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GOVERNANCE AND PUBLIC FINANCE

IN THE SAN DIEGO/BAJA CALIFORNIA REGION

A DISCUSSION PAPER FOR
THE FORUM *FRONTERIZO* COUNCIL

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Introduction

In its series of discussions on San Diego/Baja California's global engagement, the Forum *Fronterizo* Council has considered a variety of topics and strategies. These discussions have addressed successful regional strategies employed in other areas for benefiting from the new global economy, the future of globally oriented high-tech manufacturing in San Diego/Tijuana, the trade infrastructure challenges facing Southern California and Baja California, and the prospects for greater regional partnerships between San Diego/Tijuana and their neighbors to the east and north. A common theme in these deliberations has been the need to strengthen existing systems of governance and public finance, as well as to create innovative new mechanisms, in order to realize the opportunities presented by globalization.

Governance, in this context, is more than the arrangements and processes of <u>government</u>. Rather, it is a set of public, public/private and private mechanisms for the region to chart and effect its global engagement. Central to governance is the process whereby public funds are raised and expended to enhance the competitive advantages of the region. In a cross-border region, governance must also include the ways in which federal, state and local perspectives are brought to, and reconciled with, decisions that advance the position of the region in the global economy.

This discussion paper examines the governance and public financing challenges related to our region's global engagement. It offers an overview of major governance and public financing reform proposals currently being discussed on both sides of the border and also reviews the current state of cross-border collaboration and planning. The paper gives particular attention to the asymmetries in the U.S. and Mexican governance and public financing systems, which hinder decision-making and cooperation and hence the region's ability to implement projects and compete globally. The paper concludes by calling for a more inclusive approach to governance, involving both public-sector and civic actors in implementing a joint strategy for global engagement.[1]

Preliminary Conclusions

The Council's discussions to date have revealed some of the new demands that globalization is placing upon regions. While many of these development questions would exist in any case, they are being put in stark relief through the impacts of globalization. These issues – which are briefly outlined below – help to define the governance challenges facing our region.

- *Developing a Regional Identity:* The Council's first briefing paper (Shirk 2000) pointed out the challenges of developing a regional consciousness and consensus in San Diego/Tijuana, especially since many San Diegans do not recognize the importance of existing and potential linkages with Baja California. The Council's consideration of the manufacturing opportunities for San Diego/Baja California (Curry 2000) revealed that the prospects for high-tech manufacturing in the region are constrained by the weakness of such a regional consciousness and cross-border networks. Council discussions have

[1] This discussion paper was prepared for the Forum *Fronterizo* Council by the staff of San Diego Dialogue, with assistance from David Shirk, Ph.D.. The staff of the Dialogue is solely responsible for its contents.

pointed to the need to encourage a regional consciousness as a precondition for catalyzing plans and actions to maximize the region's gains from globalization. However, there is no single effort or process dedicated to exploring our cross-border regional identity or raising regional consciousness.

- *West Meets East:* Another issue facing the Council has been the extent to which its definition of the region should be expanded to incorporate San Diego/Tijuana's eastern neighbors as partners for engaging the global economy. At the first Forum *Fronterizo* program organized as part of this initiative, NADBank managing director Victor Miramontes argued that the factors that constrain the San Diego/Tijuana region's growth – particularly water, land and housing– are readily available to the east. However, given Imperial County's participation in the Southern California Association of Governments and the relatively limited processes of communication and joint planning between Tijuana and Mexicali, it may be difficult to structure a joint west/east visioning and planning process using traditional approaches.

- *The Southern California Connection:* The Forum *Fronterizo* Council has looked north to greater Los Angeles and the rest of Southern California as both a possible model and a partner for global engagement. The analysis prepared for the Council of trade infrastructure (Erie and Nathanson 2000), for example, revealed a severe deficit in the San Diego/Tijuana region's transportation systems – airports, highways, ports and railways – relative to (and partly because of) the extensive infrastructure investments of Los Angeles. At the same time, important questions have been raised by the Council analyses (Erie and Nathanson 2000; Kyser 2000) about Los Angeles' ability to continue meeting the infrastructure needs (particularly in terms of airport capacity) of all of Southern California. While there are important new lines of public-sector communication between the region and our neighbors to the north, a cross-regional civic conversation is essentially non-existent.

The Council's forthcoming deliberations on equity and community development, as well as the related issues of education and environmental sustainability, are likely to pose similar challenges for governance in this diverse cross-border region.

Based on our research and discussions to date, the imperatives of globalization have prompted the following tentative conclusions, each of which raises its own set of governance issues:

1) ***The cross-border region should make complementary, and perhaps collective, investments in its transportation infrastructure.*** How are alternatives to be weighed and decisions arrived at regarding infrastructure development in San Diego and Baja California?

2) ***The region should build a technology-oriented employment base that is sustained by high value-added manufacturing capacity.*** How will a strategy be crafted and implemented to build higher value-added manufacturing on both sides of the border?

3) ***The region should reach out to the surrounding regions east and north of itself, in order to define its global engagement as part of a broader Southern California/Baja California context.*** San Diego/Tijuana's strategy for global engagement must be rooted in a Southern California/Baja California conversation regarding our macro-region's role in the global economy. How should this conversation be organized, and what institutions should take the lead in engaging our neighbors in greater Los Angeles, Orange County, the Inland Empire and Imperial Valley/Mexicali?

The Challenge of Governance

This section of the paper describes the major institutional reforms that are currently being considered for the region, on both sides of the border, and assesses their potential implications for the governance challenges posed by globalization. It also assesses the current state of cross-border collaboration in planning and development in San Diego/Tijuana.

Institutional Challenges in San Diego County

There are multiple layers of governmental institutions in San Diego County. In all, there are essentially four main forms of local institutions that operate in San Diego: county government, city government, special districts and voluntary governmental associations. Currently being contemplated are three major reforms that would alter existing structures for governance in San Diego: 1) regional transportation infrastructure reform, 2) fiscal reform and 3) municipal charter reform for the City of San Diego.

Reforming Transportation Infrastructure Decision-Making

<u>Background</u>: Special districts and voluntary regional associations make many public policy decisions in San Diego County. Special districts – such as the Port of San Diego – are units of government that deal with problems that extend beyond the territorial limits of city and county boundaries, such as water supply, air pollution, education, resource conservation, transit, and ports and harbors. In addition to special districts, the San Diego Association of Governments (SANDAG) is one of 25 metropolitan planning organizations (MPOs) formed in California by joint powers agreements. SANDAG was created in 1980; its board includes representatives from the County of San Diego and its 18 cities. SANDAG addresses water, energy, transportation and housing issues and serves as San Diego's Regional Transportation Commission, Airport Land Use Commission and Regional Growth Management Board. Currently, transportation decision-making in San Diego County is divided between SANDAG and several special-purpose districts and agencies.

<u>The Problem</u>: While special districts and the metropolitan planning organization have developed specialized capacities in public policy-making, they also create a fragmented system of decision-making that slows and "clouds" decisions on transportation matters of regional significance. In particular, many critics argue that the siting, planning, development and financing of major

region-serving transportation facilities have been delayed and frustrated by San Diego’s current system of transportation governance.

A significant finding of the Forum *Fronterizo* Council’s research has been the relationship between San Diego's current governance structures and its historic challenges for trade infrastructure development. As Erie and Nathanson (2000) point out, San Diego has a trade infrastructure deficit partly resulting from the way governance has been organized in the cross-border region: "Airport, port and rail development decisions are made by limited purpose special authorities – the Port District and the Metropolitan Transportation Development Board – rather than by centralized city agencies as is the case in Los Angeles, Long Beach, San Francisco and Oakland" (p. 5).

San Diego's port, rail and airport decision-making is divided among different agencies with limited jurisdiction and authority. Air transportation provides an example of this fragmentation; while SANDAG is responsible for regional airport planning and site decisions, the Port District manages Lindbergh Field and the City of San Diego is responsible for Brown Field. San Diego has begun to make progress in addressing its trade infrastructure problems, thanks to active cooperation between the Port District and SANDAG. However, in an era of global competition, in which world-class multimodal transportation systems are a critical determinant of regional competitiveness, today’s dispersed processes of governance may still constrain the region’s global engagement.

<u>Options</u>: A recent legislative initiative – California Senate Bill 329 – seeks to provide a permanent institutional solution to San Diego's regional infrastructure planning and governance challenges. SB329 would create a regional entity to be known as the Regional Infrastructure and Transportation Agency (RITA). RITA would consolidate at least six different state-created local government entities and their functions by taking over the planning functions of SANDAG; the multiple planning, development and management roles of the San Diego Unified Port District (SDUPD); the transportation management authority of the Metropolitan Transit Development Board (MTDB) and the North County Transit Development Board (NCTDB); the air quality functions of the San Diego Air Quality Management District, and the financing powers of newly created infrastructure districts along the U.S.-Mexico border.

What are the potential benefits and costs of RITA? RITA's supporters claim that the consolidation of transportation decision-making will allow for full and complete debate and weighing of major transportation options facing the San Diego. They argue that by creating a single “center of gravity” for transportation policy-making, with clear lines of authority and responsibility, RITA will accelerate and regionalize the development of effective transportation systems. This will have a direct benefit for San Diego’s global engagement by expediting the flow of goods and business travelers to, from and through the region and will also indirectly benefit our global competitiveness by preserving and enhancing the quality of life in the county.

Critics assert that the focus of RITA's elected officials would be on the short-term interests of voters in their respective districts (e.g., more roads and better public transportation), rather than on larger regional goals (e.g., airport or port development). How the electoral districts are drawn and how the officials are elected will have an important impact on the degree to which RITA’s leaders incorporate regional perspectives into their decision-making. Equally important will be whether the various funds managed by RITA are co-mingled or are kept separate and distinct, as the agency tries to achieve its priority objectives.

Detractors also note that RITA confers no new land-use authority. While the border infrastructure zones included within RITA may assist in the development of trade-enabling infrastructure directly along the Mexican/U.S. border, the agency will not be able to unilaterally site and develop major new region-serving facilities. This means, for example, that the new agency would lack the power to create a new airport at possible sites such as Miramar, Otay Mesa or south Camp Pendleton.

Fiscal Challenges for San Diego County

Background: In recent years, public officials and non-governmental organizations in California have urged reforms to increase the fiscal capacity and change the revenue generating incentives of local governments. Many of the challenges facing local governments are the result of the unintended consequences of Proposition 13, approved by the voters in 1978, which limited property tax rate increases. This caused local governments to rely increasingly on other forms of revenue, particularly the sales tax. One such unintended consequence has been the "fiscalization of land use," in which local governments make planning decisions based not on what is best for the community, but on what kinds of development will produce the most revenue for local government coffers. In particular, city governments have had financial incentives to prioritize the development of commercial zones and retail establishments over other much-needed types of development, such as housing or office complexes.

The Problem: It is becoming more and more apparent that a region's quality of life is a crucial factor in attracting and retaining high-value-added economic activity. In San Diego County, as in other high-technology centers such as Silicon Valley, threats to quality of life such as rising housing costs, increased traffic congestion and the loss of open space are perceived to be a significant risk factor for future global competitiveness. San Diego now ranks among the least affordable housing markets in the country. Traffic congestion has increased markedly in recent years, at least partially because of commuters who are forced to live farther and farther from their work in order to obtain affordable housing. To improve our quality of life, reform advocates call for a package of "smart growth" strategies that expand the supply of housing, locate housing closer to jobs and encourage the use of public transit. However, many analysts note that such strategies will only be feasible if the state-local fiscal relationship in California is restructured.

Options: While there are institutions and groups that benefit from the status quo and the familiarity of existing arrangements, a significant fiscal reform movement has been initiated in California. Most importantly, in 1998 the California legislature formed the Speaker's Commission on State and Local Government Finance – with a diverse professional and civic membership – to recommend viable fiscal reform measures. The general recommendations of the Speaker's Commission were:

1. *Diversification of Local Revenue:* "[T]o change the mix of revenues available for local services by increasing local reliance on property tax and decreasing reliance on sales tax."

This could mean swapping state-controlled revenues for local dollars, such as transferring 5 percent of the county government's share of sales tax to the state government in exchange for a larger share of the property tax (as recommended by SANDAG).

2. *Regional Governance Structures:* The development of a process for "state, regional and local growth and development policies and a governance structure that connects fiscal powers with roles and responsibilities" (Villaraigosa 2000).

These recommendations (detailed in the Speaker's Commission's *Final Report* [March 2000]), as well as those of SANDAG (found in its bulletin *Achieving Fiscal Reform* [December 1999]), seek to provide a balance between conservation, development and fiscal policies. Such a balance could benefit the region by helping to preserve the unique quality of life found in San Diego County, a key asset for the region's engagement with the global economy.

Reforming San Diego City Government

<u>Background</u>: San Diego municipal government features the council-manager system of government, which has been in place since 1931. The city council includes the mayor, elected at large, and eight council members who represent individual districts. The mayor presides over the city council and has the power to vote on, but not to veto, council legislation. The mayor and city council are responsible for selecting and overseeing the city manager, who in turn appoints the heads of most of the city's administrative departments.

<u>Options</u>: The alternative to the city manager system, now under debate, is the mayor-council form of government. In the mayor-council system, governmental functions are divided between an executive (the mayor) and a legislative body (the council). The mayor has direct authority over the city administrative officer and municipal agencies.

Either as provided by charter or state law, some mayor-council systems provide the mayor with more power than others over budgets and appointments, hence producing differences between so-called "strong" mayor models and "weak" mayor models. Advocates of mayor-council government argue that it makes elected government officials more accountable to voters and is a more effective form of government for administering large, diverse metropolises. For example, while most small city governments in California employ the council-manager system, both Los Angeles and San Francisco have relatively strong mayors (though not as strong as many mayors in Eastern cities).

Recently, prominent San Diegans have begun to campaign for a mayor-council system, with powers and resources to strengthen both the mayor's office and city council. Proponents assert that strengthening the mayor would help to consolidate a broader vision for San Diego by increasing the authority and voice of a public official with a more regional constituency. Under the charter proposal currently being debated, the city manager position would be directly subordinated to the mayor and the city council would hire an independent budget analyst.

Advocates of a stronger mayor system argue that an office with enhanced authority can better advance regional interests and projects, such as a new airport. They suggest that not only will a strengthened mayor represent broader regional interests, but that the office can more effectively bargain with other governmental agencies and officials at the regional, state and federal levels. This stronger position could allow the mayor to play an important role in defining and spearheading new initiatives to enhance the cross-border region's global competitiveness.

Building Local Government Capacity in Baja California

Strengthening Municipal Government

Background: Tijuana is one of five municipalities in Baja California. State laws mandate that each local government be composed of a mayor, an internal supervisor (*síndico*)[2] and a predetermined number of city council representatives. Tijuana's 15 city council members vote on policies implemented by the local government and serve on committees (*comisiones*) that oversee municipal agencies and make policy recommendations on a range of issues. The mayor's office of Tijuana concentrates its efforts in three main areas: public safety, public works and services, and social policy. As in other municipalities in Mexico, Tijuana's local government has limited jurisdiction and administrative capacity to deal with the many problems it faces. Historically, decision-making authority has been highly centralized under the federal executive branch and, to a lesser extent, in the hands of state governors.

Some positive changes over the last decade have encouraged more effective public administration at both the state and local level. In 1998 and 1999, the Mexican legislature enacted reforms to promote greater municipal autonomy by allowing city councils to make extended commitments beyond their terms of office and to clarify municipal entitlements and obligations. Also, in Baja California, state and local government lobbying of the federal government has wrought concessions to decentralize responsibility for a variety of policy areas, including potable water services, rural transportation infrastructure, public education, planning and land tenure regularization. The state government has also worked to decentralize important responsibilities to the municipal governments, including the transfer of property assessments, the management of locally generated revenue, and greater responsibility for infrastructure, education and health services. Greater local control over municipal revenue generation, in particular, has led to dramatic increases in the collection and efficiency of local fees and taxes.

The Problem: Despite recent progress, local governments in Mexico remain fiscally weak and heavily dependent on state and federal transfers of funds. The fiscal weakness of municipal governments directly affects the administrative professionalism and level of service provision in Tijuana and other municipalities in Baja California. While these northern cities are years ahead of local governments elsewhere in Mexico, they remain decades behind major U.S. cities like San Diego and Los Angeles. There are few institutions in Mexico – let alone Baja California – for technical and administrative training to develop a truly professional civil service. Moreover, the limited budgets of local governments in Mexico make it difficult to attract talent away from

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[2] An elected position meant to ensure internal supervision, *síndico* combines functions similar to those of a local auditor, attorney general and independent council.

the private sector. The access of many public officials and administrators to modern technologies such as computers and the Internet is still very limited.

Effective governance in Baja California is also challenged by rules that prevent the reelection of elected leaders. The revolutionary principle of "no reelection," which is imbedded in the Mexican Constitution, prevents the immediate reelection of all municipal elected officials. While this tends to prevent demagoguery, "no reelection" has at least two very detrimental effects. First, it reduces the incentives for accountability to local constituents, a problem exacerbated by the fact that city council members are elected "at large" rather than from individual districts. Second, single three-year term limits make for an excessively short time-horizon for all city council members; this also leads to high turnover rates among other local government functionaries as new appointees are brought in from one administration to the next.

The lack of technical capacity in the civil service, limited accountability and the absence of long-term planning horizons all serve to constrain Baja California’s capacity to plan for its global engagement. As a result, it is difficult to prepare, launch and complete local projects that would improve the competitive advantage of Baja California. It is also very challenging to partner with agencies and institutions north of the border on cooperative, region-serving initiatives.

<u>Options</u>: Multiple options have been presented for strengthening the capacity of municipal governments in Baja California. These range from reforms that would need to be enacted by Mexico’s national legislature, including amendments to the Constitution, to local efforts that could be pursued on a cross-border basis. Among the reform alternatives are the following:

- Eliminate the “no reelection” rule. Proposals to end single term limits for legislative and local governmental offices were eliminated from recent constitutional reforms passed by Mexico's legislature. However, this issue is likely to remain a key point of debate for the foreseeable future. The elimination of single term limits for local government officials in Mexico could enhance the quality of governance and facilitate cross-border cooperation.

- Increase cross-border training and technical exchange programs. San Diego public officials might help to improve the effectiveness and professional capacity of its regional partners in Baja California if they could increase the number and scope of cross-border exchanges and training programs open to participation by Baja residents. Such programs could provide training in public administration, planning, municipal finance and related technical services.

- Many analysts argue that an overall acceleration of the devolution of powers to state and local authorities in Mexico would increase the capacity of Baja California to manage the stresses of globalization. This is particularly true in the areas of public health and environmental pollution, where local capacity is swamped by the scope of the developmental challenges faced by the state’s rapidly expanding population.

Building Baja California's Fiscal Capacity

The Problem: Perhaps the greatest challenge to achieving the cross-border region's shared goals for engaging the global economy will be to find ways to overcome the severe fiscal limitations of local governments on the Mexican side of the border. Building globally competitive trade infrastructure, assuring a stable water supply and grappling with the externalities of globalization will require local government in Baja California to be able to finance projects, either independently or in collaboration with San Diego and/or multilateral partners. Among the significant financial limitations faced by Baja California's governments are the following:

- ***Local Revenue Generation:*** Recent federal and state initiatives to allow for fiscal decentralization and greater fairness in the transfer of revenues to local governments, as well as important changes in municipal revenue generation, have helped to increase the size of municipal budgets in Mexico. In many cases, increased electoral competition has led public officials to attack corruption, increase efficiency and even raise taxes to ensure better governmental performance in the delivery of public works and services. Nonetheless, Mexican municipalities have a long way to go to develop fiscal bases that will enable them to meet their development challenges and fully cooperate with their U.S. partners. Current impediments include the continued concentration of value-added tax (IVA) revenue at the state and federal levels, and the inability of local governments to raise their own taxes without state congressional approval.

- ***No Bonding Authority:*** An additional constraint on financing public projects at the local and regional level in Mexico is that there is no legal or practical system for sub-national (state and local) public entities to issue bonds. In the United States, large public or private projects often have access to long-term sources of financing in the form of municipal bonds or public activity bonds. Yet, in Mexico, city governments – lacking a solid revenue base – are without strong credit ratings and hence cannot access long-term capital markets. Appendix I, which was provided for this paper by Sempra Energy, provides an additional discussion in outline form of the challenges of financing infrastructure projects in Mexico.

- ***Constraints on Borrowing Foreign Capital:*** Some public entities in Mexico – such as states and municipalities – are constitutionally restricted from accepting direct loans from foreign sources. This – combined with the prohibitively high interest rates and discretionary power of Mexican public lending institutions – dramatically limits the potential of state and local public officials to engage in large-scale public works projects and cross-border collaboration. However, there are some exemptions to these restrictions, notably the North American Development Bank's *Corporación Financiera de América del Norte, S.A. de C.V.* (COFIDAN), a corporation partnered with the Mexican treasury (*Secretaría de Hacienda y Credito Público*, SHCP). As a limited-purpose, Mexico-based lending institution, COFIDAN – in conjunction with the Mexican foreign exchange hedging mechanism (FOAEM) – can make direct loans to projects south of the border, allowing state and municipal governments to accept more competitive interest rates.

- ***Long-Term Financing*****:** Most Mexican entities lack ready access to the sort of long-term external finance that is critical to major infrastructure projects. However, Mexico traditionally has had access to long-term finance through the multilateral development banks (the World Bank and the Inter-American Development Bank) and official export credit agencies (the U.S. Export-Import Bank and its European and Japanese counterparts). These sources are more disposed to lend to projects in regions whose economic outlook promises solid prospects of timely repayment.

Options: Several reform alternatives have been proposed to help build and expand the financial capacity of local governments in Baja California. However, this is an area that still requires concentrated attention and significant creativity from civic and political leaders on both sides of the border. Among the most promising ideas suggested to date are:

- Encourage state and local governments to cooperate with the newly emerging system for pension funds in Mexico to help finance bonds.

- Encourage reforms in Mexico's growing private pension system, which could develop as a major market for bonds in the future.

- Expand NADBank’s capacity to lend to state and local governments, which would enhance their abilities to finance vital projects.

- Explore the use of U.S. dollar-denominated financing instruments by Baja California institutions to help support projects that will generate dollar, or dollar-based, revenues.

- Develop governance structures, and credible regional strategies and plans, to succeed in the global economy. With a proactive strategy and strengthened capacity for cross-border governance, San Diego/Baja California could enhance its access to long-term finance from official multilateral and bilateral sources.

Cross-Border Planning and Collaboration in San Diego/Baja California

The usual barriers to effective cross-jurisdictional planning on a regional basis are exacerbated between San Diego and Baja California by the presence of a federally controlled international border. While these unique challenges have been recognized for decades, and have been the focus of considerable attention over the last seven to 10 years, many would argue that we have yet to find an effective mechanism for ongoing cross-border planning and collaboration. Local government officials on both sides of the border remain limited in the extent to which they can cooperate with their neighbors by centralized frameworks for decision-making. For example, federal control of customs and immigration functions means that local communities are not empowered to reduce the border-crossing inefficiencies that prevent stronger economic linkages between San Diego and Tijuana.

Background: A range of pragmatic strategies for trying to plan and administer the border region has evolved in response to the dynamic changes spurred by regional integration. These strategies were created to deal with the accelerated pace of regional integration in the 1990s, although they were shaped by the constraints of the larger bilateral relationship between Mexico and the United States. In response to demands created at the regional level, a variety of formal and informal institutional mechanisms have been created for the development and administration of the zones along the Mexican/U.S. border. The primary legal framework for the creation of these new cooperative mechanisms has been the Border Liaison Mechanism (BLM.)

The BLM was created in 1992 through a diplomatic protocol adopted by the U.S. State Department and the Mexican Secretariat of Foreign Relations. The BLM mechanism allows for binational agency coordination at a local level without routing communications through the capital cities. BLM meetings are supposed to be held on a quarterly basis and are directed by the respective consuls-general of the border sister-cities. The BLM mechanism allows for the convening of representatives of federal, state and local government agencies, as well as civic stakeholders, on both sides of the border. These meetings are intended to provide a medium for local authorities to discuss regional issues and create proactive strategies for addressing regional problems.

The main purpose for the creation of the BLM was to prevent day-to-day administrative difficulties at the border from escalating into international crises. Prior to the establishment of the BLM, problems that emerged at the border would be responded to from the capitals, frequently through diplomatic notes. This method typically was not an effective or efficient response to time-sensitive problems. Moreover, relatively minor regional issues had the potential to become major points of conflict in the larger bilateral relationship. The BLM was established as a vehicle for regular communication on a variety of issues of common concern between local agencies on both sides of the border.

In the case of San Diego/Tijuana, the general BLM acts as an umbrella for a series of issue-specific working groups, which include groups focused on public safety, migration, water supply and the operation of the land ports of entry. The degree to which these groups have evolved into successful mechanisms for cross-border collaboration has varied. The working group on the land ports of entry, for example, has stagnated in recent years, even as concerns continue to be voiced about the impact of border wait times on regional economic development. The working group on water supply, by contrast, has made rapid progress in defining joint solutions to the region's water supply challenges, including preliminary planning and feasibility studies for the construction of a binational aqueduct.

The BLM process has also facilitated the growth of informal cooperative mechanisms in areas where more formal processes are precluded by the bilateral relationship. For example, in San Diego/Tijuana, government agencies have developed a Memorandum for Mutual Assistance, which provides guidelines for action in the case of emergencies but does not require signatures from the participating agencies. This document delineates how the agencies would respond in case of fire, floods and special emergency situations. An early version of these processes proved effective in the winter of 1998, when heavy rains and flooding in Tijuana required the quick transfer of special heavy equipment (e.g., earthmovers and similar types of machinery) from San Diego.

The Problem: While the BLM and other informal processes of collaboration have been effective vehicles for addressing short-term issues facing the border region, they have not evolved into sustainable forms of binational regional governance. There has been an ongoing tension over whether the BLM is a problem-solving vehicle or a mechanism for long-range planning. In San Diego/Tijuana, government officials have tended to view the BLM as a tool for the resolution of minor disputes and as a vehicle for information-sharing. Many civic leaders, on the other hand, have hoped to use the BLM for binational regional planning.

Real concerns remain regarding the absence of institutionalization for these new vehicles for cross-border collaboration. Local participants stress that the BLM mechanism only provides an opportunity for cooperation, and that local agency participation in these processes is still voluntary. Some local stakeholders fear that these cooperative mechanisms may only be temporary and are still too reliant on individual personalities and personal relationships. The realities of globalization may justify a more aggressive approach to cross-border planning and development than has been adopted in the past.

Options: Two main options have been proposed to enhance cross-border collaboration in planning and development. While to some degree these options are dependent on progress being made in the individual areas described above, they remain worthy of further exploration in order to strengthen the region's capacity to engage with the global economy:

1) Create an independent cross-border planning and development authority that possesses its own bonding capacity. Members of San Diego Dialogue first proposed this idea several years ago. At the time it faced significant opposition from several quarters; however, it is worth noting that less aggressive mechanisms for cross-border collaboration have not yet produced substantial results.

2) Develop public–private partnerships around specific issues and projects in which the private sector takes the lead in project development and securing project financing, while the public sector's role is limited to bond guarantees in order to reduce the cost of capital. Some discussions around the development of a binational aqueduct are proceeding along these lines.

Conclusions: A Role for Many Sectors

With multiple interests and organizations eager to strengthen the region's engagement with the global economy, San Diego/Tijuana needs to develop a consensus about how citizens can best work together toward shared goals. This requires the region to address tough questions about the roles of government, the private sector, non-governmental organizations and the community at large in charting the integration of the region into the new global system.

- *Public vs. Private Sector:* The role of government in an economy is one of the most divisive and pivotal questions of political ideology around the world. Some say government should limit its role in the economy so that business can respond effectively to market demands, while others see government as a catalyst for business and a protector from the negative externalities of excessive market competition. Clearly, there is a middle ground in which compromises can be made between these two positions. Public-private partnerships (PPPs) help to generate broad consensus and to overcome fiscal challenges that can be overwhelming for either government or the private sector on its own. PPPs have become a common part of the discourse of economic development and can play an important role in San Diego/Baja California's global engagement.

- *Non-Governmental Organizations (NGOs):* Many non-governmental organizations and associations have embraced the reality of cross-border regional integration, yet there are relatively few truly binational civic networks between San Diego and Tijuana, let alone between our region and potential partners to the north and east. More could be done to expand civic life across the border by investing in the capacity of NGOs and associative groups to maintain an ongoing binational civic identity. NGOs could also take the lead in developing a macro-regional visioning and planning conversation that assesses the role of Southern California and Baja California in the global economy.

- *The Media:* News media organizations in the cross-border region can take a more active role in helping to promote regional consciousness. Existing efforts by some organizations to make their programs and publications more accessible through a bilingual format is an important step in the right direction. However, the region would also benefit greatly if the media increased the depth of their attention to critical issues related to globalization, regional integration and an emerging binational regional identity.

- *The Community:* Community participation is needed in developing San Diego/Tijuana's regional strategy for global engagement. However, once a general consensus has been established, the community must be able to entrust decision-making authority to policy-makers who will not bow to excessively local concerns or parochial interests. Thus, the first step is to encourage the community to "think regionally" and to participate in developing the region's larger strategies for development. The next step is to develop institutional mechanisms to see those strategies through.

Next Steps

The Forum *Fronterizo* Council's research papers and dialogues have suggested that the successful global engagement of the cross-border region requires a critical reassessment of our existing structures for governance and public finance. The institutional and fiscal reform opportunities described in this paper may represent a necessary, but not sufficient, set of conditions to ensure the region's successful global engagement. Even if all of the potential reforms are enacted, the region may be no "smarter" about its global engagement strategy than it is today. Ultimately, both civic and political leadership will be required to take advantage of the opportunities afforded by globalization, and true governance will mean collectively pursuing a set of strategies to secure a better position in the global economy.

The Forum *Fronterizo* Council might begin such a process by exploring the challenges of governance through the formation of a smaller working group. Such a working group could give special attention to three issues raised in this paper: 1) partnering with the other regions of

Southern California, 2) pursuing a joint development strategy with the Imperial Valley and Mexicali, and 3) advancing our progress in the area of cross-border planning. If a set of constructive, specific recommendations can be crafted by this working group and endorsed by the full Council, it will provide a roadmap for future action by civic and elected leadership from both sides of the border.

Appendix I: Infrastructure Financing in Mexico

[*Prepared and provided by Sempra Energy*]

Background/Introduction

- Infrastructure encompasses assets with long lives (toll roads, ports, wastewater treatment plants, water/sewage facilities, power plants, etc.).
- These types of assets are politically, socially, and economically sensitive (i.e., price of water, tolls, cost of power, etc.)
- Tariffs for use of these assets are usually regulated.
- To finance these assets you need long-term (longer than 15 years) and relatively inexpensive financing.

Infrastructure Financing in the United States

- In the United States, large viable public or private projects usually have access to long-term sources of financing in the form of municipal bonds, public activity bonds, other long-term capital markets instruments, and long-term bank financings
  - Examples:
    - The Gillespie Field Port Project in San Diego was financed by a 25-year revenue bond
    - Kings River Power Project in California was financed by a 37-year revenue bond.
    - Sweeny Power Plant (335 MW gas-fired facility) had a 22-year tranche of debt
    - Municipal water authorities can access 30-year financing for upgrades at very attractive rates. The San Diego Water Authority has at least 10 bond issues outstanding at those tenors.

Issues Related to Financing in Mexico and Other Emerging Markets

- The situation in Mexico, where infrastructure needs are great, is much more challenging than in the United States.
- There exists a lack of local long-term sources of financing – no municipal finance is readily available. States and municipalities have limited access to financing for infrastructure projects. Development banks have limited funds, and what they do have is mostly earmarked for smaller infrastructure and more social programs.
  - Example
    - Banobras, a national development bank in Mexico, provided a guarantee of payment by the local utility in Chihuahua, Mexico. This guarantee was instrumental in making it possible to secure financing for the construction and operation of a municipal wastewater treatment plant. Financing amounted to US$9 million in debt. Tenor of the debt was eight years.
- There is also lack of ready access to long-term external sources of financing
  - The international capital markets are only available to the sovereign and top-tier corporations (for the most part, tenors are for a maximum of 10 years)

    - Uncovered (no political risk) bank market is limited to five to eight years at the maximum
        - Example
        - Private sector parties were able to secure eight-year-term limited recourse project financing for the construction and operation of industrial wastewater treatment plants for Pemex.
- Political risk in the form of expropriation, political violence and convertibility of local currency for hard currency causes investors to shy away, shorten tenors and /or increase pricing. Political risk insurance is available but at expensive rates.
- Additionally, there is foreign exchange risk. Revenue for most of these projects is in local currency, while the cost and servicing of the debt is in hard currencies. There is also no market for long-term currency hedges, given historical volatility.
- There also exists regulatory risk. Regulations related to public services are sometimes lacking or unclear, making certainty of revenue for infrastructure projects a major risk.
- Furthermore, there are certain legal issues that make it difficult to finance infrastructure projects. One of the more prominent ones is that the nature of public services for these projects makes it difficult to take a security in the assets as collateral for loans.
- Last, but of great importance, is the issue of the creditworthiness of the revenue source. As an example, if a wastewater system is serving a small community in Mexico, the residents of the community may have a difficult time paying for the services, making it very difficult to finance.

Sources of Long-Term Financing for Infrastructure Projects in Mexico and Other Emerging Markets

- Multilateral banks (InterAmerican Development Bank, International Finance Corporation, Export Development Corporation of Canada, etc.) and exports credit agencies (U.S. Exim Bank, COFACE – France, Hermes – Germany, etc.) can and have provided long-term sources of financing with their various programs (A/B loan structure, political risk insurance programs, etc.).
- Examples:
    - Energia Mayacan Gas Pipeline: Tenor of debt was 12 years. The multilateral involved was the InterAmerican Development Bank.
    - Rio Bravo Power Plant. Debt was provided in three tranches: tranche A’s tenor was 12 years, tranche B’s tenor was 14 years, and the smallest tranche’s (tranche C’s) tenor was 16 years. The multilateral involved in this transaction was IFC.
- Until Mexico has a solid municipal finance system or until the country risk strengthens to the level necessary for long-term capital sources to feel comfortable in investing there, these multilateral sources are, for the most part, the only deep sources of financing available to infrastructure in Mexico.

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