

Emily Edmonds-Poli

Debt Financing and Municipal Autonomy in Tijuana

University of San Diego

Political Science

Faculty Research

**USD TRANS-BORDER INSTITUTE
TBI GRANT COVERSHEET**

Please submit all grant materials with this form by March 15, 2007.
Please type or print (please use black or blue ink).

Project Title: Debt Financing and Municipal Autonomy in Tijuana

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Co-Applicant(s) and Department(s):

Date(s) of Grant Research and Activities: July 07 - June 08

Total Amount Requested: _____

Type of Grant (select one*): Faculty Research; _____ Other Border Activities

Brief Description of Project/Activities:

This project examines Tijuana's recent efforts to enhance local fiscal autonomy through the use of debt financing.

Please list any additional funding sources and/or sponsors:

Funder	Contact Information	Total Amount
<u>N/A</u>		

For TBI's annual grant competition please submit all required materials by **March 15, 2007** (see grant guidelines). Requests for mini-grants may be submitted throughout the year. Please direct any questions or concerns about TBI's Grant Program to:

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Project Abstract: TBI Intramural Grant, 2007-2008**Faculty Research Project: Debt Financing and Municipal Autonomy in Tijuana**

On paper, Mexican municipalities have a considerable amount of independence to decide their own affairs. However in practice, municipalities rely heavily upon the federal government for the bulk of their economic resources. Even in relatively wealthy cities like Tijuana approximately sixty-five percent of the budget comes from federal transfers. Moreover, the vast majority of federal transfers are earmarked for specific purposes and remaining funds often must be used to cover a municipality's basic operating expenses. Consequently, municipal autonomy is severely limited in Mexico: without full authority over the budget, local governments lack the ability to make and address their own priorities. This has profound implications for the quality of local governance and democracy in Mexico.

Given this reality, the past ten years have seen a plethora of attempts by municipal governments to maximize their autonomy by increasing locally generated revenue. One of the most recent and understudied types of efforts is debt financing. Tijuana is one of the few local governments to contract foreign debt for the purpose of augmenting their pool of unrestricted budget funds. The purpose of this project is to examine how and for what purpose the government of Tijuana borrowed abroad. It will also focus on the economic and political implications of this revenue generation strategy. A cursory look at this issue suggests that debt financing allows local governments to deliver more in the way of public services and infrastructure, without incurring the political costs that often accompany other revenue generation strategies (e.g., raising taxes). Moreover, if successful, such a strategy has the potential to contribute significantly to local development in Tijuana, which in turn might lead to improvements in living conditions, more job opportunities along the border, and fewer incentives to emigrate. However, much more research is needed before such conclusions can be drawn. This project will combine semi-structured interviews and archival research in an effort to understand the dynamics and implications of Tijuana's experience with debt financing.

Project Description: TBI Intramural Grant, 2007-2008**Faculty Research Project: Debt Financing and Municipal Autonomy in Tijuana****Project Description and Rationale**

Despite the provision of Article 115 of the Mexican constitution, which calls for local autonomy (*municipio libre*), municipalities in Mexico have traditionally been subservient to higher levels of government. During the era of PRI hegemony, this subservience was felt politically—party leaders often hand-selected mayors, and economically—mayors were wholly dependent upon federal largess for the size of their budgets. Electoral competition has altered this scenario only partially. While local officials are now elected in mostly free and fair contests, municipalities still rely heavily upon the federal government for the bulk of their resources. Even relatively wealthy cities like Tijuana are beholden to the federal government—sixty-five percent of its revenue comes from federal transfers—because municipalities possess weak mechanisms for generating their own revenue. Moreover, local governments have little say in how federal transfer money is used because most of it is earmarked for specific purposes by the federal government. Consequently, municipal autonomy is severely compromised. To be sure, local and federal priorities often coincide, especially with respect to providing basic infrastructure to underserved communities. However, the very fact that municipal administrations must abide by federal guidelines when allocating what often amounts to over half of their annual budget, significantly undermines the independence of local governments to decide and fund their own priorities. Local autonomy is further limited by the fact that the vast majority of unrestricted transfers are used to cover the municipality's basic operating expenses (e.g., salaries and benefits, administrative costs and equipment maintenance, etc.). Therefore, when it comes to funding local priorities, municipal governments have very limited funds with which to work.

While local governments are financially dependent upon the federal government, there are two important mechanisms available to local governments for generating revenue: property

taxes and debt. The significance of these types of income should not be underestimated because they often give local administrations the ability to realize projects that fall outside the scope of the earmarked federal transfers, or would otherwise fall victim to insufficient funds. Understandably, many municipalities look to these mechanisms as a means of generating additional unrestricted funds. Of the two, debt traditionally has been more attractive to local leaders because it yielded more in the way of resources and did not incur the same political costs as collecting taxes.¹

Municipalities in Mexico have long used debt as a method of paying for public works and services, as well as addressing budget shortfalls, especially in the wake of economic crisis. Moreover, debt was even more attractive as an economic strategy because until recently, the federal government served as a guarantor that would regularly bail out state and local governments rather than allowing them to default on their loans. Under these circumstances, municipalities had few incentives to pay back loans on time, or even in full. Recognizing the financial and political consequences of the recurrent need to bail out subnational governments, the Zedillo administration (1994-2000) enacted a number of reforms in 1999 to harden subnational budget constraints. The reforms included allowing states and municipalities to borrow from foreign sources, but at the same time established that the central government would no longer guarantee subnational debt. Equally important were the reforms that required state and local governments obtain credit ratings from independent firms and guarantee their own loans with federal transfer revenue, often channeled through a trust. Together, these reforms made the use of debt financing more difficult for municipalities, but they made the practice of contracting debt more objective and financially sound. That is, before 1999, a local government's ability to borrow money depended not on its financial base or creditworthiness, but on personalism (i.e., the mayor's relationship to the PRI leadership) and political criteria (e.g., the electoral importance of

¹ Property taxes traditionally did not yield many resources for local coffers because local bureaucracies lacked the necessary training and technology to fully exploit this source of revenue. Equally important was the absence of a taxpaying culture in Mexico: why give money to the government just to see local officials line their pockets? Slowly both of these situations is changing and many municipalities, Tijuana among them, have made great strides in using property taxes and other local fees as important sources of revenue.

the municipality in question). With the new reforms, debt financing is now theoretically an option for any local government, regardless of its partisan affiliation, as long as it can demonstrate its creditworthiness.

The broad purpose of this research project is to get a preliminary look at the extent to which these changes in the national laws that regulate local debt have affected municipalities' efforts to generate their own revenue. In other words, despite the difficulties of borrowing money, have local governments seized the opportunity to issue bonds in order to have access to more unrestricted resources? If so, under what circumstances and to what effect? Given that these reforms are relatively recent, and that not many municipalities have the financial resources or political will to take out loans under these circumstances, it is not surprising that Tijuana is one of the few local governments that has engaged in this kind of activity. My research will focus on the municipality's experience between 2001 and 2007 in an effort to understand the local view of debt financing as a strategy for generating local revenue. More specifically, I hope to gain insight on how and for what purpose the government of Tijuana decided to contract debt. I will also examine whether using this strategy has had political benefits that other strategies (e.g., raising taxes) do not. That is, are there electoral or other political advantages to using debt to realize public works projects that otherwise would have been impossible to implement?

Answering these questions will contribute to our understanding of not only the specific experience of Tijuana, it will also help elucidate whether debt financing is an attractive and viable strategy for municipalities interested in enhancing their financial autonomy by generating a new source of unrestricted funds. If the practice becomes widespread (even if it is limited to the larger, wealthier municipalities), this will have important implications for Mexican democracy. Local governments that are more self-sufficient have the ability to be more efficient and responsive to local demands because they are no longer beholden to federal rules that regulate transfer revenue. In turn, once citizens see that their elected officials are responsible and responsive, they may be more likely to trust public institutions and, therefore more willing to see

the value, and indeed their responsibility, to contribute to the public coffers with local taxes. On a broader scale, public trust in local government can also be parlayed into stronger support for democracy more generally. Reinforcement of the value of democratic ideals and practices is important in Mexico where the transition away from single-party rule is quite recent and not fully consolidated. Also of importance is the possibility that debt financing might help promote local development by increasing the pool of resources available to address a range of issues from hunger and housing shortages, to new and improved infrastructure projects. The benefits of local development cannot be overstated. In the case of Tijuana, this could mean improved living conditions for citizens, more local job opportunities, and fewer incentives to emigrate to the United States. Such developments could have other important implications for the border region and U.S.-Mexican relations. For example, if municipalities like Tijuana are more financially sound and demonstrate their ability to repay loans and reliably uphold their end of an international financial contract, they will become more attractive to U.S. (and other) investors looking for investment opportunities close to the United States.

In sum, examining the issue of local debt financing has the potential to shed light on a variety of important topics and Tijuana is a particularly good case study for this project. As one of the wealthiest and most economically sound municipalities in the country, it is considered a good credit risk and therefore more likely to engage in debt financing. Furthermore, with its history of partisan alternation (the PAN governed the municipality between 2001 and 2004, but the PRI came to power in 2004 and remains there at least until later this year), it provides a preliminary look at whether party affiliation has impact on a local administration's willingness to use debt as a source of local revenue. Finally, Tijuana's size and political history make it an important bellwether for the rest of the country. As one of the most advanced local governments, practices and strategies adopted there will undoubtedly influence those of other local governments. Thus, studying Tijuana provides insight on future trends in Mexico.

Research Methodology

In order to understand the dynamics of local debt financing I will need to combine three methods of data collection. First, I will need to conduct some background research on the reforms of 1999 and the rules regulating debt financing in Mexico. Much of this information is available through the *Diario Oficial de la Nación*, posted on the Internet or available in the state government offices in Mexicali. I will then need to gather data on Tijuana's experience during the past six years. This information will come from a combination of semi-structured interviews of current and past local officials, academics at COLEF (most notably, Dr. Tonatiuh Guillén, a knowledgeable scholar in the field), and state level officials in Mexicali. I will also have to conduct archival research in order to gain acquire all of the necessary budget figures and public records on Tijuana's public debt. While most of this information is theoretically public, prior experience suggests that it will require several trips and/or serious digging to acquire. For this reason, I have included in my budget money to hire a graduate research assistant to help with the project. It is my hope that working with graduate student on this project will not only allow me to complete it in a timely manner, but that it will also give the student first-hand research experience.

Expected Outputs

This research project will yield at least two outputs. First, I will compile my preliminary findings in a conference paper to be presented as part of a panel entitled: "Transnationalization and Border Cities" at the Latin American Studies Association International Congress in September 2007. Presenting this paper will provide me an opportunity to reflect on my early findings and obtain valuable feedback from my academic peers that will no doubt help me refine the project. I will then be in a stronger position to enhance the project with the additional research discussed above. By the summer of 2008 I will be prepared to submit an article for a peer-reviewed journal (e.g., *Publius: The Journal of Federalism* or *Mexican Studies/Estudios Mexicanos*). This research will also serve as the foundation for a future comparative study of other municipalities in Mexico.

Select Bibliography: TBI Intramural Grant, 2007-2008

Faculty Research Project: Debt Financing and Municipal Autonomy in Tijuana

Roy Bahl and Johannes Linn, *Urban Public Finance in Developing Countries* (New York: Oxford University Press, 1992)

Wayne A. Cornelius, "Blind Spots in Democratization: Sub-national Politics as a Constraint on Mexico's Transition," *Democratization* 7, no. 3 (2000), 117-132

"The Debt Market, a Financing Option for State and Local Governments." *Fitch Ratings Special Report*, February 2004

Alberto Díaz-Cayeros, *Desarrollo económico e inequidad regional: hacia un nuevo pacto federal en México* (Mexico City: Fundación Friedrich Naumann, Grupo Editorial Porrúa and Centro de Investigación para el Desarrollo, 1995)

----. "Decentralization, Democratization and Federalism in Mexico," in *Dilemmas of Political Change in Mexico*, ed. Kevin Middlebrook (La Jolla: Center for U.S.-Mexican Studies, University of California, San Diego, 2004)

Alberto Díaz-Cayeros, José Antonio González and Fernando Rojas, *Mexico's Decentralization at a Cross-Roads* (Working Paper No. 153, Center for Research on Economic Development and Policy Reform, Stanford University, 2002)

Emily Edmonds-Poli "Decentralization under the Fox Administration: Progress or Stagnation?" *Mexican Studies/Estudios Mexicanos*, 22:2 (Summer 2006)

Richard Fagen and William Tuohy, *Politics and Privilege in a Mexican City*, (Stanford: Stanford University Press, 1972)

"Financing of Mexican States, Municipalities and Agencies: Alternatives and Strategies." *Fitch Ratings International Special Report*, January 31, 2002

Marcelo Giugale and Steven Webb, eds., *Achievements and Challenges of Fiscal Decentralization. Lessons from Mexico* (Washington DC: The World Bank, 2000)

Richard Musgrave, *The Theory of Public Finance* (New York: McGraw Hill, 1959);
Wallace Oates, *Fiscal Federalism* (New York: Harcourt Brace Javanovich, 1972)

Victoria Rodriguez, *Decentralization in Mexico: From Reforma Municipal to Solidaridad to Nuevo Federalismo* (Boulder: Westview Press, 1997)

Victoria E. Rodriguez and Peter M. Ward. *Policymaking, Politics, and Urban Governance in Chihuahua: The Experience of Recent Panista Governments*, (Austin: LBJ School of Public Affairs, University of Texas at Austin, 1992).

----. *Political Change in Baja California: Democracy in the Making?* Monograph Series 40, (La Jolla: Center for U.S.-Mexican Studies, University of California, San Diego, 1994).

---- eds., *Opposition Government in Mexico*, (Albuquerque: University of New Mexico Press, 1995)

Charles Tiebout, "A Pure Theory of Local Expenditures," in *Journal of Political Economy* 64:5 (1956)

Peter M. Ward and Victoria Rodriguez, *New Federalism and State Government in Mexico: Bringing the States Back In*, (Austin: Lyndon B. Johnson School of Public Affairs, University of Texas at Austin. U.S.-Mexican Policy Studies Program, Report no. 9, 1999)

Proposed Project Budget: TBI Intramural Grant, 2007-2008**Faculty Research Project: Debt Financing and Municipal Autonomy in Tijuana**

Expenditure Type	Calculation	Total Expense
Grad. Research Assistance 10 hours per week for 40 weeks to begin approx. July 15, 2007 and end approx. May 30, 2008.	400 x \$13 per hour	\$5200.00
Non-benefits based rate	\$5200 x .067	\$348.40
Travel costs to Mexicali, COLEF, Tijuana (costs include mileage, insurance, copy expenses, etc.)	10 x \$100	\$1000.00
Materials and misc. (e.g., photocopying, books, telephone calls, newspaper subscription)	\$350	\$350
Travel costs to attend LASA Congress in Montreal (September 5-8, 2007)	Conference hotel: 4 x \$275 per night	\$1100
	Airfare:	\$700
	Cabs, tips, misc.:	\$100
	Meals 4 x \$50 per day:	\$200

Total Requested: \$8998.00

Emily Edmonds-Poli

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Education

1994-2001 Ph.D. Political Science, University of California, San Diego.
1992-1994 M.A. Latin American Studies, University of Texas at Austin,
1988-1992 B.A. Latin American Studies, Middlebury College.
Cum laude and High Honors.

Professional Academic Experience

Assistant Professor (2001-present) Department of Political Science and International Relations.
Undergraduate Courses: Politics of Mexico, Politics of Latin America, Comparative Politics,
Introduction to International Relations.

Graduate Seminars: Politics of Latin America, US-Latin American Relations, Comparative
Politics, Politics of Mexico.

Director and Adviser (July 2006 to present) Master of Arts in International Relations Program
at the University of San Diego.

Publications

Journal Articles

"Decentralization under Fox: Progress or Stagnation?" *Mexican Studies/Estudios Mexicanos*
22:2 (Summer 2006).

Book Reviews

Mexico under Fox, (Lynne Rienner, 2004) Luis Rubio and Susan Kauffman Purcell, eds.,) and
Courting Democracy in Mexico: Party Strategies and Electoral Institutions, (Cambridge, 2003).
Latin American Politics and Society, 47:2 (Summer 2005).

New Federalism and State Government in Mexico: Bringing the States Back In, by Peter Ward and
Victoria Rodríguez with Enrique Cabrero, (LBJ School of Public Affairs, University of Texas at
Austin, 1999. *Journal of Interamerican Studies and World Affairs* (Winter 2001).

Encyclopedia/Reference

"Mexico" in Neal C. Tate, ed., *Governments of the World: A Global Guide to Citizens' Rights
and Responsibilities*. Detroit: MacMillan Reference USA. Forthcoming 2006.

Essays

"The United States and Latin America in the Post-September 11 Era" in Lisa Papera and Randy
Willoughby, eds., *Comparative Politics and the War on Terror*. University Reader Publications,
2005.

Work in Progress

Book Manuscript

Contemporary Mexican Politics (with David Shirk). Under contract with Rowman and Littlefield Publishers.

Journal Articles

"Debt Financing and Municipal Autonomy in Tijuana."

"The Emerging Role of Mexico's Governors in the National Political Arena."

Conference Papers and Presentations

"Mexico's 2006 Elections" Colloquium sponsored by the Transborder Institute and the Guadalajara Program, in Guadalajara Jalisco, June 2006.

Discussant for the panel entitled, "Decentralization at the Crossroads: Critical Junctures, Processes, and Actors," at the XXVI International Congress of the Latin American Studies Association, San Juan, Puerto Rico, March 2006.

Discussant for the panel entitled "The Politics of Decentralization Policy I: Mexico" Annual Meeting of the Southern Political Science Association, New Orleans, LA, January 2004.

"Local vs. National Priorities: An Assessment of the Fox Administration's Position on Decentralization 2000-2003." Prepared for delivery at the XXIV International Congress of the Latin American Studies Association, Dallas TX, March 2003.

"Decentralization and the Politics of Local Fiscal Independence in Mexico and India." (with Eduardo Gómez) Delivered at the 97th Annual Meeting of the American Political Science Association, San Francisco CA, September 2001.

"A Theoretical Approach for Understanding Variations in Municipal Autonomy in Mexico." Delivered at the Latin American Studies Association XXII International Congress, Miami, FL, March 2000.

"Making Decentralization Real: Strategies for Local Fiscal Autonomy in Mexico." Delivered at the 96th annual meeting of the American Political Science Association, Atlanta, GA. September 1999.

"The Implications of Electoral Competition for Fiscal Decentralization and Subnational Autonomy in Mexico." Delivered at the Latin American Studies Association XXI International Congress, Chicago, IL. September 1998.

"Local Governance in Mexico." Delivered at the Canadian Association of Latin American Studies XXVIII Congress, Vancouver, BC, Canada. March 1998.

"Fiscal Decentralization and Municipal Governance in Mexico: The Case of Chihuahua."
Delivered at the Latin American Studies Association XX International Congress, Guadalajara,
Jalisco, Mexico. April 1997.

Professional Service

Active member of the Latin American Studies Association (LASA)
Peer reviewer for *Publius*, *Latin American Politics and Society*, and *Mexican Studies/Estudios Mexicanos*.

University and Community Service

Graduate Studies Committee (College of Arts and Sciences)
Graduate Assembly (University-wide)
Study Abroad Committee
TBI Faculty Oversight Committee (FOCO)

Invited guest speaker/lecturer/commentator:

Transborder Institute conferences entitled, "Assessing the Mexican Vote Abroad," (February 2006) and "Transborder Migration and Development," (October, 2006).

KUSI (San Diego, Channel 9) (2006)

Johns Hopkins University Center for Talented Youth's College Colloquium (2004)

Center for US-Mexican Studies of the University of California, San Diego (2003, 2004)

Centro de Investigación para el Desarrollo, (CIDAC) in Mexico City (2002)

Ford Foundation Conference of Ford Fellows (2003)

USA Today (2005)

KBNT, Spanish-language television news (Univisión, Tijuana) (2004, 2005)

KPBS radio program "These Days" (2004, 2006)

CNN news broadcast (2000)