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COUNCIL OF ECONOMIC ADVISERS
WASHINGTON

October 27, 1975

ALAN GREENSPAN, CHAIRMAN
PAUL W. MACAVOY
BURTON G. MALKIEL

MEMORANDUM FOR THE PRESIDENT

Subject: An Economic Analysis of the New York City Financial Crisis

New York City, with approximately $1 billion of expenditures each month, is now to the point that its revenues fall short of current and capital expenditures even without including the costs of service on its debt. The City needs more income to pay policemen and firemen and to continue capital improvement projects. This income in recent months has been forthcoming from issuing new debt. But unless additional financial resources are found the City will default and stop debt service payments in December. At that point the funds for current expenditures will also be insufficient.

This memorandum provides an economic analysis of the financial crisis in New York City. The question is how the present financial problem evolved over the last ten years -- what were the political and economic decisions that resulted in deficit operations. Proposed solutions to the crisis are reviewed and analyzed in the concluding section of the memorandum. The analysis makes clear that it is unlikely that the various "plans" now offered contain the solution to the crisis without Federal legislation.

1. The Present Financial Condition of New York City

The City of New York expects to receive from tax sources, welfare aid, and other State and Federal aid, approximately $906 million per month for the last nine months of this fiscal year. The expense budget calls for expendigures of approximately $903 million per month. Capital outlays, some of which are in reality current expenses, exceed $100 million per month. Without including debt service, the deficit in current and capital account should be $98 million per month. This deficit will probably be exceeded, however, because the expense budget may underestimate actual outlays if the new State plan is not enforced. The City Comptroller testified before the Senate Banking Committee on October 24th that revenues will fall short of expected expenses by $1.2 billion for the period December through March of 1976 alone.

Additional outlays are necessary to maintain the capital budget. The amounts required in the rest of this fiscal year are expected to exceed $50 million per month for repayment of principal and interest and for maintenance of currently budgeted capital improvement programs. Even if debt service is suspended, the City will need as much as $500 million to $1 billion in the next three to six months to meet expenses related to capital projects.

Mayor Beame and the Emergency Financial Control Board have adopted a three-year financial plan to attain a balanced budget for the fiscal year commencing on July 1, 1977. This plan is designed to achieve an end to the deficits, by reducing the rate of expenditures by $200 million in this fiscal year, $300 million more in fiscal year 1976-1977, and $300 million more in fiscal year 1977-1978. At the same time the capital budget is to be cut from $1.7 billion to $1.1 billion, with operating expense items in the capital budget reduced by $350 million per year.

This plan does not promise a solution to the problems created by the debt service deficits in the next few months unless investor confidence is restored immediately. The State of New York plan to deal with debt service needs calls for the State purchase $450 million of City notes this month. This would seem to be achievable even if some outside sources of money have to be obtained by the State to provide the needed amount. But it is highly uncertain whether the State can provide the funding necessary to complete debt service and meet payrolls in the capital budget items after December. The most likely course of events is for the City to default on debt service in December even with the maximum possible assistance from the State.

In the next year, and in the long term, the solution to the financing problem is to balance City revenues and expenditures. For this to be done certain critical political decisions of the last decade have to be reversed. These decisions related to the City's reasponses to demands for more and better services, and to the City's methods of obtaining both tax revenues and borrowed funds.

Decisions on corporate taxation and rent controls were equally important because they reduced incentives for industry and housing to develop in the New York area.

2. Creation of the Fiscal Crisis

The current financial problems in New York City are the result of a process which has been going on for a decade or more. Recent economic conditions of course, have played a role in default at this time. Inflation has raised the costs of services, unemployment and recession have increased the needs for services. The recent record high interest rates have especially affected New York by increasing debt service costs on the extraordinarily large volume of short-term paper issued by this city.

The influence of the recession is shown in Table 1. Although the CPI increased by 9.3 percent from June, 1974 through June, 1975, the sales tax base for New York increased only 1.7 percent. This fact is important because New York City obtains more of its revenues from non-property taxes (57 percent as compared to 38 percent in 1972-1973) than do other metropolitan areas and thus the tax receipts are more income sensitive than those of most local governments. The unemployment rate for New York City has been greater than that of the nation as a whole, but the volatility of that unemployment has not been more marked. The number of welfare recipients has risen, but not markedly. The index for welfare recipients in fact declined from the 1972 high to levels 5 to 10 percent lower in 1974 and 1975. An influx of welfare cases as a result of the recent recession cannot be the cause of the financial poblems of the city. Consequently, general economic conditions in 1974-1975 can be said to have caused problems of New York City but not significantly more than those of the rest of the nation's cities. And the other cities did not experience New York's financial crisis.

New York City has been losing population and jobs (as shown in Table 2). The tax base has been disappearing as well (as indicated by deflating the sales tax base by the CPI for commodities).

The effect of these trends on the tax burden in New York City is shown in Table 3. Through fiscal 1971, taxes as a percent of personal income fluctuated within .4 percent of 7.7 percent, but then rose a full percentage point in 1971-1972. For fiscal 1975 taxes are 10.2 percent of personal income.

TABLE 1-- Measures of the Recession's Impact on New York City

Year		Unemployment Rate[1]	Welfare* Recipients[2]	Sales Tax* Base[3]
1970		4.8	101.5	78.1
1971		6.7	109.5	81.5
1972		7.0	112.9	NA
1973		6.0	106.4	91.9
1974		7.2	101.4	96.7
1974	June	6.9	100.0	100.0
	July	7.3	100.2	100.4
	Aug.	6.8	99.3	100.2
	Sept.	7.3	100.5	99.1
	Oct.	7.2	101.3	99.8
	Nov.	7.4	101.3	99.6
	Dec.	8.5	102.4	100.4
1975	Jan.	10.3	102.8	101.0
	Feb.	10.2	102.5	101.0
	Mar.	11.0	103.1	101.7
	April	10.8	104.3	102.0
	May	10.9	104.3	101.9
	June	11.7	105.0	101.7
	July	12.0		
	Aug.	11.0		

Sources:
1. New York State, Department of Labor
2. New York State Department of Social Services
3. Annual figures from New York State Department of Taxation and Finance. Monthly figures from Municipal Assistance Corporation

*Indexes use June 1974 as the base period (Sales Tax Base 100 = $1.6 billion; Welfare Recipients 100 = 949,000). Sales Tax Base is equal to the total value of sales subject to taxation. Index is based on a twelve-month moving average to eliminate seasonal effects.

The Welfare index includes recipients under the AFDC and home relief programs.

Table 2 -- Employment, Population, Welfare Recipients and Sales Tax Base, 1970-1975 (first half)

Year	Total Jobs Index	Private Sector Jobs Index	Population Index	Welfare Recipients Index	Sales Tax Base Index	Sales Base Deflat Inde
1960	94.5	98.4	98.6	NA	NA	NA
1970	100.0	100.0	100.0	100.0	100.0	100.0
1971	96.4	95.5	99.9	107.9	104.4	101.0
1972	95.1	94.2	99.4	111.2	NA	NA
1973	94.5	93.1	97.1	104.8	117.7	102.8
1974	92.4	90.4	95.8	99.9	123.8	96.6
1975	90.1	88.1	NA	102.2	129.9	94.8

Congressional Budget Office, "New York City's Fiscal Problem," calculated from Tables 3 and

Table 3

New York City Personal Income as Related to Taxes, Expenditures and Deficits

Fiscal Year	Personal Income $ B	Personal Income Deflated by CPI	Taxes $ B	Taxes as Percent of Personal Income	Municipal Expenditures % Personal Income	Municipal Deficit % Personal Income	Municipal Debt as % Personal Income
1963-64	27	29	2.0	7.6	NA	NA	NA
1964-65	28	30	2.2	7.9	12**	NA	NA
1965-66	29	30	2.2	7.3	13**	NA	NA
1966-67	31	31	2.4	7.7	14**	NA	NA
1967-68	34	33	2.6	7.8	16**	NA	NA
1968-69	37	34	2.8	7.6	15	.2	16
1969-70	39	33	3.0	7.5	17	1.8	17
1970-71	41	34	3.2	7.7	18	3.5	16
1971-72	43	34	3.7	8.7	20	2.5	21
1972-73	45	34	4.0	8.9	21	.9	21
1973-74	48	33	4.5	9.4	22	3.4	23
1974-75	50	32	5.1	10.2	NA	NA	NA

Source: CBO Table 5, and calculated from data found in Annual Report of the Comptroller, The City of New York, Fiscal Years 69-70 through 73-74, New York City: Economic Base and Fiscal Capacity Summary, Maxwell Research Project on The Public Finances of New York City.

* Excludes fees and charges, stock transfer taxes and nonresident income taxes.

** Not strictly comparable with data for later years.

At the same time municipal outlays increased more rapidly than the tax burden. Table 3 indicates the change which overtook city expenditures and debt in relation to personal income. While for the four years 1964-65 through 1967-69 city expenditures rose as a percent of personal income by three percentage points, for the 6 years ending in 1973-74 they rose 7 percentage points. Cumulative municipal debt relative to personal income rose as well.

The conclusion is that New York City experienced demographic and economic changes which led to a stagnating and then declining city economy. The changes eliminated the possibility that today's problems could be solved by tomorrow's growth. There was no longer an expanding economy on which more debt could be placed in expectation that future growth would make continuous funding of current deficits feasible. As the deflated personal income figures in Table 3 show, the City's economy was stationary in the late 1960's and early 1970's. This condition put a limit on revenues from tax sources. New Federal policy in the early 1970's reduced the expansive growth of aid programs at the same time. Thus income growth for the city was likely to be much lower than in some of the newer large cities in the South and West.

The pressures for expansion of expenditures did not abate, however. The demand for social and educational services for the poor were responded to by interest groups across the political spectrum. The momentum built up on the expenditure side was carried along by rising expectations for City services. In addition, the ability of the City's powerful unions to extract wage settlements, coupled with ineffective lower and middle management contributed significantly to the situation in which the City finds itself. The political process in New York City and the way in which the municipal government chose to postpone problems allowed the deficits to accumulate to crisis dimensions. The gap between what the City paid out and took in from tax and grant receipts exploded beyond levels acceptable in other cities.

The budgetary process which relates expenditures to revenues broke down in New York City and allowed the gap to be created. Controls that normally would have forced reconciliation between expenditures and receipts were loosened by the use of questionable accounting practices. The result of the slippage in management was to postpone the day of reckoning. The postponement made the problem worse because the deficit increased significantly. This made refunding not only a financial problem but also an operations problem because of the necessity to raise money to meet payrolls.

The fiscal practices which contributed to the City's ability to spend more than income are as follows:

(a) Borrowing on accounts receivable. In a number of instances, the City borrowed on accounts receivable that had little if any likelihood of being collected.

(b) Capitalization of operating expenses. Operating expenses have been put in the City's capital budget so as to reduce the need for tax levy monies in a given fiscal year. This practice grew to the point where it eroded the City's ability to finance capital improvements to its own physical plant. Further, this practice, while legal, inevitably cost the taxpayer 15 to 20 percent more each year because of the interest payments on the borrowed funds. In the 1973-74 budget, for example, the entire cost of the vocational education program (estimated at $148 million) was transferred from the operating budget to the capital budget through a technical loophole in the law.

(c) Underfunding pension costs. The City underfunded the entire pension program by holding to acturarial assumptions made in 1917 that imply short lifetimes for retired employees. In addition, the Fire Department Pension fund has been $200 million in arrears because of an impasse among members of the fund's Board of Trustees as to the respective responsibilities which the employees and the City should assume in making payments to liquidate the deficit. Despite these factors, the City took advantage of some questionable fiscal practices to use $125 million of "excess" income in the Employees Retirement System to balance the 1974-75 budget.

(d) Underfunding collective bargaining settlements. In each of the last two fiscal years the City has underfunded the cost of collective bargaining settlements by about $100 to $150 million annually. Essentially, the City assumed that contracts negotiated in one fiscal year, e.g., 1973-74, would not be settled until the following year, e.g., 1974-75. This allowed the 1973-74 costs of such contracts to be paid retroactively through bonds issued under the "judgements and claims" provision of the City Charter and the State Finance Law. The effect on relative expenditure levels in the following year, e.g., 1974-75, was to double count the cost of the collective bargaining increase as the amount allocated doubles to meet the base year (1973-74) salaries plus the second year (1974-75) cost increases. This practice has permitted the City to grant salary increases in excess of what they might normally provide since there is little effect on the City tax levy funds in the base year.

Decisions on budgetary practices were important, but not the only determinant of deficit operations. A number of key political decisions were made, including the following:

(a) Mayor Wagner in 1958 granted city employees the right to bargain collectively. This created what one of Wagner's advisers called "a powerful special interest group" able to influence elections and bargain effectively for salary and benefit increases beyond those in effect in other cities.

(b) Successive Mayors in the decade from 1965 to 1975 developed the practice of borrowing on short terms so as to cover budget deficits. On June 30, 1965 the city's short term debt was $526 million. By February, 1975 it had grown to $5.7 billion.

(c) Mayor Lindsay postponed decisions to balance budgets in both 1973 and 1974. More than $270 million of expense items were moved to the capital budget, contingency accounts were drained, and one year notes were "rolled over" a second year. As a result, between June 1973 and March 1975 short term debt increased from $2.5 billion to close to $6 billion.

(d) At a number of points each Mayor considered and rejected proposals to remove rent controls. These controls in the last few years have kept rents below operating costs for many owners, thus reducing property values for tax purposes effectively to zero. About 25 percent of city apartment buildings are in arrears on taxes. Of the 125 subsidized Mitchell-Lama projects for middle income residents, 90 are in various stages of default. Outright abandonment runs to 90,000 housing units per year. The incumbant Mayors depreciated the tax base for the sake of voter approval in the next election.

With these actions the New York City municipal government ceased to practice levels of fiscal restraint found in other city governments. The results are shown in Table 4.

Table 4
Revenues and Expenditures of New York City
(Millions of dollars)

Revenues	Fiscal Year 1969-1970	Fiscal Year 1971-1972	Fiscal Year 1973-1974
Real estate taxes	$1,831	$2,100	$2,489
General fund	2,012	2,752	3,379
State and Federal aid	2,433	3,370	4,123
Other	251	377	84
Total Receipts	6,527	8,589	10,075
Expenses			
Current (excl. debt)	6,420	8,088	9,997
Current and capital (excl. debt)	7,139	9,207	11,579
Net Surplus Before Debt Service	-612	-618	-1,504
Debt Service	221	325	474
Net Surplus after Debt Service	-833	-943	-1,978

Source: Annual Report of the Comptroller of the City of New York

Although significant gaps did not occur between current revenues and current expenses, this was in part due to large expansions in the capital budget and in debt service. Funding problems were postponed by shifting from current account into the capital account. The day of reckoning was postponed.

These practices allowed New York City to extend itself beyond other large cities in the magnitude of its expenditures. As indicated in Table 5, the per capita expenditures of New York City exceeded those of every other except Washington, D.C. (a special case because of its national capital status). After taking account of the fact that New York City provides its own school services while many other cities do not, New York is still operating beyond the levels of expenditure provided elsewhere. State of New York studies indicated that New York City expenditures in the early 1970's for all categories of city services exceeded or matched those in the other of the 10 largest cities on a per capita basis. Cities having higher per capita incomes did less, and took a smaller proportion of per capita incomes in local taxes. The New York style of public service was lavish and expensive.

3. Proposed Solutions to the Financial Crisis

After New York's financial difficulties became apparent, the State set up the Municipal Assistance Corporation (MAC) to do the City's borrowing and the Emergency Financial Control Board (EFCB) to oversee the City's spending. To avoid default in September, the State legislature approved a complex financial plan to use the State's credit to help the City raise \$2.3 billion to meet cash needs until December. The merging of State and City credit has caused investors to lose confidence in both governments. Prices for both State and MAC securities have dropped, raising the real possibility that the marketability of State securities may decline to the point where new debt issues will not meet both the City's and State's needs. Were this to occur, the State would be dragged to default along with the City. At the present time seven State agencies are in danger of defaulting unless they can raise a total of \$1.5 billion by June 30. Beginning in March, the State government has to find ways to borrow approximately \$4 billion in short-term funds primarily to supply State aid to local governments for welfare, school costs and other services.

To restore investor confidence and thereby prevent default by both the City and the State governments the City and EFCB have attempted to put together a plan to balance the municipal budget within three years. It is widely

Table 5

Comparison of Per Capita General Revenues for the Ten Largest U.S. Cities, 1966, 1970, and 1974

Cities with * Dependent School Population	Per Capita Total General Revenues				Per Capita General Revenues Raised from Own Sources				Percent of Total General Reve Raised from Own Sources		
	1966	1970	1974	Aver. annual % increase 1966-1974	1966	1970	1974	Aver. annual % increase 1966-1974	1966	1970	1974
New York City	$509	$838	$1378	13.2	$348	$454	$714	9.4	68.4%	54.2%	51.8%
Baltimore	335	618	945	13.8	184	285	373	9.2	55.2	46.1	39.5
Washington, D.C.	526	908	1520	14.2	385	581	840	10.2	73.4	64.0	55.3
Cities without Dependent School Population											
Chicago	132	183	319	11.7	105	139	218	9.6	80.1	75.8	68.3
Los Angeles	130	188	311	11.5	110	156	253	11.0	84.8	82.8	81.4
Philadelphia	166	276	457	13.5	142	241	321	10.7	76.1	87.1	70.2
Detroit	185	272	486	12.8	131	197	300	10.9	70.7	72.6	61.7
Houston	84	112	185	10.4	76	108	154	9.2	91.2	96.3	83.2
Dallas	89	142	260	14.3	87	137	220	12.3	98.5	96.0	84.6
Cleveland	127	194	370	14.3	100	170	253	12.3	76.5	87.4	68.4
Averages	$228	$373	N.A.	N.A.	$167	$247	N.A.	N.A.	73.4%	76.2%	N.A.

Source: U.S. Department of Commerce, Bureau of the Census, City Government Finances.

* Cities that operate school districts within the municipal budget.

acknowledged that the City's public payroll has to be reduced significantly, that City services have to be cut, particularly in the municipal welfare, hospital, and education systems, and some City agencies have to be abolished. It is also acknowledged that means must be found to increase City revenues, including raising sales tax rates. But encouragement must be given to business and industry to develop within the City so as to add to municipal tax receipts within existing corporate rates.

The plan is possible only if a significant initial expenditure reduction is made in the 1975-76 fiscal year. Mayor Beame and EFCB have proposed that the City government reduce expenditures from tax levy funds by $200 million over this fiscal year. This requires a redu ction of total outlays for services of $342 million (the difference being reductions in those services paid for by Federal and State funds). The proposed redu ctions occur primarily in welfare and other social services, and secondarily in education, hospital and police services. The important categories are shown in Table 6. Social services are cut the most, because $4 of reduction are required in Federal and State aid to achieve a $1 reduction in the City's own outlays.

These cutbacks require a reversal of City expenditure growth trends not likely to be achieved. Moreover, past patterns of decision making in New York imply that cutbacks, if achieved, may not be made in the most effective manner from the long run viewpoint.

-- The reductions in the educational and police serices are expected to come out of operating programs -- from the high school and community school districts, or from crime control -- rather than from support services where excess employment is the greatest.

-- The reduction in social services is attained primarily by cutting back on personnel which if across the board could have the effect of increasing overall welfare expenditures (as more people enter the welfare roles without being checked).

-- Health and hospital services are reduced by curtailments in hospital care in all the hospitals without actually closing down the most outmoded and inefficient hospitals.

These cuts will be objected to by the municipal unions and local community interest groups concerned with their

Table 6: Major Proposed Reductions in New York City Expenditures in 1975-1976

Agency	Total Reductions ($ million)	Reductions in Expenditures from the City's Own Tax Receipts ($ million)
Education	39	38
Police	20	20
Social Services	128	37
Environmental Protection	14	13
Health and Hospitals	39	12
Human Resources	10	10
All others	92	71
Total	342	201

own police, education and hospital services. They have not been achieved voluntarily by the City in the past, and they are not likely to be achieved by a City government in the future. The question is whether EFCB or succeeding agencies will be able to make these redu ctions and follow through in the face of strong union and local community pressure.

Long term cost reductions. There is no plan at this time that specifies the additional $600 million of reductions to be achieved in the next two fiscal years. Budget saving proposals have to be much more drastic than those outlined for the rest of this fiscal year. But any feasible plan would reduce further the police, fire and sanitation department employees that are still on the job. These would include sizable reductions in 3,500 supervisory jobs at the rank of sergeant or above in the police department, and in fire inspection positions. They would call for eliminating up to one-third of the employees of the sanitation department by means of a long-term capital enhancement program. The reductions would be the most difficult to obtain in the fire department and somewhat less difficult in the sanitation department, although significant capital expenditures would have to be made in new garbage collecting equipment. The changes required in thee sanitation department would be most likely achieved by contracting out garbage collection to private corporations able to borrow at lower rates in the capital markets and to operate at lower costs in collection.

The cutbacks require reductions in real income for those employed by the City. There is some doubt that substantial savings could be made from reducing real wage rates for both political and economic reasons. The municipal unions have threatened general strikes to protest extended wage freezes. Comparisons between salaries in New York and other cities indicate that New York's salaries are somewhat "out of line" with those elsewhere or in the private sector given that, although wages are comparable, fringe benefits are paid for entirely by the City so that wages net of health and pension payments are at least 10 percent greater. Fringe benefits and pension payments in New York City are well beyond those offered elsewhere. In addition to wages totalling $4.5 billion this year, the City will spend another $2.8 billion on fringe benefits and pensions. This constitutes 55 percent of the payroll, while in private industry the fringe-pension package averages 20 percent of the payroll. City workers receive four weeks vacation their first year on the job, and most have unlimited sick leave, personal leave days and a variety of other time-off provisions. The City pays the full health insurance costs of its employees and supports annunity funds for policemen, firemen and sanitation men (with total health and annunity expenditures of $100 million per year). Although it will be extremely difficult to curtail these fringe benefits, bringing expenditures under control will require that to be done. Most proposals stress that employees should pay a significant part of their own health insurance premiums, vacation periods should be reduced, and there should be an elimination of annuity payments. But these in effect constitute salary reductions which the unions say they will not accept.

In the longer period, the services extended to the City resident have to be reduced as well. Cutbacks in education, health, and welfare services would be a prime consideration. Particularly important is a cutback in the municipal hospital system -- an 18-hospital complex and related health care facilities that provides medical services for more than 2 million patients per year. The system costs close to $1 billion a year and has chronic deficits as a result of inefficient operations, low capacity utilization and expensive treatment in relation to charges. Last year the City experienced a deficit close to $334 million in that portion of the budget.

Proposals have been widely made to phase out or severely reduce the number of municipal hospitals. These plans have been opposed not only because the facilities provide health care particularly to the poor, but also because they are an important source of jobs to members of minority groups. Suggestions to close a hospital have provoked bitter protests among neighborhood residents fearing the loss of this resource and have touched off sensitive racial issues. Nevertheless, cost savings must be made and the most effective way is to reduce the number of small inefficient facilities. Eliminating hospitals has been a tentative municipal goal for years, but has been abandoned each time the issue is raised because of strong local community reaction.

Other City agencies will have to undergo drastic pruning. The City University system, by attempting to carry out policies of open admissions at the undergraduate level and full doctoral programs at the graduate level, has extended itself beyond its resources. Its annual expenditures of up to $600 million could be reduced by eliminating graduate training and by shifting the open-admissions program back to the high schools as a remedial education program. Tuition should be equivalent to that now being paid by State University students. In the long run the City University should be a division of the State University of New York, for cost reductions obtained by consolidation could be beneficial to both governments.

Plans for reducing welfare costs call for either shifting the costs to other governments or for eliminating the outmoded system now in operation. Most likely neither policy could be put into effect, and reductions in expenditures will be achieved only by more diligent surveillance of the caseload. This city's caseload is now close to 1 million, with slight increases likely in the next few years. State audits indicate that the proportion of ineligible people receiving welfare in New York City is close to 11 percent for the first half of this year. This is an increase from a preliminary report of 9 percent for the first four months, but is less than the 18 percent reported last year. Improved operations have to come from simplifying the error-creating regulations in the system.

The fact is that a solution to New York City's problems that relies on expenditure reduction is doomed to failure unless there is a restructuring in the way the City responds to the pressures of interest groups. Unless this is achieved the budget gap will not be closed. The gap that exists is not transitory because those with the power to make changes benefit from the status quo. "Business as usual," however fervent and well intentioned the efforts at expenditure reform, cannot suffice to put the City on a sound financial basis.

Increased City tax revenues. One of the means for balancing expenditures and revenues in the past has been to raise taxes. Yet as business taxes have been increased, companies have been driven from New York City. Further extensive increases in City corporate taxes will in the long run probably reduce revenues paid into the municipal government. Important policies for long-term stability include measures to add to the tax base rather than to reduce it.

First, corporate taxes should not be raised unduly. Recent studies indicate that the City is once again cost competitive in attracting corporations in certain industries. Because of large scale building of office space, rents on space for banking, communications, publishing, and other important industries are at levels competitive with those in other important metropolitan centers. If efforts are made to hold corporate tax rates down, the long term gains for the City itself may be substantial.

Second, an important step in encouraging additions to the tax base is to remove the City's archaic rent control law. Because landlords have not been able to raise rents to levels that cover costs, much housing has been abandoned. Tax delinquencies on real estate have been rising and reached $200 million in fiscal year 1975. Rent controls must be phased out and incentives provided to re-establish building programs and home-ownership in the City.

Additional income and sales taxes have to be levied on residents if they are going to continue to demand such extensive services. In addition to an 8 percent sales tax, a city income tax is levied on residents and to a lesser extent on commuters. City and State taxes for a New York family of four earning $15,000 a year now come to more than $650. While these amounts are large, they may not be out of line with the extensive services provided by the municipal government.

<u>Summary</u>

At the present time it does not seem likely that significant cost reductions and income increases are about to be realized. Budgetary balancing is still quite speculative.

The plan for a $200 million reduction this year is not more likely to be more successful than plans to achieve the same reductions in earlier years. Voluntarism by City or State officials in cutting back programs deemed important by local community groups or municipal unions had no previous success. Although the crisis atmosphere may generate some reforms, it is not possible to foresee immediate results from the Beame-EFCB plan. The interest groups still have considerable power. Although questionable financial practices have been eliminated, the results will be first the long-delayed bankruptcy.

The use of Federal funds to prevent bankruptcy would be no more successful in solving long run problems. A Federal bailout to prevent default would require more than $4 billion this fiscal year for refinancing debt and the capital program, and would require an additional $2 million to finance the operating deficits on current and capital accounts during the year. Without a reduction in expenditures, the Federal outlays would have to increase by $1 to $2 billion a year in the next few fiscal years. These amounts would be excessively large and inequitable in a period of Federal program reductions designed to obtain a more balanced Federal budget. The problem of expenditure and receipts control would remain.

Paul W. MacAvoy
Member

Alan Greenspan
Chairman

THE WHITE HOUSE

WASHINGTON

October 25, 1975

MEMORANDUM FOR THE PRESIDENT

FROM: JIM CANNON

SUBJECT: New York City

I asked Dick Dunham to come over this morning to discuss a possible resolution of the New York City problem.

Dick and I felt it would be appropriate for him to summarize his views for you, and a copy of his memorandum is attached.

CC: The Vice President
Mr. Rumsfeld
Mr. Hartmann
Mr. Seidman
Mr. Greenspan

THE WHITE HOUSE

WASHINGTON

October 25, 1975

MEMORANDUM FOR: JIM CANNON

FROM: DICK DUNHAM

SUBJECT: New York City

It is my recommendation that the Administration propose a new statute which would govern the situation in New York City. This statute should not use the words bankruptcy or default but would be called something like, "A statute providing for the reconstitution of municipalities' debts."

The main features of this statute would be:

1. It would parallel the existing Chapter 11 of the Federal bankruptcy laws.

2. It would reference the existing Chapter 11 in such a way that the existing state law which gave New York City permission to petition the Federal court under Chapter 11 could be used.

3. The essential feature would be that it would by-pass the existing provision of Chapter 11 which requires that permission of 51% of the creditors is required in order to effectuate a voluntary reorganization of debt. This feature would avoid the present problem of trying to find the note and bond holders and the fact that so much of the paper is in the form of bearer certificates.

4. On petition of the city, the Federal judge would authorize the reconstitution or conversion of the existing three billion dollars of short-term notes into the three billion dollars of long-term Big Mac bonds. The Big Mac authorization is now for a total of five billion dollars of bonds, of which two billion have been sold.

5. The court would designate the state Emergency Financial Control Board to act as trustee and/or enforcer of the three-year financial plan already adopted by that board this week and hold them accountable for accomplishing the balancing of the budget over a three-year period. You will recall that the three-year financial plan adopted by that board includes in its plan the assignment of sufficient revenues to finance the debt service on the five billion dollars of Big Mac bonds.

6. The purpose, therefore, of this statute would merely be to effectuate and legitimize the state plan which has already been adopted. This plan cannot be accomplished at the present time because of the inadequacy of existing Federal statues governing "bankruptcy of municipal corporations" and the failure of the financial community or investors to accept that board's plan and reopen the market.

7. There are two elements of the New York City debt situation that this plan would not solve:

   The first of these is the financing of the legitimate short-term cash flow needs of the city other than the accumulated three billion dollars of deficit mentioned above.

   There are two possibilities: First, if the Big Mac plan is in effect legitimized by this Federal statute and action of the appropriate Federal court, it is quite possible that the financial markets would be reopened to the city for legitimate short-term financing on a tax-anticipation basis of the city's short-term cash flow needs.

   Second, if this reopening does not occur, the statute could provide for the issuance of trustee certificates under the authority of the Federal court to get over the one, two or three-year period while the city budget is being balanced and the accumulated deficits paid off.

The Federal court would not have and, in my opinion, should not have, any direct enforcement powers over the management decisions required to accomplish the three-year financial plan and the budget actions necessary to accomplish that plan. The Federal court could, by statement or by its order, designate the Emergency Financial Control Board as its trustee or representative.

If, however, the trustee certificates mentioned above were used to finance the legitimate short-term cash flow needs of the city which, in normal course, turn over every 30, 60 or 90 days, it would get direct enforcement powers by refusing to permit the issuance of new certificates during the course of the period that they were needed.

8. The second problem that is not covered, as I understand it in either the three-year plan adopted by the Emergency Board or in this scenario, is the financing of the cash requirements of the capital budget. The capital budget has always been financed by 40-year bonds with the property tax as the basic and underlying guarantee. By virtue of the fact that the markets have been closed to all issues of the city of New York, the expenditures generated under former capital budgets are not now being financed on a long-term basis and therefore constitute a working drain on the current revenues of the city. This sum amounts to, on the average, about 1.5 billion dollars for each of the next three years.

If these actions discussed in this memorandum are successful and the market is reopened to New York City securities, the problem, of course, disappears.

It should be pointed out that the cash requirements of the capital budgets decrease quite rapidly over the next two and three and four-year periods and that capital expenditures discussed in this section were generated by authorizations of the last decade. The city and the state board have cut the capital budget extensively and, as I understand it, have not authorized any new starts.

Jim, this is not a completely staffed-out proposal and I do not know all the legal issues on either the Federal or the State side.

In addition, I would want to have some more understanding of the State's three-year financial plan for the city that I now have before it was finalized.

Therefore, please consider it an outline of a method which provides for an orderly bankruptcy proceeding without calling it that and thus may avoid more radical and undesirable Congressional actions such as guarantees.

[10-75]

QUESTION: What impact is the New York City financial crisis having on other large cities? If New York City defaults, will it precipitate defaults by other cities?

ANSWER: In the third quarter of this year, state and local governments raised a record \$13.5 billion in municipal bonds and notes. And in the last three weeks alone, average municipal borrowing costs, as measured by the Daily Bond Buyer index have dropped a full one-half percentage point.

With respect to defaults by other cities, such a risk would be presented only if such cities needed to borrow to pay off maturing debts. Very few cities finance in this way. And for those that do, the market will judge them according to their ability to pay. Amidst all the scare talk about the impact on cities in New York State, just last week Syracuse, New York sold nearly \$10 million in bonds. And the previous week Philadelphia, often cited as a city impacted by New York City's problems, borrowed \$75 million.

In short, those cities which are able to pay their bills will be able to borrow.

GLP per RA
Gerald L. Parsky
Assistant Secretary

Optional paragraph re seasonal cash flow financing for New York City:

This court authority will assure the funds necessary to meet seasonal cash flow needs for essential services. If New York State and City take appropriate actions, these borrowings should be saleable. The Secretary of the Treasury will be authorized to assure such marketability by providing Federal assistance if, in his opinion, short-term market conditions require such assistance. His authority will include the right to set such conditions as appear appropriate prior to such assistance.

I want to make it absolutely clear that I do not believe the Federal Government can or should be involved in providing financial assistance in the form of a bail-out to avoid default. To provide assistance in advance of default would merely protect the bond holders and remove any incentive the city's political leaders may have to restore fiscal integrity.

After default, it may be necessary, if state and local officials continue to refuse to accept responsibility for managing the affairs of the city, to provide sufficient assistance, IN CONJUNCTION WITH THE COURTS ~~through justice,~~ TO ~~for~~ maintain~~ing~~ essential services for the citizens of New York City. I believe we have to make a distinction between bailing out the bond holders and politicians on the one hand, and on the other, protecting the people of New York City from the consequences of the lack of courage which may be exhibited by their office holders.

Optional paragraphs concerning New York City to be inserted after first paragraph on Page 15 of the draft speech.

This court authority should assure the funds necessary to meet seasonal cash flow needs for essential services. If New York State and City take appropriate actions, these borrowings should be salable.

Out

~~I want to make it absolutely clear that I do not believe the Federal Government can or should be involved in providing financial assistance in the form of a bail-out to avoid default. To provide assistance in advance of default would merely protect the interest of the bond holders and remove any incentive the City's political leaders may have to restore financial integrity.~~

In the event of defalut, state and local officials would be required to accept responsibility for managing the affairs of the City, and to maintain essential services for the citizens of New York. If, however, the federal court finds that the borrowings are not salable because of a failure on the part of state and local officials to take appropriate action to bring revenues and expenditures into balance, the Secretary of the Treasury would be authorized at his discretion to assist the court by assuring the marketability of these short term notes. He would do this by purchasing the court approved short term notes, if in his opinion market conditions require such purchases, and after he has established stringent requirements for state and local government officials to insure the closing of the gap between revenues and expenditures.

In short, in the event of default, essential services of New York City will continue, if action is taken by state and local officials to balance the New York City budget. This will occur either as a result of action taken at their own initiative, or, in the event they fail to act, [it will occur at the direction of the Federal Government] as a condition which must be met before the Secretary of the Treasury would COMMIT FEDERAL FUNDS FOR THE PURCHASE OF COURT APPROVED SHORT-TERM NOTES ~~move~~ to maintain essential services in New York ~~necessary~~ [by purchasing court approved short term notes.] Finally, these notes issued WITH ~~at~~ the APPROVAL ~~direction~~ of the federal court responsible for supervising the default procedure would have first call on all revenues flowing to New York City ~~and New York State,~~ either in the form of state and local taxes or in the form of ~~all~~ financial assistance currently provided to the ~~state and~~ city by the Federal Government, such as revenue sharing payments.

How do we ensure essential services will be maintained.

Is default a foregone conclusion

who controls city after default

Loan guarantees ?

How do we tide them over ?

Do we expect other cities ?

What is the debt

How much do they need ?

10/28/75

Option A

After default, it may be necessary, if State and local officials continue to refuse to accept responsibility for managing the affairs of the City, to work with the courts to maintain the protection of life and property for the citizens of New York City. I believe we have to make a distinction between bailing out the bond holders and politicians on the one hand, and on the other, protecting the people of New York City from the consequences of the lack of courage which may be exhibited by their office holders.

Option B

After default, we will work with all of the appropriate agencies of government to insure the protection of life and property for the citizens of New York City.

Option C

The real victims of the default caused by mismanagement of the affairs of the City by its leaders, are the eight million citizens of New York City who have paid their taxes but have been hurt by this fiscal tragedy. I wish to assure them that I will work with the appropriate governmental agencies to insure the protection of life and property.

Option D

In the event of default, the Federal Government will work with the Court to assure that police, fire and other essential services for the protection of citizens are maintained.

10/23/75

Option A

After default, it may be necessary, if State and local officials continue to refuse to accept responsibility for managing the affairs of the City, to work with the courts to maintain the protection of life and property for the citizens of New York City. I believe we have to make a distinction between bailing out the bond holders and politicians on the one hand, and on the other, protecting the people of New York City from the consequences of the lack of courage which may be exhibited by their office holders.

Option B

After default, we will work with all of the appropriate agencies of government to insure the protection of life and property for the citizens of New York City.

Option C

The real victims of the default caused by mismanagement of the affairs of the City by its leaders, are the eight million citizens of New York City who have paid their taxes but have been hurt by this fiscal tragedy. I wish to assure them that I will work with the appropriate governmental agencies to insure the protection of life and property.

Option D

In the event of default, the Federal Government will work with the Court to assure that police, fire and other essential services for the protection of citizens are maintained.

four

FUNDS FOR ESSENTIAL SERVICES

Q. Under your proposal, how would New York City get the funds to meet essential services?

A. According to New York City's figures, the City's cash needs for operations and capital projects (not including any payments of principal and interest on outstanding debt) will exceed revenues by approximately $700 million during the period December 1, 1975 - June 30, 1976. There are at least ~~three~~ ways this gap could be made up.

First, New York State could impose a temporary and emergency tax -- perhaps a package involving the income, ~~gasoline~~ and sales taxes -- to generate the necessary cash.

Second, the assets of the pension funds could be used to collateralize borrowing by MAC or the City. State and City pensions hold well in excess of $10 billion of ~~unencumbered~~ assets which ~~could~~ be used for this purpose.

Third, in the context of an orderly debt restructuring proceeding, the court could authorize the City to issue certificates of indebtedness, to be payable, on a prior claim basis, out of revenues in years after the budget balancing process is complete.

Fourth, the gap could also be reduced by immediate expenditure cuts in the City budget.

Background

There are really two problems: the net cash flow shortfall referred to in the answer and the so-called seasonal problem. The remaining seven months of the fiscal year can be broken down into two periods: December-March in which the City runs a $1.3 billion cash deficit (net of debt service) and April-June in which it runs a $600 million surplus. On a direct revenue anticipation basis, the City should be able to borrow $600 million during December-March, but it needs one of the mechanisms described in the answer to borrow the remainder.

GP/10-28-75

(3)

FUNDS FOR ESSENTIAL SERVICES

~~QUESTION:~~ Q. Under your proposal, how would New York City get the funds to meet essential services?

~~ANSWER:~~ A. According to New York City's figures, the City's cash needs for operations and capital projects (not including any payments of principal and interest on outstanding debt) will exceed revenues by approximately $700 million during the period December 1, 1975 - June 30, 1976. There are at least three ways this gap could be made up.

First, New York State could impose a temporary and emergency tax -- perhaps a package involving the income, gasoline and sales taxes -- to generate the necessary cash.

Second, the assets of the pension funds could be used to collateralize borrowing by MAC or the City. State and City pensions hold well in excess of $10 billion of unencumbered assets which would be used for this purpose.

Third, in the context of an orderly debt restructuring proceeding, the court could authorize the City to issue certificates of indebtedness, to be payable, on a prior claim basis, out of revenues in years after the budget balancing process is complete.

Get insert #3

— o —

BACKGROUND: There are really two problems: the net cash flow shortfall referred to in the answer and the so-called seasonal problem. The remaining seven months of the fiscal year can be broken down into two periods: December-March in which the City runs a $1.3 billion cash deficit (net of debt service) and April-June in which it runs a $600 million surplus. On a direct revenue anticipation basis, the City should be able to borrow $600 million during December-March, but it needs one of the mechanisms described in the answer to borrow the remainder.

~~Gerald L. Parsky~~
~~Gerald L. Parsky~~
~~Assistant Secretary of Treasury~~

GP/10-28-75

~~How ensure essential services?~~

Q. ~~If New York does default, how do you propose to ensure that essential services will be maintained?~~

INSERT # 3

~~use three points of Mr. Gerard and add this 4th:~~

Four, the gap could also be reduced by immediate expenditure cuts in the City budget.

RP/10-28-75

(4)

WHO WILL BE IN CONTROL?

Q. If New York City goes into default, under your proposed amendment to the federal bankruptcy act, who will be in control of the City?

proceeding

The type of ~~bankruptcy~~ proposed by this new legislation is one in which the debtor remains in control of its assets. ~~In other words, this City will remain under~~ the city form of government would remain unchanged from its present state.

STET

A. Under the legislation the federal government ~~(neither the Administration nor the Federal Courts)~~ would not control the City's affairs -- ~~it~~ City control would remain ~~under~~ with the Mayor, and the State Emergency Financial Control Board.

However, Under the proposal the Court ~~would have authority to~~ could authorize the City to issue new debt. The Court could condition the issuance of such debt ~~by~~ on specific actions to be taken by the City. ~~This is no~~ ~~not~~

~~Protest~~ Such conditions are no more onerous than those that would be required by a prudent investor.

RP/10-28-75

(1)

IS DEFAULT DEFINITE?

Q. In your estimation is the New York City default a foregone conclusion?

~~Mayor Beame and the Governor have predicted/ there will be a default that the City has exhaused its financial resources and that default is in the hands of the state and federal government.~~ ~~in recent testimony~~

A. City and State officials in recent congressional testimony stated that the financial resources of the City and State will have been exhausted ~~and that the stated plan for maintaining solvency through~~ by December, ~~has very limited chances of success beyond December~~.

~~Financial analysists and economists generally agree with this pessimistic outlook.~~

~~(agree that the cash flow position of the City will not liekly allow the City to meet debt service obligations or to meet current payments for essential services. . . . .)~~

~~If the State and~~

Accordingly,

If the City and State continue to be unwilling to take the measures necessary to avoid a default, it ~~is~~ seems likely that a New York City default will occur.

RP/10-28-75

(2)

CURRENT DEBT SITUATION

Q. What is the current debt situation in New York and how much additional financing ~~do they~~ does the city need in order to avoid a default?

A. According to the City's 1975 financial 1976 plan, the City will require~~s~~ $4.055 billion between December 1 and June 30 to retire maturing short-term debt, to meet debt service obligations on long-term bonds, and to pay operating and capital expenses. ~~[Additional amounts aggregating approximately $2 billion would be required to meet these obligations in the fiscal years 1977-1978.]~~

~~(net cash need)~~

(maturing in December of $400 million and operating capital shortfall of $600 million in December .... [can supply figures])

~~Simply to get through the month of December~~ the City will need close to $1 billion ~~due to~~ ~~seasonal~~ ~~seasonal~~

Due to seasonal cash flow ~~the~~ ~~demands~~ patterns,

to meet its obligations in December.

RP/10-28-75

(11)

10/28/75

COURT AUTHORIZED DEBT CERTIFICATES

Q: Will the ~~trustee~~ COURT AUTHORIZED DEBT certificates be marketable?

A: If New York City submits, as the ~~statute (or~~ proposal~~)~~ statute requires, a budget which places its financial affairs upon a sound footing, ~~and procedures~~ ~~there is every reason to believe that~~ the certificates ought to be marketable.

(10)

10/28/75

SAFETY OF INVESTMENTS

Q: Are the creditors going to lo~~o~~se their investments?

A: Accordingly, ~~I~~if New York City acts responsi~~v~~bly, ~~there is likelihood that~~ eventually all creditors ~~will~~ should be paid. ~~In working out the arrangements~~ Major states and cities have defaulted before--for example Arkansas and Detroit--and in all these cases the creditors have received 100 dollar cents on their dollar.

(1)

RIPPLE EFFECT

9. What ripple effect do you expect on the financial community from a New York City default?

There are two risks in any major financial reversal: the financial and psychological.

We have ~~Carefully~~ carefully assess~~ing~~ed the financial risk ~~requires~~ -- the impact on the markets and the impact on the banking system, and we believe these risks are ~~m=angenr~~ manageable. Markets tend to discount future ~~affects (efforts)~~ events? and to some significant degree ~~possible~~ a potential default by New York City has been discounted.

The psychological risks cannot be measured. However, it is clear that the dire predictions and vigorous rhetoric employed by those who seek to force a federal bail-out for New York City have enhanced the psychological risks. It remains of utmost importance that all who concern themselves with the affairs of New York City view the situation objectively.

These conclusions ~~are~~ have been confirmed by many disinterested observers of the market.

In short, assuming responsible conduct from now on, we do not anticipate a serious ripple effect.

(8)

Reuss Proposal

9. What is your view of Henry Reuss's proposal to extend loan guarantees to the State of New York for the benefit of the City subject to the City's bringing its budget into balance, the GAO being empowered to audit the City to ensure a balanced budget, securing any federal exposure by a first lien on all payments which the federal government may in the future owe the City or State, and acceptance by the large creditors of New York City of a stretch-out of their debt.

~~We think these things are the most appropriately resolved in the Judicial system.~~

A. ~~However;~~ However clothed, the proposal basically involves the taxpayers of America financing the cumulative ~~default~~ deficit of New York City.

~~(don't bail out the creditors -- keep the essential services going.)~~

Moreover, the proposal ~~two concerns w/Reuss:~~ involves a tremendous direct expansion of federal control over ~~local~~ (fiscal) and financial affairs of state and local government.

~~all? federal — taxpayers of America bail out. . . .~~

~~default (legislation) is a good idea for the time -- will provide these positive benefits. in favor... judicial system....~~

~~they propose to help the creditors; cannot do this at this time.~~

RP/10-28-75

(5) OTHER CITIES USE THE LEGISLATION?

Q Do you expect cities other than New York to utilize the legislation you are proposing?

A Absolutely not. No other major city in the United States has ~~have~~ engaged in consistent deficit spending and, therefore, no city has a cumulative deficit of any size, much less the size of New York's.

Note: #7 follows

RP/10.28-75

(7) LOAN GUARANTEES?

~~Q~~ ~~Would you consider a form of loan guarantees~~ to assist New York in financing its short-term financial needs?

~~NQ: Would you consider pruchasing debt certificat~~ -

rephrase the question to read:

Q Would you consider any form of financial assistance?

~~I would not until the City and the State have done absolutely everything in their powerto restore the City to a sound footing -- which they are so far from having done everything that is necessary that it is not a realistic~~

A. Under our proposal, one of the ways in which the City can ~~raise money after default under our proposal~~ finance short term needs is by the issuance of certificates authorized by the Court. ~~We expect that these certificates will be marketable.~~ It must be remembered that in order to begin the judicial process, the City must submit a plan for balancing its budget. If that is done they should be ~~no difficulty~~ able to raise necessary funds.

RP/10-28-75

3

STATE DEFAULT 10/28/75

Q: Will the State of New York default in the wake of the New York City default?

A: There is no reason for New York State to default because they are in sound financial position. Once appropriate action has been taken with respect to New York City, New York State should have no problem ~~with the~~ if officials act in a responsible way.

(13)

delete earlier answer
10/28/75

SPECIFIC CUTS

Q: What specific cuts do you propose?

A: ~~None. It is up to the City of New York.~~

As I mentioned, New York City expenditures ~~seem~~ appear out of line ~~with respect to those in the rest of the country~~ by comparison to expenditures of other cities.

It is up to the appropriate New York State and City authorities to make ~~the~~ specific decisions ~~of which they have~~ regarding cuts.

~~choosen. That is the difficulty that New York City now has in waiting too long.~~

72

10/28/75

FRAUD PROSECUTION

Q: Fraud in New York City?

A: ~~No information on fraud is available at this time. There has not been uncovered anything beyond any other city's doing.~~

~~The matter should be investigated and handled by the appropriate authorities.~~

I am confident that the ~~appropriate authorities~~ responsible agencies will take whatever action ~~if information turns up on fraud.~~ may be ~~necessary~~ appropriate.

[illegible] 2d [illegible]

[illegible] NYC

(14)

IMPACT ON BANKS

~~1~~. How many banks will be placed in difficulty in the ~~effects~~ event of a New York City default? What are the names of the banks?

The federal bank regulatory agencies have conducted an exhaustive review of holdings of New York City securities in our banking system and the potential impact on that system of a default by New York City. They have concluded that no major bank would be materially affected, as a direct consequence of a ~~deficit~~ default by New York City.

While the impact ~~of~~ on a ~~very small number~~ handful of smaller banks could be more serious, the Federal Reserve and the FDIC have adequate mechanisms to protect bank depositors ~~in~~ the banking system. In view of the protections which do exist, and it would not be appropriate to create unnecessary concern by identifying individual banks.

RIPPLE EFFECT

Q: What ripple effect do you expect on the financial community from a New York City default?

A: There are two risks in any major financial reversal: the financial and psychological.

We have carefully assessed the financial risk--the impact on the markets, and the impact on the banking system--and we believe these risks are manageable. Markets tend to discount future events and to some significant degree a potential default by New York City has been discounted. These conclusions have been confirmed by many disinterested observers of the market.

The psychological risks cannot be measured. However, it is clear that the dire predictions and vigorous rhetoric employed by those who seek to force a Federal bail out for New York City have enhanced the psychological risks. It remains of utmost importance that all who concern themselves with the affairs of New York City view the situation objectively.

In short, if all those concerned act responsibly in the future, the ripple effect would be minimal.

10/28/75

FUNDS FOR ESSENTIAL SERVICES

Q. Under your proposal, how would New York City get the funds to meet essential services?

Insert

A. According to New York City's figures, the City's cash needs for operations and capital projects (not including any payments of principal and interest on outstanding debt) will exceed revenues by approximately $700 million during the period December 1, 1975 - June 30, 1976. There are at least four ways this gap could be made up.

First, New York State could impose a temporary and emergency tax -- perhaps a package involving the income and sales taxes -- to generate the necessary cash.

funds

Second, the assets of the pension funds could be used to collateralize borrowing by MAC or the City. State and City pensions hold well in excess of $10 billion of assets which could be used for this purpose.

later

Third, in the context of an orderly debt restructuring proceeding, the court could authorize the City to issue certificates of indebtedness, to be payable, on a prior claim basis, out of revenues in years, after the budget balancing process is complete.

Fourth, the gap could also be reduced by immediate expenditure cuts in the City budget.

Background

There are really two problems: the net cash flow shortfall referred to in the answer and the so-called seasonal problem. The remaining seven months of the fiscal year can be broken down into two periods: December-March in which the City runs a $1.3 billion cash deficit (net of debt service) and April-June in which it runs a $600 million surplus. On a direct revenue anticipation basis, the City should be able to borrow $600 million during December-March, but it needs one of the mechanisms described in the answer to borrow the remainder.

GP/10-28-75

PROVISION OF ESSENTIAL SERVICES

Q: How does the proposal assure for the provision of essential services?

A: ~~First~~, The proposals provides an orderly mechanism for the restructuring of New York City's debt, allowing deferral of the massive debt service burden while the budget is being balanced.

Second, we have provided a procedure for borrowing to meet cash shortages in the interim period.

10/28/75

FUNDS FOR ESSENTIAL SERVICES

Q: Under your proposal, how would New York City get the funds to meet essential services?

A: The proposal provides an orderly mechanism for the restructuring of New York City's debt, allowing deferral of the massive debt service burden while the budget is being balanced.

According to New York City's figures, the City's cash needs for operations and capital projects (not including any payments of principal and interest on outstanding debt) will exceed revenues by approximately $700 million during the period December 1, 1975 through June 30, 1976. There are at least four ways this gap could be made up.

First, New York State could impose a temporary and emergency tax--perhaps a package involving the income and sales taxes--to generate the necessary cash.

Second, the assets of the pension funds could be used to collateralize borrowing by MAC or the City. State and City pension funds hold well in excess of $10 billion of assets which could be used for this purpose.

Third, in the context of an orderly debt restructuring proceeding, the court could authorize the City to issue certificates of indebtedness, to be payable, on a prior claim basis, out of revenues, in later years, after the budget balancing process is complete.

Fourth, the gap could also be reduced by immediate expenditure cuts in the City budget.

Background

There are really two problems: the net cash flow shortfall referred to in the answer and the so-called seasonal problem. The remaining seven months of the fiscal year can be broken down into two periods: December-March in which the City runs a $1.3 billion cash deficit (net of debt service) and April-June in which it runs a $600 million surplus. On a direct revenue anticipation basis, the City should be able to borrow $600 million during December-March, but it needs one of the mechanisms described in the answer to borrow the remainder.

10/28/75

WHO WILL BE IN CONTROL?

Q. If New York City goes into default, under your proposed amendment to the federal bankruptcy act, who will be in control of the City?

A. Under the legislation the federal government would not control the City's affairs -- control would remain with the Mayor and the State Emergency Financial Control Board.

However, under the proposal the Court could authorize the City to issue new debt. The Court could condition the issuance of such debt on specific actions to be taken by the City. Such conditions are no more onerous than those that would be required by a prudent investor.

RP/10-28-75

COURT AUTHORIZED DEBT CERTIFICATES

Q: Will the court authorized debt certificates be marketable?

A: If New York City submits, as the proposed statute requires, a budget which places its financial affairs upon a sound footing, the certificates ought to be marketable.

10/28/75

FRAUD PROSECUTION

Q: Do you expect there to be prosecutions for fraud resulting from a default of New York City?

A: I am confident that the responsible agencies will take whatever action may be appropriate.

10/28/75

FEDERAL FINANCIAL ASSISTANCE

Q: Would you consider any form of financial assistance to New York for financing its short term needs?

A: Under our proposal, one of the ways in which the City can finance short term needs is by the issuance of certificates authorized by the Court. It must be remembered that in order to begin the judicial process, the City must submit a plan for balancing its budget. If that is done they should be able to raise necessary funds.

10/28/75

STATE DEFAULT

Q: Will the State of New York default in the wake of the New York City default?

A: There is no reason for New York State to default because they are in sound financial condition. Once appropriate action has been taken with respect to New York City, New York State should not have financial problems if officials act in a fiscally responsible way.

10/28/75

REUSS PROPOSAL

Q: What is your view of Henry Reuss' proposal to extend loan guarantees to the State of New York for the benefit of the City subject to the City's bringing its budget into balance, the GAO being empowered to audit the City to ensure a balanced budget, securing any Federal exposure by a first lien on all payments which the Federal Government may in the future owe the City or State, and acceptance by the large creditors of New York City of a stretch-out of their debt.

A: However clothed, the proposal basically involves the taxpayers of American financing the cumulative deficit of New York City. Moreover, the proposal involves a tremendous expansion of direct Federal control over fiscal and financial affairs of State and local government.

10/28/75

FUNDS FOR SERVICES

Q: What happens if New York City does not have funds to pay for police, etc.

A: There are vast financial resources availabe in New York State. However, if the State of New York fails to provide the funds, we will work with the appropriate authorities to see that services essential for the protection of life and property are provided.

10/28/75

IMPACT ON BANKS

Q: How many banks will be placed in difficulty in the event of a New York City default? What are the names of the banks?

A: The federal bank regulatory agencies have conducted an exhaustive review of holdings of New York City securities in our banking system and the potential impact on that system of a default by New York City. They have concluded that no major bank would be materially affected, as a direct consequence of a default by New York City.

While the impact on a handful of smaller banks could be more serious, the Federal Reserve and the FDIC have adequate mechanisms to protect bank depositors and the banking system. In view of the protections which do exist, it would not be appropriate to create unnecessary concern by identifying individual banks.

10/28/75

OTHER CITIES USE THE LEGISLATION?

Q: Do you expect cities other than New York to utilize the legislation you are proposing?

A: Absolutely not. No other major city in the United States has engaged in consistent deficit spending and, therefore, no city has a cumulative deficit of any size, much less the size of New York's.

10/28/75

IS DEFAULT DEFINITE?

Q. In your estimation is the New York City default a foregone conclusion?

A. City and State officials in recent Congressional testimony stated that the financial resources of the Ctiy and State will have been exhausted by December.

Accordingly, if the City and State continue to be unwilling to take the measures necessary to avoid a default, it seems likely that a New York City default will occur.

RP/10-28-75

CURRENT DEBT SITUATION

Q. What is the current debt situation in New York and how much additional financing does the City need in order to avoid a default?

A. According to the City's financial plan, the City will require $4.055 billion between December 1, 1975 and June 30, 1976 to retire maturing short-term debt, to meet debt service obligations on long-term bonds, and to pay operating and capital expenses.

Due to seasonal cash flow patterns, the City will need close to $1 billion to meet its obligations in December.

RP/10-28-75

SAFETY OF INVESTMENTS

Q: Are the creditors going to lose their investments?

A: Major states and cities have defaulted before--for example Arkansas and Detroit--and in all these cases the creditors have received 100 cents on their dollar. Accordingly, if New York City acts responsibly, eventually all creditors should be paid.

10/28/75

RIPPLE EFFECT

Q: What ripple effect do you expect on the financial community from a New York City default?

A: There are two risks in any major financial reversal: the financial and psychological.

We have carefully assessed the financial risk--the impact on the markets, and the impact on the banking system--and we believe these risks are manageable. Markets tend to discount future events and to some significant degree a potential default by New York City has been discounted. These conclusions have been confirmed by many disinterested observers of the market.

The psychological risks cannot be measured. However, it is clear that the dire predictions and vigorous rhetoric employed by those who seek to force a Federal bail out for New York City have enhanced the psychological risks. It remains of utmost importance that all who concern themselves with the affairs of New York City view the situation objectively.

In short, if all those concerned act responsibly in the future, the ripple effect would be minimal.

10/28/75

SPECIFIC CUTS

Q: What specific cuts do you propose?

A: As I mentioned, New York City expenditures appear out of line by comparision to expenditures of other cities. It is up to the appropriate New York State and City authorities to make specific decisions regarding cuts.

10/28/75

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RP/10-28-75

OK

IS DEFAULT DEFINITE?

Q. In your estimation is the New York City default a foregone conclusion?

A. City and State officials in recent Congressional testimony stated that the financial resources of the Ctiy and State will have been exhausted by December.

Accordingly, if the City and State continue to be unwilling to take the measures necessary to avoid a default, it seems likely that a New York City default will occur.

RP/10-28-75

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OTHER CITIES USE THE LEGISLATION?

Q: Do you expect cities other than New York to utilize the legislation you are proposing?

A: Absolutely not. No other major city in the United States has engaged in consistent deficit spending and, therefore, no city has a cumulative deficit of any size, much less the size of New York's.

10/28/75

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10/28/75

ok

IMPACT ON BANKS

Q: How many banks will be placed in difficulty in the event of a New York City default? What are the names of the banks?

A: The federal bank regulatory agencies have conducted an exhaustive review of holdings of New York City securities in our banking system and the potential impact on that system of a default by New York City. They have concluded that no major bank would be materially affected, as a direct consequence of a default by New York City.

While the impact on a handful of smaller banks could be more serious, the Federal Reserve and the FDIC have adequate mechanisms to protect bank depositors and the banking system. In view of the protections which do exist, it would not be appropriate to create unnecessary concern by identifying individual banks.

10/28/75

OK

REUSS PROPOSAL

Q: What is your view of Henry Reuss' proposal to extend loan guarantees to the State of New York for the benefit of the City subject to the City's bringing its budget into balance, the GAO being empowered to audit the City to ensure a balanced budget, securing any Federal exposure by a first lien on all payments which the Federal Government may in the future owe the City or State, and acceptance by the large creditors of New York City of a stretch-out of their debt.

A: However clothed, the proposal basically involves the taxpayers of American financing the cumulative deficit of New York City. Moreover, the proposal involves a tremendous expansion of direct Federal control over fiscal and financial affairs of State and local government.

10/28/75

STATE DEFAULT

Q. Will the State of New York default if New York City defaults?

A. There is no reason for New York State to default because they are in sound financial position. Once appropriate action has been taken with respect to New York City, New York State should have n o problems if officials act in a responsible way.

10/29/75

SPECIFIC CUTS

Q. What specific expenditure cuts do you propose that New York City make?

A. As I mentioned, New York City expenditures appear out of line by comparison to expenditures of other cities. It is up to the appropriate New York State and City authorities to make specific decisions regarding cuts.

10/29/75

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The psychological risks cannot be measured. However, it is clear that the dire predictions and alarmist rhetoric employed by those who seek to force a Federal bail out for New York City have enhanced the psychological risks. It remains of utmost importance that all who concern themselves with the affairs of New York City view the situation objectively.

In short, if all those concerned act responsibly, the ripple effect would be minimal.

10/29/75

LOAN GUARANTEES?

Q: Would you consider any form of financial assistance to assist New York in financing its short term financial needs?

A: Under our proposal, one of the ways in which the City can finance short term needs is by the issuance of certificates authorized by the Court. It must be remembered that in order to begin the judicial process, the City must submit a plan for balancing its budget. If that is done they should be able to raise necessary funds.

10/29/75

FRAUD PROSECUTION

Q. Do you expect there to be prosecutions in fraud resulting from a default of New York City?

A. I am confident that the responsible agencies will take whatever action may be appropriate.

10/29/75

IF NEW YORK CITY CAN'T SELL SECURITIES?

Q: Supposing they cannot sell securities or otherwise raise funds to pay for essential services?

A: We have said we will work with the Court to assure essential police, fire and other services are maintained -- whatever it takes to provide these will be done.

10/29/75

OTHER CITIES USE THE LEGISLATION?

Q. Do you expect cities other than New York to utilize the legislation you are proposing?

A. Absolutely not. No other major city in the United States has engaged in consistent deficit spending and, therefore, no city has a cumulative deficit of any size, much less the size of New York's.

However, the statute applies to all cities over 1,000,000 population not just to New York.

10/29/75

IS DEFAULT DEFINITE?

Q. In your estimation is the New York City default a foregone conclusion?

A. City and State officials in recent Congressional testimony stated that the financial resources of the City and State will have been exhausted by December.

Accordingly, if the City and State continue to be unwilling to take the measures necessary to avoid a default, it seems likely that a New York City default will occur.

10/29/75

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Q. What is your view of Henry Reuss' proposal to extend loan guarantees to the State of New York for the benefit of the City subject to the City's bringing its budget into balance, the GAO being empowered to audit the City to ensure a balanced budget, securing any Federal exposure by a first lien on all payments which the Federal Government may in the future owe the City or State, and acceptance by the large creditors of New York City of a stretch-out of their debt.

A. However clothed, the proposal basically involves the taxpayers of American financing the cumulative deficit of New York City which I oppose. Moreover, the proposal involves a tremendous expansion of direct Federal control over the fiscal and financial affairs of State and local government.

Further, the practicality of handling the situation in this way is doubtful. Particularly, in dealing with small creditors, union contracts, and other obligations.

10/29/75

TIMING OF SPEECH

Q: Why did you give this speech now?

A: It was becoming increasingly likely that New York City might default because actions to prevent default were not forthcoming. Thus, I think it was important to provide for an orderly system for handling the situation should this occur.

10/29/75

CURRENT DEBT SITUATION

Q: What is the current debt situation in New York and how much additional financing does the City need in order to avoid a default?

A: According to the City's financial plan, the City will require \$4.055 billion between December 1, 1975 and June 30, 1976 to retire maturing short-term debt, to meet debt service obligations on long-term bonds, and to pay operating and capital expenses.

Due to seasonal cash flow patterns, the City will need close to \$1 billion to meet its obligations in December.

10/29/75

CREDIT INVESTMENTS

Q: Are the creditors going to lose their investments?

A: Major states and cities have defaulted before -- for example Arkansas and Detroit -- and in all these cases the creditors have received 100 cents on their dollar. Accordingly, if New York City acts responsibly, eventaully all creditors could be paid if New York City officials act responsibly in handling the city's fiscal affairs.

10/29/75

WRIGHT PATMAN
FIRST DISTRICT
STATE OF TEXAS

WASHINGTON ADDRESS:
2328 RAYBURN HOUSE OFFICE BUILDING
20515

HOME ADDRESS:
P.O. BOX 1868, TEXARKANA, TEXAS
75501

COMMITTEES:
BANKING, CURRENCY AND HOUSING
JOINT ECONOMIC COMMITTEE
JOINT COMMITTEE ON DEFENSE PRODUCTION

Congress of the United States
House of Representatives
Washington, D.C. 20515

October 29, 1975

The President
The White House
Washington, D. C.

My Dear Mr. President:

As I understand your speech before the National Press Club concerning the financial problems of New York City, you are suggesting that there be no assistance until the city enters default and goes through bankruptcy proceedings in the Federal courts. You indicated that there would be two major beneficiaries of any pre-default assistance -- the present officials of New York City and the commercial banks or other large investors who purchased the city's securities. You made it clear that you opposed a "bail out" of either group.

It is well-known that the Federal banking agencies, particularly the Federal Reserve, have often provided direct and indirect bail-out mechanisms for commercial banks when they have been caught with bad investments. As you know, there has been Congressional testimony and news reports about such assistance in relationship to the troubled Real Estate Investment Trusts, to feed lot operators, and of course, it is a matter of public record that the now-defunct Franklin National Bank was provided about $1.7 billion in bail-out assistance from the Federal Reserve.

Judging from the tone of your speech, which is clearly "anti bail-out", I assume that such mechanisms would not be employed in this instance and that the commercial banks and other investors would, like the city, be required to seek relief in the courts. I assume that you have discussed this with Federal Reserve Board Chairman Arthur Burns and other bank regulatory officials and that you have instructed them that there will be no behind-the-scenes bail-outs employed by these agencies.

In conclusion, Mr. President, your speech very clearly indicated to the American public and the Congress that it is your policy that the municipality and those who have invested in its securities are to be treated alike and that their basic remedies lie in bankruptcy proceedings. This would represent a significant change in policy toward the commercial banking industry and other investors who make bad judgments. I am most interested in learning how you plan to implement this policy at the Federal Reserve and the other regulatory agencies and what steps will be taken to monitor their continuing relationships with the institutions which hold the New York City paper in question.

Respectfully,

Wright Patman

MAC NEGOTIATING PLAN WITH LENDERS
TO PROVIDE NYC WITH 8 BILLION

N Y -(DJ)-- A PLAN TO PROVIDE SOME 8 BILLION TO PULL NEW YORK CITY OUT OF ITS FISCAL CRISIS IS BEING NEGOTIATED BETWEEN MUNICIPAL ASSISTANCE CORP AND ? POTENTIAL LENDERS.

A MAC SPOKESMAN SAID COMMITMENTS HAVENT BEEN OBTAINED THUS FAR FROM BANKS PENSION SYSTEMS AND INVESTORS. BY NEXT MONDAY OR TUESDAY WELL HAVE A SENSE OF WHETHER WE CAN DO IT HE SAID. A MAC BOARD MEETING ON THE FINANCING PLAN ENDED AT THE GOVERNORS NEW YORK OFFICE BEFORE MID-DAY.

ELEMENTS OF THE PLAN ARE-

-EXTENSION OF 1.1 BILLION OF MAC BONDS HELD BY BANKS TO 10-YEARS AT A 6 PC INTEREST RATE FROM THREE TO FIVE-YEAR MATURITIES.

-EXTENSION OF 1.3 BILLION OF MAC BONDS HELD BY PENSION FUNDS SAVINGS BANKS AND OTHER STATE FUNDS FOR THE SAME PERIOD AND RATE.

-A BANK ROLLOVER OF 550 MILLION OF NEW YORK CITY NOTES PREVIOUSLY AGREED TO.

-VOLUNTARY EXCHANGE BY INDIVIDUAL HOLDERS OF 1.6 BILLION OF CITY NOTES FOR 9 PC MAC BONDS DUE IN 15-YEARS.

-THE PURCHASE OF 1.87 BILLION OF THREE-YEAR NEW YORK CITY SECURITIES BY CITY PENSION FUNDS.

THE CITY ALSO WILL NEED 1.5 BILLION OF SEASONAL THREE-MONTH LOANS FROM BANKS TO MEET ITS NEEDS THROUGH APRIL.

THE LARGEST PROBLEM WILL BE GETTING COOPERATION OF INDIVIDUALS WHO ARENT EVEN ON RECORD AS HOLDERS OF THE CITYS BEARER SECURITIES THE MAC SPOKESMAN SAID.

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PMS PRESIDENT GERALD R FORD
THE WHITE HOUSE
WASHINGTON D C

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WHITE HOUSE
MAIL ROOM

DEAR MR. PRESIDENT

WE RESPECTFULLY BUT URGENTLY ASK YOU TO RECONSIDER YOUR ANNOUNCED INTENTION TO ALLOW NEW YORK CITY TO GO INTO BANKRUPTCY. WE AGREE WITH YOU THAT THE LAWS GOVERNING MUNICIPAL BANKRUPTCY SHOULD BE MADE MORE WORKABLE BUT WE URGE THAT, AT THE SAME TIME, FEDERAL FINANCIAL ASSISTANCE SUCH AS LOAN GUARANTEES BE MADE

AVAILABLE TO MAKE IT POSSIBLE FOR NEW YORK CITY TO WORK ITSELF OUT OF ITS FINANCIAL CRISIS. SUCH ASSISTANCE COULD AND SHOULD BE SO CONDITIONED AS TO ASSURE NOT ONLY THE FEDERAL TREASURY IS PROTECTED, BUT THAT IN THE FUTURE NO MUNICIPALITY WILLINGLY SEEKS FEDERAL AID TO STAVE OFF BANKRUPTCY.

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WHITE HOUSE
MAIL ROOM

WE URGE TWO MAIN ARGUMENTS AGAINST BANKRUPTCY FOR NEW YORK: FIRST. GOVERNOR CAREY AND MAYOR BEAME ALREADY HAVE PLACED MANAGEMENT OF THE CITY'S FINANCES IN THE HANDS OF SOME OF THE ABLEST BUSINESS EXECUTIVES IN THE COUNTRY. IN COOPERATION WITH LEADERS OF ORGANIZED LABOR THEY CAN DO A FAR BETTER JOB OF PLANNING AND EXECUTING A WORK-OUT PROGRAM THAN COULD ANY FEDERAL REFEREE IN

BANKRUPTCY. SECOND. WE BELIEVE THE DOMINO EFFECT OF NEW YORK CITY'S GOING BANKRUPT IS FAR GREATER THAN SOME OF YOUR ADVISERS HAVE PREDICTED. HERE IN NEW YORK THERE WILL BE A PREDICTABLE LARGE FALL-OFF IN MUNICIPAL TAX REVENUES, AND MANY HOSPITALS BOTH PUBLIC AND VOLUNTARY, AS WELL AS OTHER CITY-SUPPORTED VITAL SERVICES, WILL BE DRIVEN INTO BANKRUPTCY. WE PREDICT THAT INEVITABLY A FEDERAL REFEREE IN BANKRUPTCY WILL HAVE TO ASK THE FEDERAL GOVERNMENT FOR EVEN MORE FINANCIAL AID THAN IS PRESENTLY BEING REQUESTED, AND THAT THE WORK-OUT PERIOD WILL BE MUCH LONGER. OUTSIDE OF NEW YORK CITY AND NEW YORK STATE, MANY INNOCENT PERSONS WILL SUFFER. THE DOMINO EFFECT ON NATIONAL AND INTERNATIONAL CREDIT MARKETS WILL IMPOSE ENORMOUS BURDENS ON THE ECONOMY

AND THE PEOPLE IN THE FORM OF HIGHER INTEREST RATES, CANCELLED AND POSTPONED CONSTRUCTION PROJECTS, REDUCED GNP, AND ACCELERATED INFLATION.

IF THE FEDERAL GOVERNMENT NEVERTHELESS DOES PERMIT NEW YORK CITY TO SINK INTO DEFAULT, AND MERELY AMENDS THE MUNICIPAL BANKRUPTCY LAWS, IT IS IMPERATIVE SUCH AMENDMENTS INCLUDE ELECTRIC, GAS, AND STEAM ENERGY SUPPLY IN ANY PRIORITY LIST OF "ESSENTIAL SERVICES". IF THEY DO NOT THE RESULTS COULD BE DEVASTATING BOTH TO OUR COMPANY AND TO THE CITY AS A WHOLE.

THE CITY PAYS US DIRECTLY ABOUT $120 MILLION A YEAR FOR ELECTRICITY, GAS, AND STEAM -- MOST OF WHICH IS USED

FOR SUCH ESSENTIAL SERVICES AS POLICE, HOSPITAL, FIRE DEPARTMENT, SANITATION, SEWAGE, AND STREET-LIGHTING FACILITIES. OUR BILLINGS TO RELATED PUBLIC AGENCIES -- SUCH AS THE HOUSING AUTHORITY AND THE TRANSIT AUTHORITY-- ARE ABOUT $150 MILLION A YEAR FOR SUCH ADDITIONAL ESSENTIAL SERVICES AS THE SUBWAY SYSTEM AND THE ENERGY NEEDS OF ABOUT 600,000 RESIDENTS OF PUBLIC HOUSING.

THE STATE, WHICH COULD BE CAUGHT UP IN THE DOMINO EFFECT OF A DEFAULT SITUATION, PAYS US ANOTHER $12 MILLION A YEAR. AND JUST TWO INDEPENDENT STATE AGENCIES--THE METROPOLITAN TRANSPORTATION AUTHORITY AND THE PORT AUTHORITY--PAY US IN TOTAL NEARLY $60 MILLION A YEAR. THUS WE RECEIVE NEARLY $350 MILLION A YEAR FROM CITY

AND STATE AGENCIES THAT COULD BE AFFECTED BY DEFAULT. WE SHOULD NOT BE PLACED IN A POSITION WHERE OUR CHOICES ARE EITHER TO DISCONNECT ESSENTIAL UTILITY SERVICE TO THE CITY OR STATE, OR TO WITHHOLD PAYING A LARGE PART OF THE TAXES WE NOW ANNUALLY PAY THE CITY AND STATE (MORE THAN $400 MILLION) OR TO OURSELVES SLIP INTO INSOLVENCY.

IT IS CLEAR CON EDISON COULD NOT SURVIVE FOR LONG IF IT CONTINUED TO SERVE A BANKRUPT CITY, AND CONTINUED TO PAY TAXES, BUT WAS NOT ITSELF PAID BY THE CITY OR THE REFEREE IN BANKRUPTCY. WE OURSELVES WOULD SOON BE

BE INSOLVENT, AND SERVICE RELIABILITY WOULD DETERIORATE.

IN A CITY THAT IS BOTH VERTICAL AND UNDERGROUND (WITH BOTH ELEVATORS AND SUBWAYS A PART OF EVERYDAY LIFE), SUCH SERVICE DETERIORATION WOULD BE THE FINAL BLOW TO OUR ONCE PROUD CITY. IT CANNOT SURVIVE WITHOUT ADEQUATE AND RELIABLE UTILITY SERVICES.

WE THEREFORE EARNESTLY REQUEST THAT ELECTRICITY, GAS, AND STEAM SERVICE BE INCLUDED ON ANY LIST OF "ESSENTIAL SERVICES" THAT WOULD BE MAINTAINED IN THE EVENT OF DEFAULT.

SINCERELY
CHARLES F. LUCE
CHAIRMAN OF THE BOARD

CON EDISON

NNNN

STATE OF NEW YORK
EXECUTIVE CHAMBER
ALBANY 12224

HUGH L. CAREY
GOVERNOR

November 4, 1975

Dear Mr. President:

I have today sent the attached letter and supporting materials to the President of the Federal Reserve Bank of New York. On behalf of the people of the State of New York, I am requesting that the Federal Reserve consider emergency credit assistance for four agencies of the state that face imminent default on their obligations. I wish to stress to you that these agencies have nothing to do with the fiscal crisis facing New York City. Each of them has an enviable record of financial soundness and prudent management. Each of them for years have been relied upon by the citizens of New York to provide housing, health and environmental facilities essential to the state's well being. Yet these agencies, the models for similar agencies in over 30 other states, now find themselves precluded from the investment market --- a condition that has only been severely aggravated since your recent speech calling for the bankruptcy of New York City.

Should these agencies default, which certainly will occur in the absence of Federal assistance, hundreds of projects involving $2.5 billion in construction funds will be stopped prior to completion and thousands of workers will be thrown into the unemployment rolls. These projects include hospitals and other health facilities, schools, and housing.

The general credit of the State will not only be placed in jeopardy but, in my opinion, could be critically impaired for many years to come.

Again, all of this does not have to occur. While these agencies have no direct relationship with the New York City problem, unfortunately the investment community views the problem as one and the same. This will continue as long as the Administration remains passive in the face of the New York City crisis.

In effect, the contagion of New York City has now spread to agencies of New York State.

In addition, your many statements on this subject continue to assert that the State of New York has sufficient resources to meet the collapse of the city. I would only remind you once more of what your own financial experts know -- the State of New York has its own budget deficit of $700 million, and is in no position to sustain the city's needs or meet the borrowing needs of these state agencies.

I sense, Mr. President, as do many others across the country that we are at an economic crossroads unparallelled since those final moments in the darkest Depression. Whatever points you thought necessary to make about the past mistakes of New York City have been made. For our part, we have labored long and hard over the past ten months of my administration to right those wrongs. Now, despite all those efforts, we see the rapid spread of financial confusion and distrust from the city to the State, and potentially to other states as well.

It is not inappropriate, indeed it is in the tradition of our nation for us now to look for and expect positive leadership from a President and his administration.

Sincerely,

Hugh L. Carey

Hugh L. Carey
Governor

The Honorable Gerald R. Ford
President of the United States
The White House
Washington, D.C.

STATE OF NEW YORK
EXECUTIVE CHAMBER
ALBANY 12224

HUGH L. CAREY
GOVERNOR

November 4, 1975

Dear Mr. Volcker:

Pursuant to my responsibilities as Governor of the State of New York, I herewith submit a preliminary application and request for consideration of a 90-day extension of credit, with the option of renewal for an additional 90 days, in the amount of $576 million pursuant to Section 13 of the Federal Reserve Act (12USC 343). The proceeds of this loan would be applied to meet the immediate needs of the following public benefit corporations which are authorized by statute to operate within New York State:

-- Housing Finance Agency
-- Medical Care Facilities Financing Agency
-- Dormitory Authority
-- Environmental Facilities Corporation

Events in recent months and weeks have disrupted the capital markets, closing them to the issues of several agencies which have traditionally enjoyed high ratings and a reputation for prudent and conservative management. New York State and the Federal government, to the extent of their capacity, have an obligation to help contain this crisis and to insure that agencies with sound credit are not destroyed.

The President indicated in his address to the nation last Wednesday that discerning investors would distinguish between sound credits and weak ones, and that the market had already largely discounted the potential insolvency of New York City. Yet, as of this moment, the capital markets are closed to four New York State authorities. Indeed, the prospects of securing financing for these seasoned agencies are considerably dimmer, not brighter, following the President's speech.

Now more than at any other time, I believe, since creation of the Federal Reserve System, the essentials of one of its crucial national purposes are sharply defined by the demands of the current crisis: to provide credit on an emergency basis to sound agencies which find traditional sources of investment temporarily closed to them.

In support of this application, enclosed is a series of analyses prepared by my office which explain the circumstances giving rise to this preliminary application.

I have discussed this request with the Lieutenant Governor, the State Comptroller, the Speaker and Minority Leader of the State Assembly, and the Majority and Minority Leaders of the State Senate, and can report they endorse the course of action proposed in this letter.

I have asked the legislative leaders to stand in readiness to convene a legislative session the week of November 10th. As you know, staff representatives of my office and the legislative leaders have been meeting with financial institutions to discuss steps that have been proposed to strengthen the viability of the State agencies; the legislative session would provide a timely opportunity for State action in support of the State agencies in connection with any definitive action regarding an extension of credit. It is my hope that this letter can lead to early discussion with you of the alternatives open to us and agreement on a common framework for action.

For a complete analysis and explanation of the public purpose to be financed under the proposed loan, and to supply further information, State Budget Director Peter C. Goldmark, Jr. and the directors of the four public authorities involved are prepared to answer any request you may have.

Sincerely,

/s/ Hugh L. Carey

Mr. Paul Volcker
President, Federal Reserve
Bank of New York
33 Liberty Street
New York, New York

Enclosure