shall soon see this will leave them only recourse to taxes or the bond market for funds to support development and operations.

Both Growth Machine Theory and Regime Theory are important to the study and application of urban affairs; however both are lacking critical elements. While Growth Machine Theory examines the role of the development community and Regime Theory explores the cooperation of the informal power plays of the business elite, thus far in the research they have not been sufficiently explored to determine what happens when and if in fact the two theories intersect. While this is an area for possible future research it is beyond the scope of this study. For now the issue remains that a lack of leadership and a need for revenues became the driving force behind the decision-making of many local governments.

Once the federal and state governments reduced funding to urban areas as has been previously mentioned, these areas were required to continue their growth through debt financing. This left local governments vulnerable to the land-based economic factions, such as developers, that sought public sector financing for private development projects. Local governments sought growth; therefore in conjunction with the developers, or at their behest, cheap, outlying lands were developed by providing infrastructure to make areas enticing for economic development.

These improvements required financing, thus, local governments were placed at the mercy of the financial elites. When debts became due and difficult to pay (due to various reasons), the governments turned to growth, both land-based and in investments as a means to avoid raising taxes. This was precisely the case with Orange County, California in 1994. The issues in Jefferson County have largely been compared to the Orange County Bankruptcy. While the two issues do have their similarities there are stark differences too.

If Jefferson County declares bankruptcy, it will more than overshadow Orange County's infamous record of the largest municipal bankruptcy by more than double. In 1994, Orange County was forced to declare Chapter 9 when the county's pension system lost nearly \$1.7 billion dollars. Specifically the funds invested were from the Orange County Investment Pool (OCIP). It "amassed revenues from 187 public bodies, including cities and school districts, water authorities and sanitation districts" (Jorion 1995, 7). The pooled investments totaled approximately \$7.9 billion in 1994. The funds collected were then invested in various securities and were earning stunning returns for the pool participants. Jorian, a professor of finance states "the OCIP earned an average return on investment of 9.4% per annum. Even during the [early 1990s] recession, OCIP delivered yields of 8-9%, even though the California treasury averaged only 5-6%. This differential amounted to additional profits for the county of \$500 million in the period of 1991-93 alone" (Jorion 1995, 8). These were major returns for local jurisdictions which had recently seen major portions of state funding reduced. Many of these jurisdictions were using the investment income to fill the budget gaps they were experiencing.

Other jurisdictions saw the returns and decided to borrow money to invest in the OCIP. This is a very dangerous game, because at some point returns cannot remain what they were historically. To further complicate matters, the OCIP was using the borrowed funds to borrow

even more. In “1994 the size of the county pool had ballooned to \$20.6 billion” (Baldassare 1998, 2). The OCIP was borrowing “\$2 for every \$1 on deposit” (Baldassare 1998, 2). However, during this period the Federal Reserve kept raising interest rates in an effort to stave off inflation. This maneuver severely impacted the returns the OCIP was able to generate, thus investments in riskier and riskier financial products such as derivatives were undertaken in an effort to maintain the previous returns.

While much of this is somewhat similar to Jefferson County in that extreme amounts of money were borrowed and these were refinanced in an effort to lower costs through exotic financial instruments Jefferson County’s problems were exacerbated by factors of corruption. Most of Orange County’s problems were blamed on Robert Citron, the elected county treasurer. Citron had served as County Treasurer for over two decades and had worked his way up to that office as a staffer before standing for election. In the end however, Citron’s financing scheme was simply untenable. Citron essentially reported his financial dealings to no one, and not surprising as long as the returns were high, no one questioned his methods. Thus far the literature has no indications of fraud and or corruption, simply poor management of funds. This is the distinctive difference as we shall see with Jefferson County.

Although the OCIP could itself be thought of as a regime, and the investors need for income could qualify them as part of the growth machine, the two theories do not stand alone, as they are intertwined inextricably. Therefore, it seems that local governments are at the behest of developers, which represent the growth machine and the financiers, which represent regimes. This places local entities in a vulnerable position whereby the developers have worked to leverage public sector funds for the sake of raising the potential economic rent gain facilitated by the growth machine. The next step requires that the government finance the projects, or portions

of projects, because in nearly all instances the costs are not planned for nor are the local governments able to finance them out of pocket due to the overwhelming majority of public sector funds being earmarked for special purposes as Wildavsky argues. Thus the local governments are forced to acquire debt financing from the financial regime. This is also compounded by the idea that the financial regime seeks to acquire a larger share of the budget base for themselves. Eventually, the developers rise again to urge other projects to occur to grow the economic engine, but now the local government is caught in even more of a conundrum because they are squeezed between the developers and financiers, however, in most cases the developers are local and the financiers are distributed across the nation and now with electronic transfers, across the globe. However, the financial markets are not without their own recourse. “From a politician’s point of view, the bond market is powerful partly because it passes a daily judgment on the credibility of every government’s fiscal and monetary policies. But its real power lies in its ability to punish a government with higher borrowing costs. Even an upward move of half a percentage point can hurt a government that is running a deficit, adding higher debt service to its already high expenditures” (Ferguson 2009, 69). Therefore, local governments that take on extreme debts that they can ill afford for the sake of growth have a direct impact on what Smith called an implied bankruptcy which is the situation that Jefferson County currently finds itself in. These fiscal strains are all the more compounded when public officials forgo any exercise of leadership and ethics. When corruption and fraud are introduced into the equation, the political and financial landscapes become extremely murky.

In conclusion, it is intended that the evidence thus presented will affirm the theory I have regarding the notion that political and personal motives are the driving force in public finance and budgeting. However, what I hope is also clear is that governments that borrow too much

begin to transfer their ability to govern the political body away from duly elected representatives to other third parties such as the creditors, court appointed receivers, and judges. Unfortunately, all these have the effect of removing government away from the people. In the case of Jefferson County, the political arena was spoiled by corruption, greed, and a lack of proper planning for growth. These factors coupled with negligence have led directly to the county's demise as a body politic. As we progress now to the narrative section, bear in mind that behind every action is a group or person with an agenda that seeks to influence the political body in hopes of gaining a larger share of government coffers. If this were the only effect, it may be manageable, but as we shall see the body politic is compromised with its own agenda and thus its own needs for growth and financing.

CHAPTER 3

The Environmentalist's Lawsuit?

Sprawl

Sprawl has become a major topic of discussion in the community and transportation planning circles. Almost anyone that has had any interaction with a city has experienced the effects of sprawl. Congested highways, strip centers, vast parking areas are all components of cities and suburbs as they spread across the landscape. Many argue that the main cause of sprawl is the automobile.

Beginning after World War II, central cities began to lose population as more people decided to vacate the urban core and live instead in the suburbs that were absorbing the population losses of the city center. The flight to the suburbs “was heavily influenced by federal and state highway construction programs, national prosperity (which fostered extensive automobile and home ownership), and the [Federal Housing Administration] and [Veteran’s Administration] housing programs” (Gerckens 1988, 44). Thus the stage was set for cities and urban counties to expand, not necessarily in population, but in land size.

As these local government’s areas extended from the urban core to outlying areas the necessity to provide service to the citizens did not diminish. It only grew stronger. Local governments were now put in a position where they had to provide infrastructure for an increasingly dispersed population. This meant that miles and miles of sewer, water, gas, and

electrical lines had to be put in place to serve the suburbs. This expansion of infrastructure also includes an enormous number of roads that were put in service to move the people from their homes to their jobs. Naturally, this entire new infrastructure cost money. The costs of building, operating, and maintaining the infrastructure was exorbitant and most could not finance their needs from the existing tax base. This caused the governments to turn to the bond markets for financing and the implementation of user fees as a means to retire bond debts. This placed local governments again in the Growth-Debt Vulnerability cycle, whereby governments were required to grow spatially for the economic return needed to pay off incurred debts.

This pattern still exists today, but it continued almost unchecked from the mid-1940s to the 1970s when environmental concerns began to dominate the political landscape. The rise of the environmental movement put politicians in a unique position where they began to be forced to balance the economic needs of the city with the environmental needs of the citizenry. Even in situations where the city boundaries end, many situations have evolved where local governments are providing service to communities outside their jurisdictional limits. This has the dual complication of promoting sprawl and environmental pollution without planning or the ability to enforce planning or pollution related regulations.

The key piece of legislation which has been used to force both planning and enforcement of environmental pollution is the Federal Water Pollution Control Act, more commonly referred to as the Clean Water Act (CWA). “The objective of [the] Act is to restore and maintain the chemical, physical, and biological integrity of the Nation’s waters” (seq. 2002). Although as a report from the Cahaba River Society (CRS) argues the CWA has largely been a success this has not been the case within Jefferson County. The CRS asserts “not all the nation’s waters have

improved. Some have decline dramatically. In fact, the biological decline of the Cahaba [River] during this time has been far greater than recorded during any previous period” (Cahaba River Society 1993, 1). Part of the reason for this decline can be traced back to growth and sprawl of the Birmingham Region, which includes both Jefferson and Shelby Counties. From 1980 to 2005 Jefferson County has experienced a decrease in population while Shelby County experienced an increase of over 158% (Isom 2008). The vast majority of this population shift has occurred in an around the Cahaba River Watershed. As stated previously much of this growth required new infrastructure. However, the growth patterns were much dispersed thus requiring new infrastructure at the expense of maintaining existing systems. This had the effect of draining resources away from existing investments and created a situation where Jeffco’s sewer system could not cope with the increased capacity or the deteriorating conditions.

Jefferson County—Polluter!

The poor conditions of the sewer collection system caused much of the waste to pour into the Cahaba River and other ancillary streams and forks of the river. Specifically, the waste discussed “can include anything and everything that can be poured down a kitchen sink, flushed down a toilet, or discharged by and industry to a public sewer system” (Cahaba River Society 1993, 3). What made matters worse was the fact that many of the waste water treatment plants (WWTP) operated in and by Jeffco were already taxed beyond their capacity. This was intensified during period of heavy rains. When combined with “poorly constructed or maintained collection lines...large amounts of ground water [can] seep into the system” (Cahaba River Society 1993, 3). This is known as infiltration. Further, “[d]uring storms, ‘inflow’ of rainwater from numerous points can overload the systems even more” wreaking havoc on the sewer system and treatments of the waste (Cahaba River Society 1993, 3). Infiltration and inflow

are collectively referred to as I & I. Once I & I reach a certain level the collection system overwhelms the WWTPs and thus raw sewage or only barely treated sewage is discharged. In this case the discharge went directly into the Cahaba and her tributaries. The end result is Jeffco violated the Clean Water Act (CWA), specifically portions of the Act that deal with effluent limitations and the National Pollutant Discharge Elimination System (NPDES).

According to the CWA, effluent limitations are defined as “any restriction established by a State or the [EPA] Administrator on quantities, rates, and concentrations of chemical, physical, biological, and other constituents which are discharged from point sources into navigable waters, the waters of the contiguous zone, or the ocean, including schedules of compliance” (Environmental Protection Agency 2002) . The Cahaba and her tributaries are considered navigable waters of the U.S., thus EPA and the federal courts have jurisdiction over the river. In addition, the NPDES section of the CWA allows each State to set up its own permitting process for the monitoring of point source pollution in accordance with the CWA. The State of Alabama did so under the umbrella of the Alabama Department of Environmental Management (ADEM). Therefore Jeffco was required to meet the requirements of both the CWA through ADEM. They failed to do so.

Although Jeffco is not the only entity at fault, they did in fact neglect the environmental concerns of the Cahaba River for years. Part of the problem lies with how ADEM permitted the WWTPs throughout the County. First, the permits were designed to monitor the amount and type of treatment of water that actually made it into the plant. The Cahaba River Society’s 1993 report alleges this permitting tactic fell far short of the intent of the CWA since Jeffco staffers had deliberately built unpermitted discharge points whereby untreated sewage was placed directly in the river. Again according to the CRS, “[a]fter studying information on sewage

treatment plant bypasses and illegal discharges from sewer collection systems, [then] Jefferson County Commissioner Jim Gunter [] decided to do some research and field work of his own. Afterwards, having seen enough for himself to realize the immense scale of the problem he remarked: ‘Imagine my surprise when I learned that the biggest polluter in Jefferson County...is Jefferson County!’” (Cahaba River Society 1993, 11). Purposefully and willfully bypassing the treatment plants is illegal.

Jefferson County Sued by Slawson

Overloaded treatment plants, poorly constructed and maintained collection lines, and illegal bypass systems combined with an expanding population created extreme environmental stress on the river. Portions of the Cahaba were (are) unsafe for recreation and for local flora and fauna. Nine native species of the Cahaba have been listed as endangered or threatened and the U.S. Fish and Wildlife Service had noted that sewage discharge was the major cause of these declining populations. According to the CRS, a grassroots organization, their complaints and desire for relief measures fell on deaf ears. However, in 1996 Bart Slawson on behalf of three local residents filed suit against Jeffco for violations of the CWA.

According to Slawson, Allen Kipp, a Scouter was taking a group of Scouts on a canoe trip in Moundville, AL (about 70 miles southwest of Birmingham), but every time his paddle hit a sandbar it literally stank. Kipp called Slawson, an environmental attorney who worked in the same law firm as Kipp’s wife, and said, “Bart, why is it every time I hit a sandbar in the Cahaba, my paddle smells like shit? (B. Bart Slawson 2010)” At that point Slawson wasn’t quite sure, but after investigating the situation some he discovered that Jeffco was bypassing its Waste Water Treatment Plants, placing untreated sewer discharge directly into the Cahaba River. Although, the CRS contends that Slawson knew of the Society’s attempts to work toward an

administrative remedy but that he decided to file suit himself when the CRS board decided not to retain him as counsel.

On November 29, 1993 Jefferson County was sued by Slawson on behalf of R. Alan Kipp, Jr., Edward Angwin and Betsy Angwin who, according to their complaint, “obtain their drinking water from the Cahaba River and enjoy canoeing, hiking, viewing the river and wildlife and other recreational pursuits involving the Cahaba and Black Warrior Rivers and land adjacent thereto” (Slawson 1993, 4). Further the complaint states the Angwin’s live and own property on the Cahaba River” and “[t]he state of the rivers directly affect the health, recreational, aesthetic and environmental interests of the plaintiffs” (Slawson 1993, 4). In the filing, the plaintiffs allege that Jeffco, violated 6 NPDES permits. Specifically the complaint contended that Jeffco illegally violated its permits through by allowing the bypass of raw sewage and semi-treated sewage to flow into the rivers at various treatment plants, along with “operating two unpermitted automatic discharges,” “failing or refusing” to prevent I & I, and provide for repairs to the sewer collection system (Slawson 1993, 1-2). The suit further alleged that Jeffco should be made to operate the treatment plants in accordance with existing permits and the county should cease and desist in using the unpermitted discharge facilities. The plaintiffs claim that each day the county operated these facilities in non-compliance with the permits constituted a separate violation of the CWA. They alleged that at the time of the filing approximately 4720 violations had occurred. At a fine of \$25,000 per day, the suit sought approximately \$118,000,000 in damages. They came to this number by declaring that Jeffco’s WWTPs violated the Clean Water Act every time it rained, which is an average of 21 times per year in Alabama. Apparently, Jeffco utilized clay pipe which may have been due to an old ordinance requirement. This clay pipe is subject to I & I and deterioration over time thus making the collection system extremely fragile.

ADEM had been warning the County about potential system failure for over 15-years, with the most recent warning to Jeffco coming in August of 1992. The 1992 letter contained a draft administrative order to Jeffco regarding the Leeds WWTP (which is upstream from the Cahaba River). The County, in particular Commissioner Chris McNair took issue with the draft order. In a 4-page September 11th response McNair intimated that no order was necessary since Jeffco had already embarked upon a process to rehabilitate and deal with the I & I from the Leeds WWTP. However, in this instance ADEM refused to back down and apparently issued a reply letter stating:

“Our normal procedure is to issue an Order requiring the Permittee to submit an engineering report and a compliance correction plan containing a compliance schedule. The Department then issue[s] another Order that implements the compliance schedule, establishes a date for compliance with NPDES permit limits, and provides interim effluent limits for use until the plant is upgraded, *thereby helping the plant to avoid future permit violations that could result in a citizen suit*” (R.Horn 1992) (emphasis mine).

To complicate matters Pat Byington the Executive Director of the Alabama Environmental Council and former ADEM Commissioner, stated that “ADEM had an unofficial policy of being light on the hammer with public agencies” (Byington 2010). When asked why this was, he replied that it was ADEM’s view that enforcing regulations and fines on public agencies ultimately hurt the public as they were the ones footing the bill. Slawson sees it differently in that he argues that ADEM was subject to agency capture by the engineers, but there is no evidence to support this allegation although, Beth Stewart, Executive Director of the Cahaba River Society viewed ADEM as “the enabler in a dysfunctional family” (Stewart 2010).

ADEM's policy of allowing its permittees to continually defer maintenance on sewer systems created and even fostered a situation in which the permittees were leaving themselves vulnerable to lawsuits. This also has the added effect of disguising the true costs of the infrastructure system as it lulls the governments into a false sense of security where they do not plan for upgrades and maintenance, much less any possible fines or fees associated with the repairs. This again is a lack of budgeting and capital planning on the part of jurisdictions as much as it is the fault of the enforcement arm of ADEM. This is analogous to buying a car at a set price, but then neglecting to include the cost of oil changes in the total cost of ownership. Keeping with the car analogy, what happened to Jeffco is that they purchased the car, didn't factor in the cost of the oil changes, but more importantly they did not change the oil (through pipe replacement and repair) which caused the entire engine to seize up thereby causing a major liability. Ironically, had someone been paying more attention and taken this matter more seriously the entire debacle could have been averted.

Once the notice to sue was filed, a sixty-day period exists for corrective action, Jeffco could have sought the administrative order referenced above from ADEM when it was suggested the plan implementing corrective actions could have short-circuited the lawsuit, thus causing Slawson's complaint to be dismissed. However, according to Slawson, Bill Slaughter, an attorney for Jeffco called the suit frivolous. Slawson thinks that his lack of notoriety in the legal world probably caused the County to ignore the original notice. This is probably why Slawson originally intended the CRS to be the plaintiff in the case, but they decided against it as the CRS was a fledgling organization barely five years old, and attempting to work with both the Chamber of Commerce and the Jeffco Commission in an effort to clean up the river. For years the CRS had examined the Cahaba River and collected samples, had them tested and worked

within the existing administrative structure in order to stop the drainage of raw sewage into the Cahaba. For this the CRS gets a bad rap. CRS may have eventually brought the lawsuit against Jeffco, but that was not their intent at the outset. Rather, it appears that a slow methodical approach to working with Jeffco was the preferred method of the CRS. Slawson stated that he felt like they joined the lawsuit “because they were shamed into it.”

Pat Byington offers a slightly different story regarding the CRS’s reasons for not suing initially. According to Byington the CRS was reticent to join the lawsuit for strategic issues. At the time, the CRS wanted to be considered a partner, or facilitator, of cleaning the river rather than a litigious organization. With Slawson’s filing the CRS was put in an untenable position. On one hand, they either joined the lawsuit and could be viewed as fighting for the river or not join and risk being viewed as completely weak on environmental enforcement. More probably is the assertion that the CRS saw the writing on the wall and decided to jump on board so as to possibly control, or at least affect, the outcome of the suit and more importantly to be at the table during settlement.

CRS’ board had declined Slawson’s request to sue on their behalf, instead seeing the train leave the station without them the CRS board did agree to have Bob Tate, an attorney with Burr, Forman, and at-that-time president of the CRS to serve as counsel for the Society and soon joined the Kipp v. Jefferson County matter as an intervenor. Apparently Mr. Tate did provide services pro bono, but eventually did get paid when Jeffco was required to pay attorney’s fees as part of the consent decree.

Judgment Levied

In an interesting legal move, Slawson did not request any discovery period, (although one was granted eventually), because he felt like he did not need it considering all the documents

presented in the original complaint were from Jeffco and they could not deny that the memorandums were indeed theirs. Thus Slawson moved for a Motion for Summary Judgement³, which was granted by Federal Judge Roy Guin⁴. This had the effect of saying that the facts of the case were clear enough to see that any jury would find that Jeffco was liable in the case, thus the remedy phase began which resulted in the Consent Decree of 1996.

³ According to conversations with an attorney not affiliated with this case summary judgments are very rare in Alabama.

⁴ It should be noted that the suit was originally filed by Slawson earlier in 1993, but when the case was handed to Judge James Hancock, a notably conservative judge, Slawson decided to pull the suit and refile at a later date, subsequently ending up with Judge Guin presiding.

CHAPTER 4

The Debt Explosion

The Consent Decree

Instead of a prolonged court battle Jefferson County (Jeffco) agreed with to a negotiated settlement. A consent decree was agreed upon and entered into the Federal Register in November of 1996 after nearly three years of negotiations. The decree itself was fairly straightforward, even if its impacts were not. Besides Jeffco being responsible for its own conduct, the consent decree required that Jeffco take on the additional burden of maintaining the sewer systems (collection systems) of twenty-one municipalities within the county. The options for municipalities were quite limited; either they allowed the county to take over their systems or they would no longer be allowed connections to the existing system. Although not part of the consent decree, it is no doubt likely that the thought of other suits being filed against the individual municipalities were almost a certainty. Therefore, it seems as if no one from the municipal side of the table had any angst about turning over their sewer systems to the county.

Besides the acquisition of the existing municipal sewer infrastructure, the consent decree also called for a three phased approach to remedy the failings of the system and end the pollution of the Cahaba. “Phase I [was to] consist of the development of a series of planning documents which [would] identify the scope, methodologies, time frame, and resources to be allocated by the County to evaluate the condition and capacity of the County Collection System” (United States District Court, Northern District of Alabama, Southern Division 1996, 20).

Throughout the three year development of the Consent Decree, the Environmental Protection Agency treated Jeffco with kid gloves. Slawson argues that this may have been because the EPA under the Clinton Administration did not want to be seen as imposing its will on a local government, or it may have been because of Commissioner McNair's image as a victim of the civil rights era⁵. In any event the Consent decree did contain a number of items that were required of the County to remedy the sewer system.

The initial steps Jeffco was required to undertake included preliminary planning subject to EPA concurrence. The Consent decree stated that such planning documents would be utilized to “identify the scope, methodologies, time frame, and resources to be allocated by the County to evaluate the condition and capacity of the County Collection System, indentify sources of I/I, and develop remedial measures” (United States District Court, Northen District of Alabama, Southern Division 1996, 20). Various and sundry other plans were required; however the most critical for this analysis was the Waste Treatment System Capital Improvement Plan (WTSCIP) (see appendix A for the full project listing from the WTSCIP).

The second phase of the remedies required by the decree was to “consist of analyses and reports undertaken and/or prepared by the County to determine the extent [of] rehabilitative needs and corrective actions necessary to meet the objectives of [the] Consent Decree *within* the County Collection System and the County's wastewater treatment plants” (United States District Court, Northen District of Alabama, Southern Division 1996, 21) (emphasis mine). As we shall soon see, this key word *within* was not strictly adhered to and thus led to the expansion of the sewer system without adequate justification. The end result of the Phase II stuides was to “be used to amend the principal Phase [I] planning document” the WTSCIP (United States District

⁵ Chris McNair's daughter Denise was killed in the infamous 16th Street Church Bombing.

Court, Northern District of Alabama, Southern Division 1996, 21). The third and final phase of the Consent Decree was the implementation of the WTSCIP.

The Consent Decree's stated intent was to require "only those waste treatment system capital improvements that have been determined to be necessary as a result of information and analyses developed during Phase II" (United States District Court, Northern District of Alabama, Southern Division 1996, 22-23). As clear cut as this statement may sound, the Consent Decree left a major loophole open for exploitation. Section G. 8. of the Decree states that the County may "make modifications to the WTSCIP for projects not necessarily covered by this Consent Decree" (United States District Court, Northern District of Alabama, Southern Division 1996, 45). This loophole allowed Jeffco to insert many additional projects not only into the WTSCIP, but also into the County's overall capital improvement plan. Slawson contends that this was done at the county's assistance for two reasons: 1) was for pork-barreling of projects and 2) so the county could claim emergency status and therefore circumvent the state-bid law. More colorfully, Slawson said that "an emergency is when you cut your leg and have to be taken to the hospital; a sewer treatment plant that has to be rebuilt in five years is not" (B. Bart Slawson 2010).

Realizing that the court may not prohibit the county from undertaking additional sewer projects, the county commission should have limited itself for the time being to those mandated requirements. This was not to be the case. In the County's 1997-1998 capital budget the entire list of 50 projects from the WTSCIP was included although there were 54 additional sewer-related projects included as well! More than double the projects required by the Consent Decree. What continually raises eyebrows about this entire debacle is the extent to which none of the budget or capital planning documents show hardly if any relationship to one another nor do they

relate to comments made by senior staffers of the county who were ultimately responsible for the production and implementation of these documents.

For example, the WTSCIP comments from EPA stated that costs should be included for the projects listed in the WTSCIP. Jefferson County responded that the Consent Decree did not require cost amounts to be included in the WTSCIP. While this may be true, it is exceedingly arrogant, not to mention a complete waste of time to not include cost estimates while compiling the plan. Further, Jeffco's capital budget summary for fiscal years 1997-2002 indicated that \$824,828,950 was programmed for sanitary sewer projects, while the actual plan itself totals 960,367,410 in sanitary sewer projects (see FY 1997-1998 budget, pages 299-310). This is an approximate difference of \$83 million⁶. The budget then goes on to state "[a]ll sanitary projects in FY 1999 and thereafter are unspecified but funding has been obtained for such project volumes" (Jefferson County, Alabama 1996, 302). Interestingly enough the previous page of the budget states that "additional debt service funding will not be required during the current fiscal year" (p. 301). From these statements one might be led to believe that Jeffco had either: a) already had enough cash on hand to deal with the projects outlined in the WTSCIP and the regular CIP or b) that the County had already borrowed an unspecified sum for unspecified projects. The record is not clear.

In February 1997, the *Bond Buyer*, a newspaper of public finance, stated that the system upgrade would cost \$1.5 billion. To make matters worse are comments made by Steve Saylor, then County Finance Director, who stated in the same article that "[w]e ran numbers and ran numbers and ran numbers until you could just not imagine" (Jefferson County, Ala., *Rolls Up Sleeves, Sells \$315 Million Issue* 1997). If that were so, why were these numbers not placed into

⁶ This number was calculated by removing the 1995 and 1996 actual numbers from the 1997-2002 estimates (see p. 302) in the budget summary and then subtracting the actual estimates included in the body of the budget (see p. 310).

the County's capital budget at the time of adoption or why was it not amended to reflect all the number crunching? Further, the same article indicates that Jefferson County on February 11, 1997 was selling \$315 million worth of bonds. This was in direct conflict with the adopted budget that stated no additional debt would be required that year. Realizing that budget projections change with events, these changes are highly unprecedented. To recap, there is an \$83 million dollar discrepancy in the budget itself, the projections suddenly shifted from a total of \$960 million to \$1.5 billion, and seemingly out of the blue, debt of \$315 million was required. This does not even take into account the fact over half of these projects were not required under the Consent Decree.

In a simple spreadsheet I took all the projects from the WTSCIP that were included within Jeffco's 1997-1998 CIP. Allowing that the projects were not categorized in any recognizable fashion and that the titles of the projects between the two documents were neither clear nor consistent, I have attempted to recreate a budget of the required consent decree items. This is exhibited in Table 1 below.

Table 1

Consent Decree Required Projects as Extrapolated from Jefferson County's 1997 CIP

Riverchase Pump Relocation	\$	3,594,314
Cahaba Lower Shades	\$	23,904,618
Patton Creek Interceptor	\$	29,989,086
Al Seier Road Pump Station	\$	10,015,143
Bluff Park Tunnel	\$	9,269,696
Turkey Creek Trunk Extension	\$	8,587,688
Pinson Trunk Extension	\$	1,538,888
Shades Creek Branch Trunk	\$	14,674,762
Trussville Industrial Park	\$	4,836,081
Rehap Infiltration/Inflow Management	\$	16,406,288
Misc. capped sewers	\$	1,255,913
Misc. assessment sewers	\$	1,001,923
Valley Wastewater Treatment Plant	\$	18,608,622
Village WWTP/Maint.	\$	18,624,989
Village WWTP/Peak Power	\$	1,543,287
Village Drying Beds	\$	5,746,048
Warrior WWTP	\$	1,294,109
Cahaba WWTP	\$	47,860,148
Trussville WWTP	\$	19,641,115
Leeds WWTP	\$	15,746,616
Prudes Creek WWTP	\$	1,024,250
Valley Wastewater Treatment Plant/Solids Handling	\$	3,580,682
Trussville Trunk	\$	5,117,686
Oxmoor Valley Trunk	\$	9,645,213
Sand Ridge	\$	1,627,073
Shannon Brick Trunk	\$	682,839
Pipe Shop Trunk	\$	176,509
Newfound Creek	\$	8,054,401
Greenleas Heights	\$	170,850
West Gardendale Trunk	\$	5,816,025
Black Creek Extension	\$	159,996
Tarrant Trunk	\$	1,089,127
Village Roberts Field	\$	18,209,727
Bham Airport/13th Ave Replacement	\$	259,943
13th Ave N Replacement	\$	655,980
West Ensley Trunk	\$	508,000
Bessemer Hospital Pump	\$	157,510
Shades Trunk Extension	\$	3,547,852
Turkey Creek	\$	122,515
Turkey Creek	\$	225,000

Turkey Creek Plant	\$	227,719
Emergency Repairs	\$	509,107
Misc.	\$	4,878,175
Comprehensive	\$	6,019,711
Unspecified Projects	\$	650,000,000
TOTAL	\$	976,605,224

As can be seen from the example (which is overly courteous to the County in terms of extrapolating the required projects) the total projects only amount to \$967 million, far short of the 1.5 billion asserted by Saylor. Further, a closer examination of the numbers reveals that nearly two-thirds of the cost of the required projects is contained in the unspecified projects category. When the \$650 million of unspecified projects listed above as a line item is subtracted and contingency plans left intact, the total for consent decree required projects is only \$326 million⁷!

Accordingly, the debt loads that Jefferson County began undertaking at this time were completely unjustified. The problem only gets worse in the coming years. Including interest charges⁸ the County's total debt service jumped from 1.3 billion in 1997 to \$6.7 billion by 2003.

A running total of debt service is detailed in Table 2

Fiscal Year	Amount of Outstanding Debt Service (Running Total)
1997	\$ 1,355,619,419
1998	\$ 1,315,869,848
1999	\$ 3,976,150,100
2001	\$ 4,572,767,084
2002	\$ 6,736,268,893
2003	\$ 6,745,072,066

⁷ The FY 1997 budget for Jeffco is completely unreliable as a management tool. The numbers in various locations do not match, projects for which there are no specifications nor revenues identified are included, and the budget in itself is difficult to read. This is true throughout the budget. I cannot determine whether this is deliberate or just poor budget practice. In any event, the budget is highly misleading and ultimately worthless.

⁸ Between 1999 and 2000 the County budget mysterious ceased a long-standing footnote that stated that assumed interest charges were 5% per year.

Source: (Jefferson County, Alabama 1996) (Jefferson County 1998) (Jefferson County 1999) (Jefferson County 2000) (Jefferson County 2001) (Jefferson County 2002) (Jefferson County 2003)

The ever increasing tally tells a very interesting story of the County's demise. Debt limits were skyrocketing when budgets were largely remaining stable. In essence due to a lack of communication between policy and practice, these debts consumed the county. As we shall soon see sewer rates were increased across the county in an effort to repay these debts. The County Commissioners began to be deluged with complaints from angry ratepayers demanding answers to why these costs were rising so quickly and so much.

Finally in 2002, the County Commission asked the same questions and commissioned a program review. This was mainly done at the behest of the aforementioned ratepayers who began complaining loudly about the continued increase in sewer rates. This report was performed by BE&K, an engineering firm, not associated with the sewer project. They in turn subcontracted with CH2M Hill, another engineering firm, Porter, White, and Company, a financial services firm, and the Public Affairs Research Council of Alabama (PARCA), a non-profit think-tank that specializes in public sector research, particularly in the areas of taxation and expenditures. The final report was not kind to the County

The most damning statement I've found thus far in the research comes from the BE&K report. "We found poor coordination between the ESD and Finance Department. It appears that ESD made spending decisions without meaningful budgets or controls, and Finance paid the bills and found the money. The working assumption appeared to have been that since the County was working under a CD, it should spend without consideration of ultimate limits" (BE & K 2003, 12-2). Therefore, there was an assumption that ESD had a blank check to spend unabated. This

was further compounded by the fact that ESD's CIP was completely void of any meaningful cost estimates related to the CD work or the unnecessary expansion work. No long-range financial planning was ever put in place to keep a check on these rising expenses. The only thing that brought the sewer system abuses to the forefront was the escalating sewer rates.

This represents an example of regime theory in action. As stated in the second chapter regime theory basically suggests that a group works to exercise influence on the political body and further its own agenda. Here both ESD and its contractors were aligned in regime and the finance department was at their mercy to comply and find the necessary funds. As we shall see, eventually the ratepayers form their own regime for actions. In addition, the final report cited numerous examples of poor management.

Since we are primarily focused on Jeffco's budget, for the moment, I will deal with the section of the report that is specific to budgeting and financial controls. In short, there was essentially no methodology for tracking costs associated with the program. "The County does not have a reporting system that is capable of tracking, reporting, and projecting accurate Program cost and progress" (BE & K 2003, 3-1). This lack of a county wide financial system is, according to the report, prone to error and discrepancies. The report further states that more than 500 instances of errors totaling over \$100 million were detected, although many of these were offset by other erroneous entries. Even more disturbing is the tone of the report that indicates no attempt to correct these abuses had occurred to date. Of further concern are the allegations that the Environmental Services Department (ESD) had no budget, just "an estimated cost of the known work" (BE & K 2003, 3-2). Budgets were developed after the bids came in for particular projects, and these bids became the budget. This constitutes a wholly ineffective way to budget a

project of this magnitude. Naturally, the management of the project was also a major cause for concern.

There is little evidence that any management of the sewer rehabilitation actually took place. Again the best source of information in this regard is the BE&K report. The report asserts that ESD had limited ability to undertake a project of this magnitude. Considering the ESD's past history of budgeting and scope of projects this argument holds true. Before the Consent Decree ESD's yearly capital budgets had been approximately \$35 million per year, however, the CD resulted in expenditures of over \$250 million per year. No additional staff was hired during this period of increased activity. Moreover, ESD contracted with mostly local firms that as previously mentioned did not have the expertise in projects of this size either.

BE&K represent that most projects of this size, such as the Atlanta CD that is a close comparable of Jeffco's, typically hire a program management firm that has expertise in large scale construction projects. This was apparently not considered by ESD, because it is reported that even if a program management firm were hired then ESD would continue to utilize local firms, thus creating a duplication of services. At first blush, it seems incredulous that a civil service department would have the gall to make such a brash statement, but in hindsight it is easy to see the amount of corruption that took place and to recognize that some (certainly not all) ESD personnel and commissioners were bought off by these local consultants. However, the fraud and corruption aspects of this situation cannot be ignored, especially in light of how much waste went into the management decisions of ESD and the eventually the Commission itself.

Corruption—Part I

Lambsdorff defines corruption as “the misuse of public power for private benefit. The term private benefit relates to receiving money or valuable assets, but it may also encompass

promises of increased power or status” (Lambsdorff 2007, 16). She also goes on to state that these private benefits may also be promises of future gifts for oneself or friends and family. As we will see this was certainly the case with this phase of the sewer scandal. There are other aspects of the situation which involved corruption, but these will be treated in the next chapter. For the moment we are primarily focused on the aspects of corruption that led to increased sewer costs, particularly in the construction phases.

Lambsdorff offers up several economic rationales for corruption, but rather than focus on those what is most important to this analysis is the end result. By contracting with only local firms ESD created an oligopoly and deprived itself of the advantages of a free market system. The creation of this oligopoly created a situation in which corrupt public and private officials could easy take advantage of each other’s positions and resources. The end result is that the corruption that took place cost the taxpayer an inordinate sum of money and cost the government the trust of the people.

Five firms have been the recipient of the majority of sewer work in the County until recently. Table 3 shows the list of firms and the funding they received due to no-bid professional services contracts.

Table 3: Contracted Firms and Award Amounts

Private Firms	Contract Amount Awarded (Totals)
U.S. Infrastructure	\$ 50,000,000
Civil Engineering Design Services	
Dougherty Engineering	\$ 11,400,000
Rast Construction	\$ 100,000,000
William Dawson (Dawson Engineering)	\$ 8,000,000
Roland Pugh Construction	\$ 178,000,000

Besides the fraud and corruption that took place, well documented by the media, the most egregious actions ESD committed took place inside the Commission chambers. ESD had absolutely no plan whatsoever for the actions it took to add additional projects to the CIP, which in reality was worthless. Finding 5-3 states that BE&K's "investigation has not revealed any specific criteria that the County has used for system expansion investments. The County does not appear to have put in place a formal approval and justification process for sewer expansion or, if one exists, to have shared the process with the ratepayers and taxpayers. All contracts are currently approved at the Commission meetings. However, neither the Commission nor the public sees the entire project, only the portion covered by the scope and cost of the bid for contractors. This approach does not allow anyone to identify the total cost and scope of a project" (BE & K 2003, 5-4,5). This is a case of incrementalism at its worst and certainly paved the way for ESD and the Commission to become complicit as a captured agency. The end result is that projects continued to be added without reason or justification. According to the Birmingham News, of \$876 million in sewer repairs "[a]bout \$315 million, 36 percent, went to initiatives not required by the court. Much of that money was used to build new lines and treatment services in growing and undeveloped areas" (Blackledge 2001). According to Jack Swann, the Director of ESD, the county decided to create additional capacity in an effort to get more ratepayers on the system. The Birmingham News quoted Swann as saying "[t]he economy of this county needs the expansion projects that we're building. I think we should be praised for that. We are good stewards of the public's money" (Blackledge 2001). Is that so?

In October of 2006, Swann was convicted on 18 counts of "conspiracy, bribery and mail fraud" (WSFA 2006). Most of the charges revolved around Swann accepting bribes and services from various contractors on the sewer project. He was ultimately sentenced to eight years in

prison, and a “fine of \$250,000 and \$355,533 in restitution” (Gordon 2010). Most of Swann’s kickbacks came in the form of renovations to his home. While living next door he would even come over and supervise the work being performed by the same contractors performing work on Jeffco sewers. Figures 4.3 and 4.4 are before and after photos of his home from the appellate decision in his fraud trial.

Figure 1—Home of Jack Swann Before Renovations



Figure 2—Home of Jack Swann After Renovations



Photo credits: (U.S. v. Jack Swann Et. Al. 2009)

However, Swann was far from being the only culprit. Many others have pleaded or been found guilty of similar charges resulting from an FBI investigation which began in 2002.

The County Commission never fully engaged in the process of setting policy for the expansion. According to Gary White, the Commissioner who oversaw ESD beginning in 2003 (and Commission President at the time of the article) stated that “commissioners never officially adopted a strategy to step up expansion efforts” (Blackledge 2001). Even he did not realize that this was the largest public works project in the history of the state and he admitted that he was completely unaware that the expansions he was voting on was the most aggressive ever undertaken by the county. However, he was not alone. White’s fellow Commissioner Chris McNair stated that he was “not disturbed by what we’re doing. I’m very proud and very optimistic about what we’re doing because we’re planning for the future of the county”

(Blackledge 2001). Apparently they were planning for failure, because according to their own words there was no planning.

This lack of planning, in my opinion contributed greatly to the ability of the engineering firms to affect the growth policies of the county. These engineering firms constitute both an integral part of the growth machine as well as a regime. These firms exhibited great control over ESD and the Commission. Much of this can be seen through the firms unsophisticated bribery techniques including remodeling of houses and landscaping being provided to Commissioners and Environmental Service Personnel.

Of the County Commissioners who have been demonstrated to be the most malleable to the growth regime Chris McNair stands out. As mentioned previously, McNair lost his daughter Denise in the infamous 16th Street bombings and due to this he became somewhat of a symbol (albeit possibly reluctantly) of civil rights. He had a long spotless career as a legislator until the sewer scandals erupted. In 2005 he was indicted on charges of bribery and conspiracy to commit bribery. Most of the indictment charged that he had received numerous favors and gifts from the contractors performing sewer work for the county. The Birmingham Post-Herald in a July 14, 2005 article valued the gifts (many of which were renovations to his photography studio) at \$194,623 and cash payments of \$55,000. By the time of the indictment McNair had been resigned from the County Commission (replaced by Small) for nearly four years. The estimates of how much the contractors received in actual work from the county according to one article are in the hundreds of millions of dollars (see Witt, 2005). As Bart Slawson said, “Who can hide landscaping? At least cash can be doled out on a piecemeal basis!” (B. Bart Slawson 2010). However, without a proper plan created by competent authorities and put in place by a Commission willing to oversee its implementation the situation was doomed from the start.

Throughout my research one thing has become abundantly clear. The Jefferson County Commission has delegated its authority (or simply chosen not to exercise it) on a great many occasions. As we have just seen letting ESD run rampant with new projects and scope creep continuously added to the financial burden of the county. However, in an effort to offset these rising costs, the solution apparently was to delegate even more authority to the County Finance Director. Thus again we see rise of an internal regime that would benefit greatly from increased growth as well as provide an opening for an external regime to benefit as well. As stated previously little of any of these events would have come to public notice without the massive increase in sewer rates and the outcry of the citizens.

Rate Increases

The rate increases have been enormous. In 1995 sewer rates were \$1.58 per 100 cubic feet of water. According to the Jefferson County Office of Sewer Service (formerly known as ESD) website rates are currently \$7.40 (effective 1/1/2008)! The average sewer bill in 1995 was \$13.43 per month; it is currently 62.90 (calculated from Birmingham News data). Between 2002 and 2003 alone the ratepayers of the county were hit with a 39% increase. How did this happen over such a short amount of time? The answer is surprisingly simple but with major repercussions. The County Commission entered into an Indenture agreement with bondholders that allowed the County Finance Director to automatically increase rates to cover debt service. Again, this is like giving a blank check tied to the people's bank account. A Bloomberg article from 2008 paints a very distinctive picture of just how the citizens of the county have been affected by this gross incompetence.

“As nighttime temperatures plunged in Birmingham, Alabama, last October, Dora Bonner had a choice: either pay the gas bill so she could heat the home she shares with four grandchildren, or send the Birmingham Water Works a \$250 check for her water and

sewer bill. Bonner, who is 73 and lives on Social Security, decided to keep the house from freezing. "I couldn't afford the water, so they shut it off," she says. Bonner's sewer bills have risen more than fourfold in the past decade" (Selway 2008).

This burden of extremely high rates for a basic necessity is unconscionable and could have been easily prevented with proper planning, attention to detail, and ethical government. However, due to the massive rate hikes the situation only continues to degenerate, because due to public outcry about the rates, the Commission resorted to very risky refinancing vehicles in an effort to control rates, thus opening the door for the aforementioned growth-driven regimes to enter into the fray and extract their pound of flesh from the taxpayer.

In conclusion, this chapter has detailed the fact that through poor management, corruption, fraud, deception, and lack of attention and planning have brought about a tremendous burden for the county. Over 6 billion dollars in debt were incurred from 1996-2003, sewer rates increased at an alarming rate considering the Consumer Price Index for the same timeframe actually decreased. Civil servants who were supposed good stewards of the public money took hundreds of thousands of dollars while giving millions to local contractor who were in no way capable of performing the work they were tasked with. Throughout all of this the County Commission just sat and did nothing until the citizens demanded action. The actions the Commission would take turned out to be just as horrendous as the problems they were meant to solve. However, one glaring piece of information must be restated. The County had absolutely no policy regarding the expansion of the sewer system, therefore the sewer system was expanded not in an effort to add more ratepayers to the system, which is a flawed argument in and of itself, but more so to enrich the pockets of the contractors and public officials at the expense of the citizens.

CHAPTER 5

Risky Refinancing

Looting Main Street?

I have had many conversations with fellow public administrators throughout the nation about the Jefferson County fiscal crisis. Many such as Dan Davenport, the Director of Public Works in Portland, Oregon has expressed his displeasure with the new financing requirements his city has had to undertake in order to obtain capital for pending sewer projects⁹. These requirements such as a sinking fund were put in place due to the fears that are so prevalent among the financial community brought about in large part by Jefferson County's mishandling of its projects and financing.

However, one misperception keeps coming to the forefront. Many are under the impression that Jeffco financial woes were brought about solely by the banking community. This myth has largely been propagated by a *Rolling Stone* article first published April 15, 2010. This article, written by Matt Taibbi, has often been cited by colleagues as gospel in the Jeffco crisis. Nothing could be further from the truth.

Taibbi argues that the banks, especially JP Morgan, committed "nomadic thievery" on Jeffco, but his analysis is lacking in several key points (Taibbi 2010, 6). Instead of focusing his lens on the corrupt political leaders and civil servants who created a breeding ground; a breeding

⁹ This information was based on an informal conversation Dan and I had while attending the Senior Executive in State and Local Government Program at Harvard University in June 2010.

ground in which the type of fraud and corruption the banks did perpetrate was able to thrive. He states:

“[T]he county decided to build an elaborate new sewer system with the help of out-of-state financial wizards with names like Bear Stearns, Lehman Brothers, Goldman Sachs and JP Morgan Chase. The result was a monstrous pile of borrowed money that the county used to build, in essence, the world’s grandest toilet—‘the Taj Mahal of sewer treatment plants’ is how one county worker put it. What happened here in Jefferson County would turn out to be the perfect metaphor for the peculiar alchemy of modern oligarchical capitalism: A mob of corrupt local officials and morally absent financier got together to build a giant device that converted human shit into billions of dollars of profit for Wall Street” (Taibbi 2010, 1).

As demonstrated in previous chapters there was absolutely no coordination between the County Finance department, Environmental Services, and the Commission. The entire sewer project was devoid of any policy setting, much less collaboration between the public officials and financial wizards to create a grand scheme of public works projects. Rather, the project suffered from compartmentalization whereby ESD operated without guidance from either the Commission or the Finance office, and where the Finance office in turn simply borrowed the money for the projects. Was this egregious and simply stupid, yes, but it cannot be laid solely at the feet of the banks. The rationale for setting aside blame from the banks is that public officials admittedly did not have a comprehensive policy for complying with the consent decree. The entire process was done on an ad hoc basis, one or two projects at a time. Budgets were lacking and as reported the Finance department simply “found the money”. There is reason to blame the banks for certain aspects of the crisis, but their actions intertwined with a very crucial player in the financial portion of the crisis, although we have not reached that part of the narrative just yet.

Further in Taibbi's article he attempts to chide conservatives by suggesting that "they" (whoever they are?) would "lay the blame for this entire mess as the feet of weepy, tree-hugging environmentalists (Taibbi 2010, 2)". Here again is a misstatement because he says the county was sued by the Cahaba River Society and the EPA. As this issue has been dealt with at length elsewhere suffice it to say that this is poor reporting of the facts since the CRS did not join the suit until they had no choice. The well intentioned citizens [who sued] he refers to in his article were not even part of the CRS. Thereto, it is impossible to lay the blame for this crisis on the environmentalists either, for even the county could not challenge the fact that the pollutants they were dumping in the Cahaba River were in fact illegal. Again, the county is at fault not the citizens, banks, or environmentalists.

At this point, Taibbi argues that the blame should be laid on the county because "the county commissioners signed a now-infamous consent decree agreeing not just to fix the leaky pipes but to eliminate *all* (emphasis in original) sewer overflows—a near-impossible standard that required the county to build the most elaborate, ecofriendly, expensive sewer system in the history of the universe" (Taibbi 2010, 2). He continues his rant by saying that construction of the "new" sewer system would be "like ordering a small town in Florida that gets a snowstorm once every five years to build a billion-dollar fleet of snowplows" (Taibbi 2010, 2). Those two previous statements are simply shoddy, irresponsible reporting by a sensation-seeking journalist. Specifically, the consent decree states "[t]he County may propose and obtain approval from the proper permitting authority for the handling of peak flows at its wastewater treatment plants" (United States District Court, Northern District of Alabama, Southern Division 1996, 60). This in no way, shape, form, or fashion requires the elimination of all overflows; what it does require is for the county to actually abide by state and federal laws that regulate such overflows, which

they were admittedly negligent in the past. Further, the consent decree does not contain *any* specific remedies for the construction of the sewer system. The entire project was developed by the county itself with approval and concurrence from EPA. As demonstrated earlier, the WTSCIP contained more than double the number of projects required by the consent decree and all of those were completely unrelated. Here again the culprit in the crisis is not the consent decree, the fault lies squarely with the county and its lack of policy setting. The creation of the elaborate sewer system was the design of the contractors and public officials who stood to gain the most from the expansion of the system under the guise of the consent decree. The consent decree evolved into a fear inducing document that became a convenient tool for various regimes to use as a means of dipping into the public coffers.

The consent decree did in fact allow other regimes to come to the table and here the banks did in fact make huge sums of money, but only because public officials allowed them to do so. Because the sewer rates were increasing at such a high rate, due to the county commission's ceding of authority to the Finance Director for rate setting in accordance with the debts undertaken, it became necessary to develop new ways of lowering the costs of the debt. Thus the county entered into a variety of refinancing methods that eventually backfired with horrendous consequences.

The big question remained: how do you refinance and lower the debt on billions of dollars' worth of sewer revenue bonds and how did it balloon to \$6.7 billion? Jeffco had apparently refinanced some of the bonds already, but for the most part the "debt was in pretty much vanilla types of municipal bonds that carried fixed interest rates" (Hansen, How debt became a crisis for Jeffco 2008). Subsequent refinancing would entail very exotic financing vehicles such as interest rate swaps and auction rate securities. Between 2002 and 2003 Jeffco

refinanced nearly all of its existing sewer debt into three bond issues that contained the swaps and auction rate securities. Seven bonds floated between 1997 and 2002 were issued for a total of \$2.8 billion. Everyone of these seven issues were fixed rates bonds, meaning no matter the market conditions, the rate the county would pay for the bonds would not change. However, these seven bond issues were refinanced into three large bond issues and one small (relatively) issue of \$41 million that remained fixed. Of all the debt incurred, this was the only remaining portion of the debt that was fixed. The three other bonds were issued in amounts totaling \$3.04 billion. Among those bonds there were a total of six embedded interest rate swaps. In addition there was another so-called “bullet bond”, which pays off in one lump sum issued with a swap for \$110 million. Therefore seven swaps (later revised to twelve) were attached to the refinanced bond issues that totaled \$3.15 billion dollars in debt, a far cry from the estimated \$356 million developed from the consent decree¹⁰.

It is necessary to pause in our narrative to review the intricacies of the municipal financial markets that Jeffco was an active participant. Specifically, it is necessary to define the interest rate swaps that became so prevalent in the county’s finances. PIMCO, a firm primary engaged in fixed income (bond) management defines “[a]n interest rate swap [as] an agreement between two parties to exchange one stream of interest payments for another, over a set period of time” (PIMCO 2008, 1). Often these swaps are known as derivatives because they *derive* from an existing contractual obligation. The swaps are quite common in the fixed income industry and are traded over-the-counter, although they are unregulated. At their core they are a method of exchanging a floating interest rate for a fixed rate or vice versa. The party receiving the fixed rate agrees to pay the counterparty a fixed rate typically to a bank. The bank then agrees to pay

¹⁰ For the most complete treatment of the actual bond issues and swap action see Jeff Hansen’s article in the March 9, 2008 Birmingham News. Graphics are included in the article and served as the basis for most of the section above.

the other counterparty a floating rate of interest based on a predetermined formula, usually the London Interbank Offering Rate (LIBOR) which is the rate at which highly rated banks lend money to each other. There are several types of LIBOR based on duration, but swaps are most commonly tied to the 1-day rate, which as the name suggests, changes every day.

Swaps are mainly used by investors and portfolio managers “to hedge, speculate, and manage risk” (PIMCO 2008, 1). Investment banks are usually the market-makers for swaps, but typically sell them to other investors seeking to manage their risk. They do this in order to take a fee for the original swap, but also to transfer the risk off of their books. As we will see in a future chapter, the transference of risk will become a major factor in the economic decline that wounded the county even further.

It was thought at the time of the swaps that they would save the taxpayers approximately “\$214 million in interest charges” (Braun 2005, 54). This was not to be the case, rather in light of the evidence that swaps had gone terribly wrong in other parts of the county such as New Jersey and California (Orange County specifically), Jeffco officials were determined to press on with the use of “financial weapons of mass destruction” (BBC 2003). Warren Buffet, the world preeminent investor and author of the quote above was speaking about derivatives. He elaborated by also saying that some of the derivative contracts were derived by “madmen” (BBC 2003). He had no idea how right he was because it was not just madmen that created them, but madmen also bought them.

Larry Langford, at the time of these swaps was president of the county commission. If ever a politician could be considered a madman, he may be next in line behind Huey Long. Langford has a very charismatic persona and as a former reporter is not shy about voicing his views on almost any subject whenever he has an audience. Before he was elected to the county

commission he was the mayor of Fairfield, Alabama a suburb just west of Birmingham. During his tenure there he cut his teeth in the world of municipal finance. Although this was not his first elected post it did bring him to prominence through his creation of Visionland, a theme park located in Bessemer, Alabama just west of Fairfield. The joke he always told was that Fairfield had the vision, but Bessemer had the land.

The Visionland project came to fruition through two important vehicles. The first was the state created entity named the West Jefferson County Amusement Park Authority. This authority was vested with the power to build and operate a theme park. Most notably the authority was given enabling legislation that allowed it to borrow money. However, the authority had no revenue streams, thus the second vehicle consisting of a consortium of municipalities were gathered together to help guarantee the bonds of the authority. The full scope of the project is beyond this analysis, so suffice it to say that nearly \$100 million in bonds were sold in order to fund the park. The park opened in 1998, but by 2000 the bonds had significantly lost value. After a few attempts to salvage the project, “[t]he park filed bankruptcy in 2002 and was sold for \$5 million” (Braun 2005, 56). As a foreshadow to his madman (and now felon) status, “VisionLand includes a brick bas-relief monument—paid for by taxpayers—of Langford with his arms resting on the shoulders of two children” (Braun 2005, 56)¹¹. However, the real issue here is not the waste at VisionLand, of which there was plenty, but the fact that the bonds for the project were obtained through “negotiated sales by Montgomery-based Blount, Parrish, & Co (Braun 2005, 56)”.

William Blount, former chair of the Alabama Democratic Party headed the firm and had always been associated with Jefferson County bond issues but really came to the forefront under Landford’s Commission presidency. “Blount Parrish received more than \$2.4 million in the

¹¹ Thankfully this was removed from the park before it was reopened as Alabama Adventures.

swap deals, payments that came from one of the counterparties, the investment bank Bear Stearns & Co [and] Bank of America” (Hansen and Velasco, Debt drama had key players 2008). Here again it was not only the fact that investment firms and consultants made tons of money in these deals, but it is the very fact that most of the bonds and swaps were conducted through the aforementioned “negotiated sales”.

Negotiated sales are no-bid contracts for borrowing money. While this is not an uncommon practice in municipal finance it is a prime example of what happens when patronage and the spoils systems rear their ugly heads. Jefferson County officials made exclusive arrangements with a handful of Wall Street firms led by JP Morgan Chase & Co” (Braun 2005, 52). Again, the banks are not completely at fault here as the responsibility for bidding any potential bond work lies with the County Commission itself. Instead the Commission chose to follow the path of good ole’ boy politics and selected financiers whom they liked based on what they could get from them. Such is the case of Bill Blount but also Charles LeCroy, whose career brought firms such as JP Morgan to the table.

Charles LeCroy, considered at one time to be one of the best in municipal finance once worked at Raymond James & Associates a Florida based investment firm. From this position he was able to work with Jefferson County and originally financed the sewer bonds. From 1997 to 1999 Raymond James underwrote approximately \$1.5 billion of the original sewer debt. “When LeCroy left Raymond James [in 1999] and went to JP Morgan Chase, the county’s debt work went with him. From March 2002 through August ’03, JP Morgan sold \$3.36 billion in sewer bonds and debt refinancing for the county. However, all of these were negotiated sales with no competitive process and no way to insure that the best possible prices and interest rates were being offered to the county.

JP Morgan did create a mess for itself and the county. Although, not all blame can be laid at JP Morgan's feet, they did have employees that committed serious crimes out of greed; however, unlike most firms they eventually did take efforts to rectify their actions¹². The fees that JP Morgan charged Jeffco for the swaps were enormous. The fees were completely outside the norm. Jeffco paid "19-20" basis points per dollar in fees on its swaps from 2002-04. In a competitive deal in New York that same year, by contrast, JP Morgan charged just a third of that rate—6 basis points—on a 311.7 million interest rate swap for the state's Local Government Assistance Corp." (Braun 2005, 59). Several other prominent scholars and financial practitioners agree that Jeffco overpaid.

Gary Gray, a professor of finance at Pennsylvania State University and "former managing director at New York-based E.F. Hutton Group and at Lehman Brothers, is the co-author of *Municipal Derivative Securities: Uses and Valuations* (Irwin Professional Publishing, 1994). He says a fair fee for swaps is 3 basis points, about one-sixth of what Jefferson County agreed to pay" (Braun 2005, 59). "Robert Lamb, a former banker at L.F. Rothschild in New York and founder of the financial adviser Lamont Financial Services Corp, [] says the highest 'reasonable fee' for Jefferson County would have been 15 basis points" (Braun 2005, 59). Robert Brooks a professor of finance at the University of Alabama: "who has taught classes on risk management and derivatives for more than 15 years" (Braun 2005, 59) and is a co-author of *Interest Rate Risk Management: The Banker's Guide to Using Futures, Options, Swaps, and Other Derivative Instruments* and has used Jefferson County as an example of how *not* to budget in his class since 1997, reported that "the average fee for an interest rate swap for more than 15-

¹² Shortly after Jamie Dimon came to the helm of JP Morgan he shut down their municipal derivatives market. See (Herman 2008) for more information.

years [in term length], says the average fee for an interest rate swap two years ago [2003] was 11 basis points, roughly half of what Jefferson County agreed to pay” (Braun 2005, 59).

However, Sayler contended at the time that the reason for the high cost of the swaps was due to the length of time involved, which for most of the swaps were 40-years. Brooks retorted, “[i]f it was really that much more expensive to do a 40-year deal, somebody in the food chain, some of these multimillion-dollar consultants should have pointed out, “Listen, you can save \$20 million by just doing a 20-year swap”” (Braun 2005, 59). And there were quite a few of those multimillion dollar consultants around too.

There have been so many firms and individuals that have been feeding at the government trough throughout this crisis that it is exceedingly difficult to keep track of the all. There are some though that have made exorbitant sums of money from Jeffco and for that reason alone they stand out.

As mentioned previously, Blount Parrish was a staple at the county courthouse and for their efforts was paid over \$2.4 million dollars just on the swaps alone. This does not take into consideration the fees they made from the bonds themselves. Other advisers on the swap financing were CDR, a California based firm later raided by the SEC, made \$2.2 million. Morgan Keegan who advised on the initial swaps under Gary White’s term as Commission President made \$1.3 million. It appears as if they were kicked to the curb soon after Langford took over as they only participated in one swap action. Haskell, Slaughter, a law firm which has been involved in Jeffco deals since the early 1980’s pocketed another \$1 million, again excluding fees for the original bond deals. The list goes on with bit players, but at the end of the day, the fees for issuing just the twelve swaps were over \$10.7 million. As recorded, many of these firms also participated in the bond refinancing themselves. Again, Haskell, Slaughter made

nearly \$2.1 million, the largest single fee recipient. In total, the fee for professionals, was over \$5.4 million during the 21-months of refinancing and swap actions.

The banks too took their pound of flesh for the swaps. It is estimated that JP Morgan Chase, Bear Stearns, Bank of America, Goldman Sachs, Lehman Brothers, and Rice Financial Products took in over \$100 million dollars in fees alone. Further, the total cost of issuing all debts not including swaps is estimated to be nearly \$60 million. Therefore for the refinancing and swaps the County spent approximately \$176 million in fees. Bloomberg reports that by competitively bidding the swaps alone may have saved over \$45 million for the taxpayers. So why with such staggering numbers would the county continue to rack up massive fees and take on variable rate debt that can change in a heartbeat? As always, Langford's comments on the matter are worth quoting at length:

Langford "says he doesn't think Jefferson County overpaid for the swaps. Even if it paid too much, the resulting savings were worth it." "You know, I get the impression that people think a bunch of rubes in Alabama shouldn't be smart enough to utilize these swaps," [a]nd let there be an understanding: As long as this is a legal instrument, and it drives down costs, if we have to do one tomorrow, I'll do it again" (Braun 2005, 59).

In hindsight, the County Commission and all the political cronies who profited from these nefarious deals were less than capable of making proper use of interest rate swaps. The amount of money pocketed by public and private officials is almost as staggering as the amounts they handed over to banks and counterparties. Here again represents the regimes discussed previously, seeking to influence the political process and in turn reap major profits from a lack of financial knowledge and corruption.

Some SEC officials have intimated that swaps and swap fees are simply a way of passing funds to public officials because they are not regulated; whereas bonds are highly regulated.

These swaps make it very convenient for cronies to pass funds to officials which is exactly what happened to Langford and others.

Corruption—Part II

In order for any regime outside the body politic to have any attempt at swaying legislative policies they must first find a method of influencing members of the body. This can be done in any number of honest and well intentioned ways. However, the financial regime as a whole used completely unsavory and not to mention illegal means of influencing members of the Jefferson County Commission. As we have seen from previous chapters this was not an unheard of practice before, but bribery and corruption continued unabated even after those who were accused during the construction phase were being investigated, taking plea deals, and found guilty.

The main culprits of the legislative body found guilty of various charges were Larry Langford, Gary White, and Mary Buckelew. Although of the three Langford certainly was the most involved in providing county money to his cronies in exchange for gifts of money and clothing. Unfortunately the story of his scandal is as tragic as it is unfathomable, of course I feel compelled to add that it is tragic for the taxpayer, not for Langford himself.

On October 22, 2009 Larry Langford was found guilty on all 60 counts of his federal indictment which charged him with “conspiracy, bribery, wire fraud, mail fraud, money laundering, and tax evasion” (Whitmire, *The Aftermath of Larry Langford* 2009, 8). “All told, Langford accepted \$236,000 in bribes from [Bill] Blount and [Al] LaPierre [a longtime Democratic lobbyist] the government says. In return, it says, he made sure Montgomery’s Blount Parrish & Co. investment bank was awarded more than \$7 million in fees for advising on the structure and public sale of the bonds that Jefferson County issued to raise money for sewer

repair and expansion” (Hubbard, Langford painted as villain, victim 2009, 6A). It is enough to say that Langford was completely in the wrong accepting bribes, but even worse was the egregious manner in which he accepted them.

According to numerous published accounts and testimony, Langford had an infatuation with clothing. His defense team tried to categorize it as an addiction. On many trips to New York, Langford and Blount would go shopping at high end boutiques. “Page after page of the indictment chronicles luxury shopping the authorities say benefited the mayor: a \$12,015 watch at Tourneau in New York on Nov. 9, 2004, paid for by Mr. Blount; \$895 at Salvatore Ferragamo two days earlier, also paid by Mr. Blount; \$4,250 at one of the mayor’s favorite stores, Remon’s in Birmingham” (Whitmire and Nossiter, Birmingham Mayor Accused of Trading County Deals for Cash and Clothes 2008).

Remon’s is an upscale men’s fashion store located in downtown Birmingham owned by Remon Danforth. He testified that Langford came into his store in 2005 accompanied by Blount and LaPierre. Remon further stated in court, Blount and Lapierre “said Larry Langford wants clothes and I should give him what he wants and that they would take care of it.’ In the end, he said the pair paid him almost \$55,000 for Langford’s clothing collection” (Hubbard, Langford painted as villain, victim 2009, 6A). Another local store, Gus Mayer, was also a frequent haunt of the well-clothed mayor. Again according to testimony in his trial by the chief financial officer of the company, Langford reportedly paid off a \$44,000 bill. That would not be so bad had the money (\$50,000) to pay the bill not come from LaPierre who had borrowed the money from then Colonial Bank¹³. LaPierre in turn repaid the loan with proceeds from Blount. Colonial Bank was a primary conduit for these activities because Blount was dating a loan officer from the Bank.

¹³ Colonial Bank failed as part of the subprime crisis. It’s assets were sold by the FDIC to BB&T.

Also, conveniently Milton McGregor, a long-time gambling advocate and owner of several dog-tracks in the state was a Colonial Board member. While it has never been substantiated there have been allegations of Langford receiving large payouts from gambling facilities owned by McGregor. These are just a portion of the items and money that Langford took illegally, but the prosecution in the case stated it best.

“During opening arguments, Rasmussen [Langford’s defense attorney] had stacked seven file boxes in front of the jury to represent the \$7 million Blount received in the scheme. Rasmussen then showed jurors a small box about large enough to hold a sleeve of business cards. That box represented Langford’s take. The defense used the proportion (or disproportion) between Langford’s \$235,000 and Blount’s \$7 million to argue that there had been no agreement. [The defense argued that Langford had no idea he was being bribed so the bribery was not “agreed upon”.]

Concluding the prosecution’s case, [George] Martin held another small box in front of the jury. It was about the same size as the box Rasmussen showed them the week before. He reminded the jury of Rasmussen’s boxes and Martin said he had known from the beginning of the trial what he would say to them in the end.

‘Langford isn’t supposed to have a box---at all,’ Martin said. ‘If he does, it’s dishonest’” (Whitmire, *The Aftermath of Larry Langford* 2009, 8).

The jury agreed with Martin. In less than two hours the jury returned from deliberations with guilty verdicts on all 60 counts. Someone even questioned whether the jury had enough time to read the entire indictment. In the end, it did not matter and Langford was facing up to 804 years in prison. Eventually he was sentenced to 15-years and \$241,000 in forfeiture. However, the never at a loss for words caricature of a mayor, stood on the courthouse steps afterward and basically said the entire drama surrounding him was race driven. While race issues continue to be a major part of life in Birmingham, Langford’s trial had absolutely nothing to do with race. This case had everything to do with greed and incompetence.

As an example of why this story has nothing to do with race look at Commissioner's Gary White and Mary Buckelew, both Caucasian. While writing this chapter, White has been sentenced to 10-years in federal prison and \$44,900 in fines and restitution for his role in the sewer scandal. Apparently he took cash from Sohan Singh the former owner of US Infrastructure allegedly for contractual work performed by White, but that was not a convincing argument. White remained defiant to the end insisting that he "'exercised very poor judgment' in letting Singh pay him in cash" (Falk 2010). No, actually poor judgment was letting Singh pay him at all. Just like Langford, he's not supposed to have a box. However, from personal experience, I am torn because when a local regional agency had financial issues and the CFO was accused of impropriety by his former employer, White was quick to call for a forensic audit of the organizations finances. Further he went to great lengths to get the audit paid for. These are not typical actions of the guilty. However, the jury has spoken and White has become the latest to fall in the scandal.

Mary Buckelew was by far the cheapest sell-out. For a pair of shoes and a spa treatment she was given on a trip to New York by bond underwriters she plead guilty to obstruction of justice and cooperated in the investigations of the sewer scandal. She was sentenced to probation and fined \$20,000.

Langford, Buckelew, and White were all elected officials, but did they act alone or did they have assistance from other non-elected officials? Many have often wondered why Sayler has never been charged with any wrongdoing. The answer to that is still unclear and may never be known. However, in the absence of formal charges, it should be noted that he did have a conflict of interest because at the time of the County's participation in the interest rate swaps, Sayler had set up or worked for another private firm offering financial advice to other local

government entities. One such entity was the Bessemer Industrial Development Board (IDB), which refinanced its portfolio of buildings it leased to businesses. The IDB had used conventional financing to obtain loans to construct these buildings and then lease them back to companies that located in the city. The rates they were charged varied with the timing of when the actual loan was originated. Saylor's firm proposed refinancing those loans with a larger bond issue from which some equity could be cashed out and used on other buildings. The IDB did this bringing their interest costs down to 4%. Unfortunately they did not stop there. They too took out an interest rate swap that eventually nearly brought the IDB to its knees early in 2009. Regions Bank which now owns Morgan-Keegan participated in the swap agreement. Since fees were being paid to the firm for which Saylor worked while he was an active participant in County finance deals certainly appears to be a conflict of interest, although to my knowledge no investigation has been performed on this aspect of the scandal, nor has it been mentioned in any coverage whatsoever. One could make the argument that Saylor was part of the growth-machine in that he potentially profited from financing any capital improvements he may have been party to.

It has been established that corruption certainly played a major part in the refinancing of the bonds Jeffco undertook for sewer repairs. It has also been argued that the banking regimes were integral in moving the county away from fixed rate bonds to variable rates. Although to this point we have been focused on the internal workings of Jeffco and its corrupt public officials. It is necessary to take a look at exactly how these bonds were structured because in the next chapter we shall see how external events played a hand in Jeffco's fate.

The way many of the new rates on the variable bonds were set was through auctions. The bonds sold in these auctions are known as auction-rate-securities (ARS). "Auction rate securities

are long term bonds whose interest rates reset typically every seven, 28 or 35 days at bidding run by dealers who are paid to run the sales” (Preston 2008, 3C). ARS have been highly utilized in the public finance markets since 2001. These attract high net worth investors or firms because of the highly liquid nature of the asset as well as the interest income stream that can change quite frequently. ARS sales are typically limited “[b]ecause ARS do not carry a “put” feature (which allows the bondholder to require the purchase of the bonds by the issuer or by a specified third party), they are very sensitive to changes in credit ratings and normally require the highest ratings (e.g. AAA/Aaa) to make them marketable. This is usually achieved with bond insurance (California Debt and Investment Advisory Commission 2004). Jefferson County had plenty of bond insurance provided by a relatively small number of firms for the amount of debt they were carrying. This would play a major role in confounding the situation. No one thought about the risks associated with these mono-line insurers. Of course why would they when the financial regimes and the public officials were all living high on the hog at the expense of the taxpayer.

Human interest stories abound about how the corruption and graft in Jefferson county has cost citizens not only their hard earned wages, but also their quality of life. Some do not even flush the toilet except every other day and we have already seen how one grandmother had to choose between heat in the winter and water. I certainly wish I could stop here and say this is as bad as it gets, but for all the incompetence and blatant stupidity in the county courthouse, I cannot. It only gets worse, however, this time not entirely due to the county commission but to the economy at large. What becomes known by names such as the Great Recession, the Subprime crisis, Too Big to Fail, and the Housing Bubble contributes greatly to the impact citizens of Jefferson County had to absorb.

The county’s lack of planning and complete lack of ethics created an environment that was not sustainable. Credit could not continue to be doled out to just anyone or any municipality unabated as it had since 2001. The massive amounts of credit that were in existence eventually had

to be called and someone had to pay. Investors finally got scared and needed cash. The only way to get it was to sell securities, thus a worldwide panic set in. Very few saw this momentous occasion coming, and no one at Jeffco ever thought the “good times” would end.

Jefferson County did not count on many things when they entered into the swap agreements, but the one overlooked aspect of the financing was that interest rates may possibly fall. Everyone has heard the old Benjamin Franklin quote about nothing is certain but death and taxes, well the corollary to that is that interest rates will always rise. Very few in the financial community and certainly no one at Jeffco had any idea that the economy was about to fall off of a cliff, taking hundreds of banks and millions of jobs in the process.

CHAPTER 6

Subprime Crisis Spillover

The Derivatives Market

In the early fall of 2008, all hell broke loose. The financial markets went into panic mode and not without reason. That September the collapse of the long-lived financial powerhouse that was Lehman Brothers¹⁴, an investment bank with an Alabama heritage, sounded the first of many alarms that all was not well in the economy. Hundreds of other banks would follow in the weeks and months ahead. For Jefferson County it was only the beginning of the worst of times.

Before diving too far into the melee that is the current economic crisis, let me state that this work is not intended to rehash the reasons or the outcomes of the recession. An entire cottage industry of books has appeared in recent years recalling in infinite detail every nuance that has led to our most recent economic climate. Some of the works are excellent; some simply come across as vindictive, especially since many authors were caught up in the aftermath. Here I shall only treat those issues that pertain to Jefferson County. The primary vehicles that caused the economic downturn and affected Jefferson County to the greatest degree were derivatives. However, not all of the derivatives that affected Jefferson County were the ones they issued or purchased, rather it was the entire market for them that mattered.

After 9/11 Alan Greenspan, then Chairman of the Federal Reserve, held interest rates at historic lows for an extended period. This caused the rates of return on many investments to

¹⁴ Technically Bear Stearns was the first investment bank to fail in March of that year, but Bear was bought up by JP Morgan for \$10.00 per share in a deal orchestrated by the Treasury Department and the Federal Reserve Bank of New York.

reach record lows as well. This combined with a “savings glut in Asia” created a situation in which many investors were looking for ways to maximize their returns since traditional investments were not yielding the returns sought after (Sorkin 2009, 4). Banks were all too willing to oblige, therefore many derivative investments based on mortgages were created and utilized to provide high rates of return with supposedly little risk. These instruments are referred to by many names such as Collateralized Debt Obligations, Mortgage Backed Securities and others, for simplicity I will refer to these derivatives as collateralized debt obligations (CDO) as this is the most generic term and broadest definition of the vehicle.

“Collateralized debt obligations, or CDOs, are created by banks that pool together otherwise unrelated debt-instruments, like bonds, and then sell shares of that pool to investors” (The New York Times 2010). CDOs can also be comprised of many of the same type of investments such as mortgages. The underlying securities (mortgages or bonds) are packaged together as one large bond and then sold to investors such as hedge funds, other banks, and investment firms. If they were sold intact the economic crisis may have turned out differently, but through the marvels of modern finance, these CDOs were sliced into various tranches. A tranche is a piece of the bond that represents a particular level of risk and return. For example, a high level tranche may have a portion of the riskiest mortgages that have a return in excess of 8 percent; whereas a low level may have the most secure mortgages (theoretically) with a return of around 4 percent. Other tranches ranged somewhere in between. The payments of the underlying securities were presented to the investor based on the class of tranche the firm held. It was traditionally assumed that mortgages were intrinsically safe, as the value of homes had not declined in over 70-years and they would continue to increase in value. Further, it was also assumed a homeowner would move heaven and earth to pay the mortgage before other bills.

Both of these turned out to be fallacies, but for the period between 2001 and 2007, the appetite for CDO's was voracious. The same was also generally true for CDO's based on corporate and municipal debt obligations.

In order for banks to generate the type of volume investors were demanding, it became necessary to generate loans of less than stellar quality, thus the birth of the subprime loan. In essence because there were not enough reputable borrowers, the banks seriously lowered the criteria for mortgages. "One cheeky lender went so far as to advertise what it dubbed its 'NINJA' loan -- NINJA standing for 'No Income, No Job and No Assets'" (Pearlstein 2007). These low lending standards gave rise to a plethora of new businesses that can be described as nothing more than mortgage factories. One such example was New Century, a mortgage originator located in California, arguably ground zero of the housing crisis. According to Lawrence McDonald, author and former vice-president at Lehman Brothers, "New Century was selling \$5 billion worth of mortgages every month" (McDonald and Patrick 2009, 183). Furthermore, New Century's deal flow was increasing over 100 percent each year between 2004 and 2007. However, one hiccup could have brought the firm down through the fact that by generating such a volume of mortgages and CDOs, supply could outstrip the demand by investors. \$5 billion a month in CDOs is a lot in any market.

Through the creation of CDOs subprime mortgages were repackaged and sold as triple A rated securities. How could you take risky loans and repackage them in a way they became a safe risk? The answer came in the aforementioned tranches where better loans were packaged with subprime loans to essentially form a blended risk. This was not done by examining each and every loan, but through mathematical modeling. The Risk Management Association Journal stated:

“The model[s] generate[] the number of defaulted loans/ bonds in a pool with the frequency of occurrences if loans/ bonds of the collateral are more or less homogeneous in probability of default [] and exposure, and if defaults of loans/bonds are independent events. For example, for a pool of 100 loans, the probability of only one loan default over the maturity is very low, and so is the probability that 99 loans will default. In reality, the underlying pools are not homogeneous, and there is a tendency for many loans to default at the same time (Young 2008).

The assumptions used by the modelers were completely in error. As described above, the individual behaviors supposed that homeowners would act in accord with traditional situations however, as rates began to reset on teaser loans (those loans with a low entry interest rate that skyrocket later on) thereby doubling and tripling what homeowners were paying on their mortgages, people began to take unprecedented actions. The most common action appears to be that many simply walked away from their homes and left the banks to pick up the pieces. Therefore major defaults began to take place undermining the safety of the tranches and CDOs in their entirety.

“By August 2007, however, the \$2 trillion subprime market had collapsed, unleashing a global contagion” (Sorkin 2009, 5). Many of the hedge funds lost investors huge amounts of money when no buyers could be found for the CDOs. Without any buyers, there was no way to accurately price them. These caused major problems for the banks as they could no longer off-load the CDOs they currently held or were obligated to that were already in the pipeline. The banks compounded the problems because many were holding CDOs off of their respective balance sheets in entities known as Structured Investment Vehicles or SIVs.

The reason for banks to hold these CDOs off their balance sheets is quite simple. It allowed the banks to skirt the Tier 1 capital requirements of the Basel II accords. These accords are a set of agreed upon rules that banks have agreed to follow to ensure liquidity. Part II of the Accords states “[t]he total capital ratio must be no lower than 8%” (Settlements 2004).

Basically this means that the bank must retain at least 8% of its assets based on weighted risk in cash. This is supposed to ensure the aforementioned liquidity. However, by carrying the CDOs off-balance sheet and by converting these subprime loans to AAA-rated bonds the value at risk (VaR) goes way down. It went so far down in fact that some highly leveraged banks had capital ratios in the neighborhood of 3%. Another highly damning facet of using off-balance sheet financing this way is that no one knows how much capital is truly at risk nor do they know how much exposure to events they actually have. Therefore, any risk mitigation strategy in that situation is worthless. Nor can a CEO, board member, or shareholder take any actions with any degree of certainty because by the very nature of the way CDOs were parked off-balance sheet the financial accounting records of any entity embroiled in the manner were flawed from the beginning. The banks were flying blind¹⁵.

The banks were not the only ones in that condition. Since the 1970s there were a group of so-called monoline insurers that offered insurance for government and municipal bonds, “but they had started to insure CDO notes in the 1990s” (Tett 2009, 127). Some in the financial services industry “had always been cynical about the monolines. They were very thinly capitalized for one thing. At some, the volume of assets they were insuring was 150 times larger than their underlying equity” (Tett 2009, 127). The reason they are called monolines is they basically only insure one particular type of risk and that is default on bond issues. These can come in the form of government issued bonds or bonds created through CDOs. However, this poses a sharp risk for the insurer because they do not have the breadth of customers needed to accurately assess risk nor do they have the offsetting types of risk on which they can charge premiums much like a Lloyds of London or Travelers. Therefore with the little capitalization

¹⁵ All but one; JP Morgan had never elected to use SIVs and/or off-balance sheet financing. This forthrightness and commitment to understanding where they were at any given moment is another reason I do not feel as if Jeffco were “fleeced” by JP Morgan.

that they do have it is not surprising that in the wake of even a small financial crisis that these firms would be wiped out.

There were traditionally only about three firms that held any market share in the municipal bond insurance sector. Those were AMBAC, MBIA, and FGIC. These firms used their insurance rating from firms such as Moody's, Standard & Poor's, and Fitch to assist municipalities get the best coupon rate for their bonds. The three monoline insurers were typically rated Aaa (Moody's) by the rating agencies and this high rating would be used to assist governments who perhaps did not have the confidence of the market to reach a level where investors felt more secure in their ability to repay the debt. In a sense this was like having your parents co-sign your first car note. Naturally, the insurers made a tidy sum from the municipalities that they helped insure. However, there is beginning to be a trend in the financial literature that examines if this type of insurance is not just essentially a corruption premium as it may be that the most corrupt governments have to use bond insurance in order to secure good interest rates. It remains to be seen, and may even be a moot point as most of the monoline insurers have gone under in the wake of the very large financial crises.

Of the Jefferson County bond issues, most all were insured by FGIC (Federal Guaranty Insurance Corporation). In February of 2008, FGIC was rated as below investment grade, a kinder sounding term for junk status. "Municipalities that relied on bond insurers for credit enhancement have been punished by the series of bond insurer downgrades due to their exposure to toxic assets. Downgrades led to an exodus of institutional investors from floating-rate financing such as variable-rate demand notes, and to the ultimate collapse of the auction-rate securities market, costing public authorities across the US heavily in restructuring, termination and penalty fees" (Haws 2009). This is precisely what happened to Jefferson County as capital

began to leave the market in droves in a flight to safety. It was not to be found in many places, but one place for certain it was not found was in auction-rate securities. These markets (or rather non-markets since there were no buyers) were absolutely brutal to the county. It is here that Jeffco's financial turmoil continues unabated, but plainly becomes unmanageable, if it weren't already.

Auction-Rate Securities

In early 2008, Jefferson County's ARS interest rates were approximately 2.98 percent. That rate went north very quickly. As soon as the investors sought cover for their capital the need for ARS went away and as stated there were no buyers. Normally, when there were no buyers for these securities, the banks that held the auctions would buy them and hold them until another auction was held. This was a tidy way of making sure the market stayed intact and neither borrower nor buyer was scathed to badly. This also allowed the banks to continue being a market-maker. Although as the over-leveraged banks began to realize that they had over extended their Tier-1 capital ratios they ceased putting money up for the auctions and the auctions started to fail and in a big way.

For Jefferson County and many other municipalities that had bought the latest Wall Street invention it was horrible news. In March of 2008, when Jeffco's ARS auctions failed, an automatic provision in the security allowed interest rates to jump from 2.98 percent to 10 percent overnight! In addition portions of the debt were accelerated from 40 years to 4. This meant that "interest on some of the \$3.2 billion in variable-rate debt it sold in 2002 and 2003 has climbed to 10 percent from 2.98 percent in January, according to Bloomberg data. That prompted Standard & Poor's to lower its credit ratings on the debt below investment grade, to CCC from A" (Marios 2008). Again this is junk status. At the time it was thought that "[t]he bonds, mostly auction-

rate, will be converted to fixed-rate because interest costs might otherwise double to more than \$250 million annually, according to county commission president Bettye Fine Collins. That would exceed the \$138 million in revenue the sewer system generates yearly". Standard and Poor's stated essentially the same thing a month earlier. A statement read: "The county can provide no assurance that net revenues from the sewer system will be sufficient to permit the county to meet the interest rate and amortization requirements of the liquidity facilities" (M. McDonald 2008). Considering the complete inconsistency of numbers that is bandied about with the sewer debt based on \$2.2 billion in ARS, the debt service over 30-years would be close to the \$250 million per year cited above (\$231 million to be precise, if the \$2.2 billion is correct which I highly doubt)¹⁶. However this would leave absolutely no cash flow for necessary repairs which would place Jeffco right back where it started from with a failed system polluting the rivers and streams and more importantly the potable water sources of the county. So what else could go wrong? Rest assured with Jefferson County no one asks that question because it can always be worse. This time would be no exception.

The Occupational Tax

The occupational tax issue has been a time bomb waiting to go off since the fuse was lit in 1967. The timing of its explosion could not have been worse if it had been planned. In 2009, at the height of Jefferson County's financial crisis, a judge nullified a county-wide occupational tax, thereby eliminating the third largest unrestricted revenue source. Depending on which source is referred to the range of the tax proceeds varies between \$67 to \$75 million dollars of revenue per year.

¹⁶ Also it should be taken into consideration that this is only a portion of the debt. There is still another billion (at least) not factored into the above calculations of debt service.

In 1967, the Alabama State Legislature granted any county over 500,000 in population to tax wages and business licenses. However, a taxing ordinance was not developed until 1987, “two decades later, when the commission was under a federal court order to build a new jail” (Velasco, Occupational tax turns 20, still a hot issue 2008, 4A). The commission believed that no other funding would be available to assist so they adopted the occupational tax and began collecting it January 1, 1988. However, from the original legislation in 1967, the tax was flawed. “Critics of the tax said it was fundamentally unfair. The 1967 law specifically exempted professionals such as doctors and engineers who already paid a state business license. That meant lawyers could avoid the tax, but their secretaries couldn’t; nor could judges. Fortune tellers were exempt; bank tellers weren’t. Private detectives were exempt; police detectives were not” (Velasco, Occupational tax turns 20, still a hot issue 2008, 4A). This type of discrepancy between those that paid, versus those that did not, was the cause of many lawsuits.

A full history of the occupational tax issue is outside the scope of this work, but there are important facets of the case that do impact subsequent conclusions and recommendations. Also, while not directly related to the sewer problems, the tax issue is a prime example of the county commission being hamstrung and manipulated by the state legislature and unable to control its own destiny even when the situation is dire.

In 1998, 10-years after the original tax was passed, a judge struck it down and ordered that it be rewritten to include any occupation in the county. This required the state legislature to rewrite the bill, but they came to an impasse with the commission when the legislature demanded the amount collected under the tax remain revenue neutral. This would have called for a slightly lower rate. The commission did not agree and introduced their own bill that eliminated the

exemptions and left the rate alone. This would have had the effect of dramatically raising revenues for the county. The legislature retaliated in force.

The commission's bill was killed and the legislature passed their own version lowering the rate, but applying it to all occupations. However, in passing the new tax, the legislature "earmarked \$29 million from the tax for 144 projects the legislators chose" (Velasco, Occupational tax turns 20, still a hot issue 2008, 4a). The commission decided not to actively pursue the projects of the legislators. Thus a showdown was in the offing. Jim Carns, then a legislator and as of this writing a sitting commissioner said, "I don't think the county commissioners then realized they were subject to the legislative body" (Velasco, Occupational tax turns 20, still a hot issue 2008, 4A). Eventually the bill was rewritten once again and this time included \$31 million dollars in special projects along with funding for a departmental operations facility sponsored by the Governor.

All of these bills were deemed unconstitutional in lawsuits and the county never collected the tax during those periods. In 2001 the original tax was upheld by the courts. However, in 2005 an unrelated court case put pressure back on the county whereby they might lose the tax revenues once again. Citing a case where the Alabama Supreme Court overturned a lower court's ruling that the judiciary cannot determine the rules of operation of the legislature a new lawsuit was filed against the occupation tax. This new suit contended that if a lower court judge had ruled in the same way of the Supreme Court the repeal of the occupational tax would have stood back in 2000. Attorneys argued that the repeal of the tax should be upheld and refunds made dating back to the date of repeal in 2000. In January of 2009, circuit court judge David Rains ruled in favor of the plaintiffs. The judge did allow the county to keep collecting the occupational and businesses license fees, "[b]ut he ordered the county to put that money in an

interest-bearing bank account and not spend it” (Velasco, Judge strikes down Jefferson County occupational tax, business license fees; collections to continue while county appeals 2009). However, the judge did not go so far as to order refunds which may total more than \$600 million. The decision was appealed by the commission.

The Alabama Supreme Court in August, 2009 upheld Judge Rains ruling and went further by reiterating the tax was repealed in 1999, therefore making refunds a requirement. Of course leave it to the state legislature to muddy the waters because during the same month a special session of the legislature was called in order to address the tax. What resulted was what the legislature had wanted nearly 10-years ago, namely a new tax at .045% that exempted no one, but did reduce the rate from .05%.

What happened next is an example of nothing more than a political power play where the only ones hurt were the employees of the county. Bettye Fine Collins, president of the commission said, “[t]he bill reduces the amount we collect. It’s going to be a new tax. So that means it can’t go into effect immediately. There are certain ordinances that have to be drafted and adopted” (B. Wright, Commission president calls occupational tax fix a "bad bill" 2009). She went further and said that the county would have to place 1,000 workers on unpaid administrative leave “until November when the new tax kicks in” (B. Wright, Commission president calls occupational tax fix a "bad bill" 2009). Sure enough in a true political maneuver over 1,000 workers were placed on leave until they were brought back later in the year. It is important to point out here that contrary to Matt Taibbi’s article that claimed the workers were placed on leave so that the banks could get paid; these lay-offs had absolutely nothing to do with the sewer crisis. The funds generated by the occupational tax are unrestricted, unlike the sewer revenues, and are used to fund the county’s general operations. Some estimates indicate the tax

accounts for somewhere between 12 and 25 percent of the general fund budget. Like most numbers at Jefferson County it is difficult, if not impossible to ascertain a true number.

The occupational tax lawsuit was, as stated, a long time coming, and its timing could not have been worse. It was akin to kicking someone when they are down, but the courts have no mercy for timing issues. They obviously run at their own pace. Of concern here is lack of coordination between the commission and the legislature. These two bodies were definitely at odds with each other and within a Dillon's rule state the legislature and the courts will normally always be triumphant. It may take years, but time works against the commission in almost every instance as they do not usually have the luxury of waiting for a solution to be handed to them, although it is very difficult to argue that the existing commission should be making *any* policies based on past performance. Commissioner Collins goes on to support above statement by claiming that you cannot "operate a county sans this amount of money. How can you grow the county? You certainly can't be providing incentives for the recruitment of businesses. (B. Wright, Commission president calls occupational tax fix a "bad bill" 2009)".

The idea that economic development stops because of a lack an occupational tax is to be completely ignorant of the needs of business and the process that drives economic development. The idea that the sewer system rates could be kept down through increased growth is also completely flawed. If the pain brought on by these fiscal issues is not felt entirely by the county and regions private citizens, but also by the business community as well. Stories of individuals dealing with the effects of the crisis have already been told and there are countless others not heard. These are a travesty and the citizens of the county deserve better. However, in all the discussions of solutions the one most keep coming back to is increased economic development,

but in the next chapter I will argue that this has been one of the most crippled victims of the crisis, corruption, incompetence and infighting we have experienced.

Before moving to the effects of the crisis and remedies it is necessary to examine the responses thus far to the crisis. Unfortunately, the reaction to the crisis has been nearly as dismal as the processes that brought Jeffco to this point. The current sitting commission, which is as of this writing lame duck, has done almost nothing substantial to rectify the crisis. Sewer rates have not been dropped, not plans to assist indigent ratepayer have been put into place, supposedly two plans have been developed by the private sector to alleviate the fiscal burdens, but neither of them have been released to public scrutiny because they allegedly contain sensitive negotiated settlements. In short, this commission has done absolutely nothing to assist itself or its citizens. Of any consequence has been actions by the Securities and Exchange Commission which sued JP Morgan, and they promptly settled by agreeing to “pay a penalty of \$25 million, make a payment of \$50 million to Jefferson County, and forfeit more than \$647 million in claimed termination fees” (Commission 2009). Jefferson County has launched some lawsuits against JP Morgan and the firms that insured the bonds such as FGIC, but this will take years to sort out. Additionally, I believe this will be hard cases to win considering the long track record of negotiated sales of bonds and the massive amounts of corruption the public officials have either plead or been found guilty of.

All in all the commission has done nothing. Instead of attempting to provide a stable and safe place in which to work, live and play the current regime has only sought out ways to avoid the catastrophic issues facing our region. I honestly believe that by avoiding the situation that they are indeed doing more harm than good, although based on their actions thus far I’m not sure they know what steps to take even begin to find a remedy. The county is faced with a long,

protracted recovery that has not even yet begun. Because of the inability of the county to pursue economic development the recovery effort will take even longer.

CHAPTER 7

After Effects and Reconstruction

Jefferson County: A Casualty of the New Civil War

Douglas Watson, in a book entitled *The New Civil War: Government Competition for Economic Development* stated:

“The battle in economic development is based not on national policy but on local competition. Because of the tremendous demographic shifts underway in this country—from Rust Belt to Sun Belt, from inner city to suburbs—there are winners and losers among the nation’s localities. Local officials are often judged on their ability to sustain or accelerate economic growth or to reverse misfortune in their economies. Certainly one of the events elected officials relish is the announcement of a major development that will create new jobs and taxes. As a result, there is strong competition among local governments in the area of economic development” (Watson 1995, 6).

Due to Jefferson County’s own self-inflicted wounds, the region is no longer able to compete for the new jobs and taxes Watson refers to. Rather, the county is only buoyed by the state of Alabama’s major efforts and successes in economic development. Jeffco has gone so far as to transfer its economic development activities to the Birmingham Business Alliance (BBA). The BBA was formed after a merger of the Birmingham Chamber of Commerce and the Metropolitan Development Board, a seven-county economic development recruiting organization. Since the merger BBA has had lack-luster support as they have been developing a new strategic plan since the merger nearly 18-months ago and they have already been through

one CEO and are currently looking for another via a national search. This search for a new CEO will be very much like recruiting new companies to the area because “the county’s image is being battered nationally as it fights to avoid bankruptcy” (DeButts, With incentives gone, Jeffco relying on BBA 2009, 18). From the business perspective, Ronnie Clayton, a professor of finance, “said businesses looking to relocate or establish branches will be skeptical of the county’s ability to fund public safety, education, and infrastructure. Employers seeking high quality of life for their employees might look elsewhere” (DeButts, With incentives gone, Jeffco relying on BBA 2009, 18). Jay Grinney CEO of HealthSouth, Corporation, also said “[i]f there is a state or community that is plagued by corruption and incompetence and fraud, it’s going to scare away potential businesses that might otherwise want to relocate” (DeButts, Out of the Sewer 2010, 6).

Besides being a drain on economic development, the black cloud that hangs over Jefferson County has also extended to the rest of the state. “Jefferson County’s unresolved debt problems are red flags for investors who might be eyeing municipal bonds from anywhere in Alabama” (DeButts, Out of the Sewer 2010, 6). There is a pervasive question that remains with Jeffco’s debt in limbo. What will the state do to assist the county? The short answer is probably nothing. There will certainly be no monetary assistance from the state. Only in some cases will oversight be increased thanks to a bill passed by the legislature in its last session that requires public hearings on any Jefferson County debt over \$5 million, but this is wishful thinking or window dressing at best. Public hearings draw few and there are probably fewer that would understand the type of financing that Jeffco undertook. It should also be noted that the bill only applied to Jefferson County and it is far from impossible from something of this magnitude happening elsewhere in the state. Cities actually have more authority than counties do in

Alabama, and there are some cities that could easily match Jefferson County's record of incompetence, fraud, and mismanagement.

There have also been discussions about setting up a board to provide oversight for municipal transactions, but this proposal has pros and cons as well. It would work well if it were set up and administered along the lines of the North Carolina Local Government Commission (LGC). The LGC is a state entity under the Treasurers' office that oversees finances and debt issuance of municipalities. The structure of the agency is composed of financial officials from the state along with governor appointed representatives. They have the responsibility for approving all local government debt issuance. "Prior to approval, sale, and delivery of all North Carolina local government general obligation bonds and notes, counseling and assistance is given to local units in determining the necessity of the project, the size of the issue, and the most expedient form of financing" (Treasurer n.d.). Additionally, "[a]fter bonds have been sold, debt records of principal and interest payments coming due in current and future years are maintained for the State and all local governments with the exception of certain State agencies and institutions" (Treasurer n.d.). Having a group of professionals that can assist with the oversight and coordination of debt issuance and management can certainly be a rich resource for those in local government.

One negative that can be thought of is similar to what occurred in New York after its financial crisis described earlier. A group of three non-elected individuals were organized into a committee that was required to sign-off on any debt issuance the city wanted to engage in. This essentially transferred the policy making from an elected body to a body that answers to no one and can circumvent the will of the public. The idea of a state entity for oversight, if properly constructed, could be a very beneficial to all local governments in that it could boost bond

ratings and possibly remove the need for insurance of which the usefulness is dubious at best. Further, by coordinating bond issues in a timely fashion, it may be possible to get better coupon rates which reduce the total debt burden on taxpayers, which should be the ultimate goal besides providing the services being funded by the debt.

While the development of an oversight board is a laudable goal it is closing the barn doors after the horses have run out. In order for Jefferson County to put its house in order and to have some semblance of the ideal political society there are three steps that should be undertaken. By striving toward an ideal it is anticipated that a restoration of credibility and viability to the county and region may begin. Of those steps, all are within the power of the county. The three steps are 1) completion of a full forensic audit of county finances, 2) the declaration of bankruptcy, and 3) the hiring of a county manager. These three suggestions for curing the ills of the body politic spring directly from the theories presented in Chapter 2, specifically regime theory.

The theoretical underpinning of these remedies lies in the suggestion that one possible way of combating the existing regime is by creating new regimes which have an ultimate goal of addressing the problems Jeffco currently faces. There is no certainty that new regimes will be instilled with positive ethical values or that new regimes will represent the interests of the public however, additional regimes may provide a check on the power of those regimes that seek to use the public coffers for private gain.

The new regimes may work in the much the same way as Hamilton, Madison, and Jay described the factions spread across the republic that would prevent any one faction from gaining a firm grasp on the power of the nation, or in this case the city. Competing regimes should be able to influence the political process and accompanying bodies in such a way that no actual

regime is able to gather the influence needed to direct the political body in any one direction for too long. Multiple, competing, regimes that struggle against each other may be able to cancel the effects of one another, if not in the short run, perhaps in the long run. This may enable policies that are detrimental to the public to be changed rather than continued unabated. However, the opposite can also be true in a case such as Jefferson County, where regimes exist with such strength that their influence may extend the life of such failed policies as has been evidenced in the previous chapters.

By completing a forensic audit of Jeffco, a regime will not be created, but those regimes that do exist and those that may be created all benefit from the audit tool. The rationale for this is that in an ideal local government, elected officials and public administrators would know reasonably their financial position. One way to accomplish this is through regular financial reporting; another is through an audit. Though the two are not mutually exclusive and should be used in conjunction with each other and in concert with the budget to determine the needs and resources of the local body. Specifically, “[a]uditing plays a critical role in public finance. Indeed auditing is essential to the credibility of accounting and financial reporting by the state and local governments” (Gauthier 2002, vii). Therefore, an absolute must for the county is to conduct a forensic audit.

The county must determine exactly how far in debt it is. In my research I have found no less than four different numbers that are supposedly the actual debt. The media typically uses \$3.2 billion, while some newspapers such as the Bond Buyer report \$4.6 billion. The actual budget for 2006 shows debt of \$6.7 billion and the last audit report for the fiscal year ended September 30, 2007 stated the total debt was \$4.5 billion (Warren, Averett, Kimbrough and Marino, LLC 2009). However, considering the audit report was not released until January of

2009, the report is worthless due to the increased debt caused by the auction rate securities. In short, no one has any inkling of how much the county actually owes its creditors.

It will most likely be necessary to recreate the 2006 and 2007 audits before beginning on the forensic audit itself. Whatever the methodology used to determine the actual balances, this audit needs to be performed immediately. The commission as well as anyone (such as the business community) that attempts to create a solution at this point has no idea how bad the problem is. How then can a solution to the problem be created when the problem cannot be stated? Of course an audit alone will not suffice to generate a plan of action, but it will at least inform the decision-makers and the public about what the current condition of the county is. From there a plan may be formulated to extricate the county from the disaster in due course. If a forensic audit is not performed the commission will continue to “steer by its wake.”

In order to prevent the type of cronyism that has pervaded the county, an audit firm with extensive forensic experience should be selected from a competitive bid process. Furthermore, the selection of firms to perform future audits of the county should also be bid at least every three years, which is the recommended practice of the Government Financial Officers Association. By implementing these tools, the citizens, banks, bond-holders, commissioners, the state legislature and others would be able to have accurate information with which to take corrective action. The information gleaned from these reports would empower the existing and potential regimes with actionable intelligence that could be used to mobilize the necessary resources that could enact change in the political and financial systems. While there is again no guarantee that the data would be used for positive public purposes, it does at least serve to make the information public can then level the playing field for various regimes.

The next step the county must take is by far the most difficult (emotionally at least) and that is declaring Chapter 9 bankruptcy. There was sharp division about whether it should be declared or not. Some commissioners saw it as inevitable, but both Betty Fine Collins and the Governor Riley were dead set against it. Regarding bankruptcy and regimes it can reasonably be asserted that a declaration of Chapter 9 would neutralize the financial regime that has been so prevalent during the later stages of Jefferson County's crisis. Due to the nature of Chapter 9, banks and bond-holders would lose not only collateral (possibly), but some degree of influence over the activities of the county. It is possible that other regimes may indeed be created which are financial in nature, but the specter of bankruptcy will aid in diminishing the power of a financially-center regime. The existing effect of the financial regimes control of the Office of the Governor is easy to see.

Governor Bob Riley has repeatedly stated that a Jefferson County bankruptcy would send a bad signal to market and to the state's next generation. "He brokered an agreement for Wall Street banks and bond insurers to offer nearly \$1 billion in concessions to resolve the emergency, but the county's [state] legislative delegation balked at a request to divert \$27 million a year or more from excess education sales tax revenue to help reduce the debt" (Kent 2008). Commissioner Collins had a similar statement regarding bankruptcy, "It would be detrimental to our community for the next 50 years" (Wells 2009). Realizing that there is a stigma attached to bankruptcy, as Adam Smith conveyed the county is in a state of implied bankruptcy at the moment. The stigma will fade in time and may even allow the county to reinvent itself into a stable political entity¹⁷.

There are certain prerequisites to declaring Chapter 9. The first deals with eligibility. Congress first authored municipal bankruptcy legislation during the Great Depression. This was

¹⁷ There was no similar outcry from the municipalities when VisionLand declared bankruptcy.

potentially a constitutional issue, because the states had (and do) retain authority over local governments. Therefore, even though a Chapter 9 exists in the IRS code, states have the option of developing alternative restructuring of debts by municipalities. As defined by 11 USC § 101 (40) a municipality is a “political subdivision or public agency or instrumentality of a State” (School n.d.). Jefferson County and most other counties of the state remained so after the adoption of the 1901 Constitution. Further the state has allowed for its municipalities to declare Chapter 9, although the statute does have additional requirements. “Section 109(c) of the Bankruptcy Codes sets forth four additional eligibility requirements for chapter 9: the municipality must be specifically authorized to be a debtor by state law or by a governmental officer or organization empowered by State law to authorize the municipality to be a debtor” (Courts n.d.). Under the Constitution of 1901 Article 12, Section 222, counties and other local governments are allowed to borrow funds and issue bonds. The second requirement is “the municipality must be insolvent, as defined in 11 U.S.C. § 101(32)(C)” (Courts n.d.). This statute states: “with reference to a municipality, financial condition such that the municipality is—

- (i) Generally not paying its debts as they become due unless such debts are the subject of a bona fide dispute; or
- (ii) Unable to pay its debts as they become due” (Congress n.d.).

As of July 2009, Jefferson County began missing due payments on its debt. Subsequently, the county and its creditors entered into several forbearance agreements, but they expired September 30, 2009. To date they have not been renewed and default has been declared, thus the county fits the second requirement. The third requirement is “the municipality must desire to [a]ffect a plan to adjust its debts” (Courts n.d.). The county may lack the political will to declare

bankruptcy, but as far as the Code is concerned this requirement can be met simply by the county willingly seeking bankruptcy protection.

Finally, “the municipality must either:

- obtain the agreement of creditors holding at least a majority in amount of the claims of each class that the debtor intends to impair under a plan in a case under chapter 9;
- negotiate in good faith with creditors and fail to obtain the agreement of creditors holding at least a majority in amount of the claims of each class that the debtor intends to impair under a plan;
- be unable to negotiate with creditors because such negotiation is impracticable; or
- Reasonably believe that a creditor may attempt to obtain a preference” (Courts n.d.).

The goal of this section of the Code is to force creditor and the debtor to sit down and work out a mutually beneficial plan for the discharge of the debts. Unlike Chapter 11 and other bankruptcy avenues, a municipality cannot be liquidated to settle the debts, nor can the courts or the creditors intervene in the daily operations of the municipality. The plan must be presented to the court and it can be accepted over the dissent of certain creditors. Furthermore, the general obligations of the county, if any, are included in the bankruptcy get an automatic stay, whereby payments stop, no further collection activities can take place and the officials even enjoy some legal protections. As for the special revenues, in this case from the sewer system, payments will continue (or restart in this case) to the bondholders, but even these revenues cannot be taken at the expense of operating the system. This, in essence, leaves only part of the revenues for the bondholders, but this works to everyone’s advantage. The bondholders benefit by getting some type of revenue stream from the bonds and the county benefits by retiring some of the debt without causing an

undue burden on its operations or its citizens. The only issue that I can foresee with this solution is that as stated previously certain revenues are not at the disposal of the county since home rule is not allowed. Therefore, it may be necessary for state legislative action before a debt relief plan can be implemented. That would indeed be unfortunate, but if the plan were solely to use the revenues from the sewer system, which is as it should be then a workable plan is feasible.

Considering the relative ease of declaring, planning, and implementing Chapter 9 it is indeed an ideal solution to the problems of lingering debt and the arguably more damaging uncertainty. Bankruptcy is not a pretty word, but in today's economic climate, I believe most would understand its necessity and support it politically. Furthermore, I do not believe that bankruptcy would be a catastrophe that would remain a haunt to the county in 50-years' time. That is fear speaking. That fear is of a legacy being not just tarnished, but completely destroyed. The markets have a very short memory. As a case in point, two years ago General Motors declared bankruptcy and as of this writing they are about to sell stock via an initial public offering. For a public sector example the often cited Orange County, California declared Chapter 9 in 1994. According to the website of the County Auditor they were able to refinance a bond issue of more than \$136 million in 1997 (Office 2010). Only three years after a declaration of bankruptcy, they were creditworthy again. The same can be true of Jefferson County if they would only realize that the options of not declaring are worse. Here again it may be possible to reduce the potential effects of the financial regime by utilizing Chapter 9.

It is precisely the need to weigh options that cements the need for Jefferson County to hire a professional manager. In the special session of the state legislature that corrected the occupational tax issue discussed in the previous chapter, a bill was introduced and passed that required the commission to hire a county manager (CM) and have them report to work no later

than January, 2011. This is a step in the right direction as I feel that one way the county can start down the path to recovery is by having a professional manager on board. However, I do have concerns that this is not well received by the commission, as it is a mandate from the state. It is usually better for a marriage to happen, rather than be forced, but this is Alabama politics.

CM's in Alabama are rare. Only the cities of Anniston, Auburn, Dothan, Mountain Brook, and Talladega have CM's, although two others are moving in the direction¹⁸. Several cities and counties have chief administrative officers (CAO) that function much like CM's only without some executive authority. Ironically, the current commission ran on a platform supporting the hiring of a CM, but that was promptly dropped once they took office. Since the commission no longer has a choice in the matter they should warm to it and seek to take advantage of the knowledge of a CM. There are three main reasons for doing so.

The responsibilities of the CM have changed over the years although there do seem to be some that are timeless and boundary-less. A primary responsibility is implementing the policies of the legislative body. This involves the actual day-to-day operation of the local government including personnel, finance, public works, public safety and economic development. Such activities include development of the budget, hiring and firing decisions, and assistance with recruitment of companies. This puts tremendous pressure on the CM to be a generalist, which is very different professionally from many of the traditionally technical jobs municipalities require. Thus the role of the city manager has changed dramatically.

Before, the early 1990's most CMs would have probably thought of themselves more as technicians however, as the demographics of the workplace has changed so has the role of the CM. Instead of a top-down approach, the CM has, at least in one role, become a facilitator. This

¹⁸ Vestavia Hills has an initiative on the ballot this fall (2010) and Decatur just approved the council-manager form of government.

has occurred because of the organization chart has ceased to be vertical and has moved increasingly to a horizontal model. Nalbandian argues that “[c]ity managers today cannot mandate changes because, more than before, they do not command the technical knowledge to fully understand what they are asking for” (Nalbandian 1999, 193). He goes on to provide an example that “[a] city manager cannot tell a public works director that the council favors a proposed development that requires hooking up to a particular sewer line because it is more economical for the applicant, when the public works director says the downstream capacity won’t handle the added load of wastewater” (Nalbandian 1999, 193). Therefore, the city manager must then facilitate some type of mutually workable solution between the technocrat and the council. It is precisely this type of facilitation that may have prevented the Jeffco sewer system from getting out of hand. By facilitating an actual planning process between the Environmental Services Department, the Finance Department, and the Commission, lines of communication could have been opened, coordinated budgets could have been adopted, and expansion policies developed. All of these items could have been implemented in a professional and competitive manner had any of the departments worked together.

This is the fallacy that some Commissioner’s still fail to see when they continue to support the commission form of government, which combines the executive and legislative bodies into one. Commissioner Sheila Smoot, in response to a proposed county manager bill by the state legislature said that it “can wait a year or years if it wants, but she will never support taking the elected commission out of the business of running the county” (Dean and Chandler 2009). She went on to say “[t]he people of this county in each of our five districts voted for each and every one of the folks on the commission. They have not voted for one person to have

all the power to run this whole county and neither will I” (Dean and Chandler 2009)¹⁹ . This is a complete misunderstanding of the role of the county manager. The CM is there to support, advise, and move the policies *adopted by the commission* from the realm of thought to reality. A CM does not in any way shape form or fashion remove the elected official from their role as a public servant; rather it enables a better form of democracy. This is accomplished by freeing the elected officials from the daily tasks of governance and allowing them more time to focus on constituent issues and policy formulation. “Hoover Mayor Tony Petelos said [] at his State of the City address in December, “We have five CEOs running the county government... I don’t know of any company in America with five CEOs” (Caputo 2009).

There should not be five CEO’s running the county government; there should be an elected body responsible to the citizens of the county and they should hire a CM to effectively, efficiently, economically and equitably run the day to day operations of the local government. The goal of the CM should be the facilitating of solving problems. This can be brought about through managing the various regimes that seek to influence county operations. It is important to note that the facilitation aspect of the CM’s responsibilities “is designed to help promote a problem-solving orientation and to develop consensus among diverse interests” (Nalbandian 1999, 195). Eric Anderson, currently City Manager for Tacoma, Washington is quoted as saying “[t]his is not warm and fuzzy stuff; it is hard work. I have found it to be the toughest work we do. You’ve got to be incredibly patient and thick-skinned, and you have to have some sense that there truly is value in the processes because they are tremendously time consuming and occasionally abusive” (Nalbandian 1999, 195). The CM’s greatest responsibility is acting as a facilitator between the ever competing values of the political sphere and the administrative

¹⁹ Jefferson County elected commissioners by district, not at-large.

sphere. This is an area where it becomes very difficult for either purely elected officials or careerists to work. Therefore the CM creates a tremendous amount of public value by bridging these two spheres of influence.

Sam Gaston, City Manager of Mountain Brook, Alabama (within Jefferson County) and President-elect of the International City/County Management Association (ICMA) said that by having a commission form of government there is “no one in charge of the big picture. There are five independent kingdoms and no one person in charge of the entire operation” (Gaston 2010). Further he indicated that a CM could have helped prevent the crisis by ensuring that contracts were legal and that the state bid laws were being followed. The CM would have been able to coordinate the activities of the CFO, ESD, and the Commission negating some, if not all of the effects of the banking and contractor regimes that influenced the process.

By having a CM, another faction is created through which the others regimes must work with and through. This has the benefit of allowing the CM to facilitate a community-building process that serves the public. Further, it would be possible to preserve the integrity of the political body while ensuring projects are moving forward at a reasonable pace and within legal boundaries. Being able to see the entire view of the operation is critical to prevent the factions and regimes from a divide and conquer strategy as we have seen work so well in Jefferson County.

Alternatives

There are alternatives to the solutions I propose that are worthy of consideration. Although no alternative suffices without an adequate accounting of the County’s current financial position, thus in any event, an audit of some magnitude is required, preferably forensic in nature. In regard to potential bankruptcy a first alternative is to negotiate a settlement with

existing creditors. A deal of this shape must include a substantial loss to the banks in order for Jefferson County to regain any financial standing in the credit markets. This may enable the County to stretch payments out beyond the 25 and 30-year bonds which are currently existent; however this will still not allow the county the necessary revenues to service the sewer system, meet the demands of the consent decree, and adequately provide future infrastructure for economic development. In addition, this remedy does not deal with the antiquated structure of the government or the revenues lost to the occupational tax.

A second alternative is a court-appointed receiver for the sewer system. This too is to the detriment of the county, because a receiver would have the interests of the creditors at heart and not the citizenry of Jefferson County, which must be the primary concern. Additionally, the cost of a receiver would come from the sewer revenues which again detract from the ability to repay the debt. Further, as has been contemplated a receiver may have the court-ordered ability to raise rates at will. This is a direct violation of citizen's rights to elect its representatives, when the connection to the sewer is mandatory by law. It is very much akin to taxation without representation.

A third alternative would be to outsource the sewer system and/or sell it to a third party. This would not alleviate the debt at all and would remove the one asset pledged to the revenue bonds thus requiring creditor approval. Only by placing the system in bankruptcy first and making this part of the Chapter 9 workout plan would this be a viable solution. In conclusion, in order to effectively deal with the debt, lost tax revenues, corruption, and poor administration, the best alternative for Jefferson County remains bankruptcy.

Regarding the administrative structure of the County it is entirely plausible that the County could retain its existing structure, although this is the equivalent of doing nothing to

alleviate the previously cited problem of having five individuals in charge of the organization. However, it is possible for the County Commission to restructure not the Commission itself, but to hire a County Administrator. It may sound semantic, but the differences between an administrator and manager are significant. Most administrators do not have hiring and firing authority and act more like Chief Operating Officers rather than Chief Executive Officers. This would allow for more of the day-to-day operations to fall on the shoulders of one individual, but this structure could easily be circumvented by the Commission, since the hiring of an administrator does not change the form of government.

Another alternative that has seen some success is that of a county-wide elected executive. This form of government basically creates a strong-mayor/executive form of government at the county level. One of the most successful implementations of this form has been King, County Washington (Seattle). However, this is also, in my opinion not the best course of action, because as with most elected posts there are very few qualifications and it would be rather easy to see someone elected with no experience managing a large organization. This has only a limited upside potential while potentially compounding the problems exponentially.

While a County Manager is certainly not a panacea, a CM would allow the Commission to hire a person with qualifications that could be dismissed at their leisure (pending contractual obligations), but that person could be a steadying force for the County and will allow the Commission to return to its rightful role as a policy-making body rather than an administrative unit. However, no structure contemplated herein can be accomplished by the County alone, thus the State Legislature must be the body that moves to make any of the aforementioned structures possible.

CHAPTER 8

Conclusion

Marty Linsky, a lecturer at the John F. Kennedy School of Government at Harvard and author of *Leadership on the Line*, is fond of saying that organizations are perfectly aligned to get the results they are currently getting. In the coming months Jefferson County is about to be completely realigned with a completely new commission. The current administration has either chosen not to run or has been defeated in the primary elections. This is the most positive event that could have happened because the past and current performance of the commission has been dismal indeed.

The county has steadfastly and foolishly not selected a course of action; rather they have chosen a course of inaction. It has been relatively easy to uncover the motivations and reasons behind the corruption, but why the elected officials have done nothing are more difficult. One could surmise that the reasons are political, and the sitting commissioners do not wish to have their reputations tarnished. It is way too late for that, because if history passes any type of judgment on this and any other Jefferson County commission of the last 15-years it will certainly not be kind; nor should it.

The commission has failed as a body politic. They have repeatedly broken state bid laws as well as federal laws of fraud, corruption, and bribery. More importantly they have broken their trust with the public. They have taken from the poor, needy, disadvantaged, middle-class and rich alike to line their own pockets and to line the pockets of their cronies. The commission has not been alone in this endeavor.

The same can be said of the public servants that have been party to this pillaging of the county. They too have broken the public trust by having their houses remodeled, by taking cash, and other bribes and for what? Not that any of this is justifiable, but the paltry sums for which they sold out speak volumes. It is rumored that everyone has a price, but these men were cheap. They used public resources they had been entrusted with to create a system that could be used by the citizenry, but diverted those to their own uses and to enrich the members of various regimes.

These regimes often did not work in concert with one another, but that is the nature of a regime, an informal group that seeks to control and influencing the political will. At various times, the contractors, bankers, and lawyers all had a hand in influence county policies for their own benefit. Many of the contractors have been jailed on the same charges as the public officials, while only two bankers have been tried and convicted. No lawyers who gave any advice in this crisis have even been remotely affected. I would argue that thus far they are the only ones who may actually profit. The banks and bondholders will be take a loss (some major) if bankruptcy is declared as they will be forced to make a deal. The ratepayers will certainly lose because no matter the settlement, they will have to pay for all of the mistakes made during the past 15-years even if no others occur between now and when the county returns to a sound financial setting.

The idea of growth was used against the commission as tool by regimes to influence continued spending and debt. A falsehood that you can grow your way out of any situation has been propagated for years. Environmental Services did it by placing sewer expansion work on the commission agenda on a piece meal basis claiming that if only we had another line we could add any number of new ratepayers to help finance the system. The concept is simply wrong. You cannot grow your way out of debt, for the simple reason that you have to pay for the new

line in the first place. Therefore you have absolutely no improvement in the status quo if you get new ratepayers, and if you don't then you are in a net negative situation. No analyses were ever performed on the "needed growth" just as there was no comprehensive planning for the sewer expansions.

This idea of getting out of debt by growth was also supported by the banking regimes. They too felt that as long as the county could continue to grow, sewer revenues would continue to increase and they would be able to continue to develop very lucrative finance products to sell to the commission to "lower costs." I am not the least surprised by the fact that the banks were trying to mislead Jefferson County or that they would sell them a bill of goods, since they were buying off the politicians, they might as well get all that they could. Was it right to do so? No, of course not, but it was the reality at the time and there are ways in which the county could and should set things right. If followed these methods will end or at least curb the growth-debt-vulnerability cycle.

There are steps that can be taken such as determining the amount of debt actually outstanding, declaring bankruptcy and hiring a professional manager. The county faces major challenges as it moves forward, but a policy of inaction is not a solution, just as hope is not a method for success. Since the current commission is reluctant to hire a professional manager, I can only hope that the new one will be more amenable. The transition to a council-manager form of government would not be difficult for the commission alone though.

The CM would also have a major challenge on their hands. The crisis was not created overnight and will not be solved anytime soon. Gaston argues, "[t]he manager must set the tone" (Gaston 2010). The staff of the county is most likely highly demoralized and new blood is required to reinvigorate it. That rejuvenation can come from a hard-charging manager that can

set a new tone, one of teamwork and efficiency. Each potential CM will have his or her own style, but leadership must be exercised. None of the aforementioned remedies will be attempted or have any chance of working without the exercise of leadership and the creation of public value.

The creation of public value comes from taking public resources, which are often co-opted from private consumption through taxation, and satisfying the needs and desires of citizens. This can include anything from garbage pick up to national defense. Certain goods are not always tangible, but they do have value--public. Naturally, we do not always agree on what constitutes public value or how to create it. There are sitting commissioners who wholeheartedly disagree with my arguments for audits, bankruptcy, and professional management because they do not value the end results that may come from these suggestions. That is perfectly acceptable, except for the fact that they have done nothing to create public value and everything to destroy it. I am sure that my suggestions are not the only ones. Nearly everyone who has any familiarity with the crisis has an opinion. What matters is that someone, namely, a CM is hired who can ultimately determine and help the commission create new public value by correcting the crisis. This is somewhat antithetical to the politics-administration dichotomy proposed by Woodrow Wilson, and later refuted by others, including Herbert Simon.

Traditionally, professional managers have been seen as exercising technical and administrative knowledge to effectively keep an organization running smoothly. However,

“[t]here is a different way of thinking about the proper role of public sector executives—one tied more closely to the reality of modern governance but geared to preserving, even enhancing, the ideals of democratic accountability. In this image, public executives are neither clerks nor martyrs. Instead, they are *explorers* (emphasis in original) commissioned by society to search for public value. In undertaking the search, managers are expected to use their initiative and imagination. But they are also expected to be

responsive to more or less constant political guidance and feedback. Their utmost ethical responsibility is to undertake the search for public value conscientiously” (Moore 1995).

This will certainly not be an easy task, and will require great leadership, but the task of rebuilding must begin and soon. The new commission must hire a manager by requirement of the state legislature. They should make the best of the situation and hire someone that will seek to use a facilitative, community-building strategy that will alleviate the debt, ease the burden on the public and remove the stain of corruption from the political landscape. Almost everyone should be able to agree that those items are all valued by the public.

Final Thoughts

As Sam Gaston and I were talking, I explained to him that the writing of this work has been a dual path for me. On the one hand, I feel as though I have been able to peel back the layers and get to the root of the problems in the county’s crisis. There is no doubt that I have missed some things and interpreted others incorrectly. However, I do feel as if I found the answers to the question I had...how did all of this happen? I am completely sad at the answer. Although I am no idealist, the thought that any government could be such an utter failure concerns me greatly. What troubles me more is the fact that the only reason for the failure is greed. Whatever manifestation of greed there was, it was at the heart of all the decisions that were made.

The Cahaba River Society did not want to sue; they only joined when it was obvious they were going to be excluded from the table that decided what the fix was going to be for the pollution. In my opinion Slawson sued for the money. He had an easy case to win and he admitted that his practice had taken off since the suit. I do not think that this was necessarily a foul idea, since the county was polluting and ADEM had no intentions of stopping it. In this instance, greed probably helped save the Cahaba.

During the development of the consent decree, I believe the seeds of corruption were sown between the public officials in the Environmental Services Division and the contractors they worked with on a regular basis. This too was all based on greed. The officials sold out for cheap and the contractors made millions. All of this came out of the pockets of the taxpayer.

As the rates increased, the bankers saw the carcass and decided to feast on it too. With new financial products that have been compared to weapons of mass destruction they sold the county on ways to lower their debt service. All the while knowing that the auction rate securities would most likely blow up, but what did that matter? They took the fees, sold the bonds and transferred the risk.

All the while the elected officials were getting spa treatments, custom-made clothes, studios remodeled, loans paid off, and cash. Again, this came at the expense of those that could least afford it as well as those that should not have to. This was no Robin Hood, steal from the rich give to the poor scheme. This was stealing from anyone and everyone. The word that keeps coming to mind throughout all of this is tragic.

I am further saddened by the fact that there is no leadership. The commission will not take any action. The state legislature has only made cosmetic changes and I am not hopeful about the pending elections. It is not clear to me why this is so. It may never be.

What is clear is that there are solutions to the problems that we face. They have been suggested before and ignored. The solution will require leadership. The hope truly lies in two bodies at the moment. The first is the public. They (we) must elect leaders that are willing to trust in a senior public executive to serve them with distinction and without blind loyalty, because their first duty is to serve the public. This will require the commission to cede a certain amount of authority and power, but it should enable them to focus more on the issues and the

formulation of policies and strategies that create public value and eliminate the greed and corruption from the county. They must be willing to face the cold hard facts no matter the political repercussions. The debt will be enormous and the bankruptcy embarrassing, but as evidenced by the Orange County example, this will be short-lived if done correctly and swiftly.

These problems of staggering debt and corruption can be solved if only the commission will exercise leadership. They need not be leaders all the time, but they must summon the will power to do what is right and necessary at the appropriate time. This is the exercising of leadership.

On the other hand, knowing that there are solutions to the problems gives me some hope that our system of governance is not beyond repair. I have no illusions that the solutions presented herein will solve everything, but I truly feel that there are solutions to the problem that can be fixed with the assistance of professional management. The regimes that have been so aggressive in policy decisions can be checked by the introduction of new regimes. The difference is that it is imperative that these regimes have the best interest of the public at heart. If not, the status quo remains and the growth-debt vulnerability cycle will continue unabated. Just as Madison desired to use factions to contain other factions at the federal level, so too must this tactic be employed at the local level.

In closing, I would like to point out that this crisis is not about the environmentalists, the contractors, bankers, elected or civil service officials. This crisis is about the public. It may not be fashionable to wax on about citizens when the foci could be on decision-making, corruption, or any number of processes, but at the end of the day, the public is the point. They are the ones who will continue to pay high rates on sewer bills, increased taxes, higher than necessary interest rates, bond insurance, and fees for construction work. All of these funds will come from the

taxpayer. One estimate shows that the cost of the crisis is more than \$11,000 per person. For now the number is irrelevant, because it's not truly known. It will be in time; however, for the time being it is still important to remember that every cent taken by the government for its failure is less the individual can use for his or her own welfare or that of their family. In a society that cherishes the ideal of the rugged individual, Jefferson County has ensured that we are all miserable together.

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Appendix A

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Appendix B

Persons Interviewed

Byington, Pat, Former Commissioner Alabama Department of Environmental Management

Gaston, Sam, City Manager Mountain Brook, Alabama

Sheets, Tricia, Office Manager, Cahaba River Society

Slawson, Bart, Attorney-at-law

Stewart, Beth, Executive Director, Cahaba River Society

Appendix C

Semi-Structured Interview Questions*

1. What has been your involvement with the Jeffco crisis?
2. Why do you think Jeffco was sued? Was it pollution of the Cahaba?
3. Why was Jeffco dumping waste directly into the Cahaba?
4. Why did the Cahaba River Society join the lawsuit late?
5. In your opinion do you feel that the EPA was light on enforcement of the Clean Water Act and during the subsequent consent decree?
6. Why did Jeffco not fight the lawsuit in court?
7. Why was Environmental Services so defiant in producing adequate documents for EPA?
8. Why was there no overarching plan that incorporated Environmental Services and the Finance Office?
9. Why was only one commissioner assigned responsibility for overseeing environmental services?
10. How did a \$500 million dollar project balloon into 3.6 billion in debt?
11. Why were \$650 million dollars in projects left unspecified?
12. What was the relationship between Bill Blount, Larry Langford, and Wayne LaPierre?
13. Why was Steve Saylor never prosecuted?
14. Why were no audits performed during those years?
15. Why was there a need to refinance the fixed rate bonds?
16. Who make the bond refinance recommendations?
17. What is the impact of the occupational tax?
18. Why do you think the body politic failed?
19. What can be done to solve this crisis?
20. What can be done to prevent a crisis of the magnitude again?
21. Should the county declare bankruptcy?
22. Are the bankers or the politicians at fault?

*Not all questions were asked of all interviewees.