The original documents are located in Box C40, folder "Presidential Handwriting, 5/7/1976" of the Presidential Handwriting File at the Gerald R. Ford Presidential Library.

THE WHITE HOUSE
WASHINGTON

Kathie -

This was in general Trip OUTBOX that Nell gave to me --- I think perhaps Dick Cheney would like to see.

Trudy

Dick returned x

5/7

THE WHITE HOUSE
WASHINGTON

Where we were | Where we are | Where we are going.

Economy –

Foreign Policy –

Government –

Morality –

THE PRESIDENT HAS SEEN....

REDISCOVERING FISCAL RESPONSIBILITY

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Detroit Economic Club
December 15, 1975

1975 is drawing to a close and, as we look back I believe we would all agree, "it's been a rugged year." In fact, it is probably well that we don't have perfect foresight. We would have seen:

- A recession worse than any since the 1930's.
- A U.S. withdrawal in Viet Nam.
- Criminal convictions of many of our national leaders.
- Energy dependence in OPEC increasing.
- New York City perilously approaching bankruptcy.

If we had been able to "crystal ball" the future we might have allowed the magnitude of the problems we faced to overwhelm us. In fact, personally I might have thought it was much wiser to continue my efforts in the private sector rather than making the journey to Washington.

Yet we have survived this difficult series of events-- a sequence that only a few years ago would have seemed impossible.

Rarely have we faced such a complicated and difficult set of problems. But I have renewed hope and optimism about America's future. We have stood the test without the loss of our institutions or our good sense. One year ago we were experiencing double-digit inflation and skyrocketing unemployment. Production, sales, and employment were declining precipitously as the economy was midway through the deepest recession since World War II.

Change is often so incremental that it clouds our remembrance of the state of events even a year past. The President declared that the time had come to move in a new direction. A brief review illustrates the substantial gains that have been achieved. The double-digit inflation of over 12 percent in 1974 was reduced during 1975 to about seven percent. During the spring of 1975 the unemployment rate peaked at 9.2 percent. Since that time the economy has begun to recover. The size of the total labor force has grown by 1.5 million people, and the unemployment rate is 8.3 percent and falling. The Gross National Product is again rising at an annual rate of growth of about eight percent during the last two quarters of 1975. We began 1975 with the greatest bruden of excessive inventories in our history and ended the year with inventories at approximately normal levels.

We are a long way from where we want to be, yet in my view, we are moving again in the right direction. Nowhere is this clearer than in the growing chorus on both sides of the aisle and all parts of America for fiscal responsibility. Even many of the big spenders are articulating the need for fiscal prudence. Still, the battle of the budget is not yet won.

This encouraging development results in part from what I call the "moral of the Big Apple," the New York City story. Let me briefly review some highlights in the New York City saga. For several years, New York City's revenues rose at an annual rate of 6-7 percent while its expenditures rose in excess of 12 percent a year. Finally, about a year ago, the creditors blew the whistle--no more loans. For many months, New York's leaders seemingly refused to accept that the end of their "debt addiction" era was at hand. Their withdrawal symptoms were predictable--borrow some more from the Federal Government to cover the deficits.

Six months ago, representatives of New York met with myself and other Federal officials and insisted that they had exhausted their own resources. What was needed, they said, was a massive and immediate infusion of money (or guarantees) from Washington. The only realistic option, they claimed, was for the Federal Government to rush to the rescue with a huge assistance program--a program what would inevitably have continued for years. We did not agree.

In September, the New York State Legislature approved a plan that would enable the city to meet its financial obligations through early December. For the first time, city pension funds were tapped. Cuts in municipal expenses were begun. But this was a temporary bandaid remedy, and everyone knew it. The plan committed the State of New York to help the City, but the plan was clearly short term. At the end of three months, it was probable that both the State and the City would need to be bailed out. Could the Federal Government resist such an urgent plea from a "debt addict."

Predictably a crisis materialized in October and I received a 1 a.m. call requesting that I advise the President immediately that unless Federal help was forthcoming New York City would default the next day. No Federal help was offered. It was so close that the New York banks stayed open an extra hour to await funds to avoid a default. New York City rescued itself for the moment with a loan from the City pension funds. New York officials began to believe what the President had been saying--there would be no Federal bailout.

On October 29, in an address before the National Press Club, the President said that he would veto any bill which had as its central purpose a Federal bailout in order to prevent a default. By bail out he meant: (1) assumption by the Federal Government through guarantees or otherwise of New York City's past indebtedness of about $4 billion; (2) Federal help to finance current deficits; (3) that losses by investors, banks and others would not be made whole by the Federal Government; (4) that the American taxpayer would not be asked to underwrite the past mismanagement of New York City.

The President said that the responsibility of the Federal Government was twofold:
First, <u>in the event New York was unable or unwilling to meet its own obligations,</u> the Federal Government should ensure that the process of default be as orderly as possible, which would require changing the Federal bankruptcy laws.
Second, the Federal Government should insure maintenance of services essential for the protection of life and property.

After the union and political leadership, the bankers and businessman in New York heard this, and believed it, we began to witness a revival of the "can do" spirit of New York that once was the pride of the Empire State. The political leaders of New York faced up to hard realities. Businessmen, such as Felix Rohatyn, were in the forefront of the effort. Together they began a concerted, all-out effort to put the finances of the City on a sound basis.

The program put together by the leadership of New York is impressive:

1. More than $200 million in new taxes have been voted.
2. Additional personnel reductions of 40,000 beyond the layoffs of 22,000 city employees already made were mandated.
3. A partial wage freeze and deferral was imposed.
4. The city reduced its subsidy to the City University by $32 million. The trustees were told to make up the difference by charging tuition.
5. The transit fare was increased from 35¢ to 50¢.
6. Municipal employees will be required to contribute $107 million per year to pension systems. The City has been directed to stop the practice of using, for budgetary purposes, income of pension systems in excess of four percent per annum. Designated business leaders have been asked to report on the actuarial soundness of such systems.

Outrageous abuses of the pension system through improper use of overtime in computing pension levels were terminated.

7. Extensive management changes including a new Deputy Mayor for Finance and a new Chief of Planning were instituted.

8. The Emergency Financial Control Board developed a three-year plan to produce a modest surplus in the City's expense budget by fiscal year 1977-78.

9. Payments to the City's note holders will be postponed and interest payments reduced through passage of legislation by New York State.

10. Banks and the large insitutions agreed to postpone collection on their loans and to accept lower interest rates.

11. The City pension system will provide up to $2.5 billion in additional loans to the City.

All of these steps, totalling $4 billion in refinancing and spending cuts are part of an effort to address New York's financing needs and to bring the City's budget into balance.

The distance between what was said to be impossible and what is actually being done today is the best measure of how far New York has come toward accepting primary responsibility for their financial crisis.

The plan is not a Federal bail out. The Federal Government will not assume any past debts or current deficits.

The City and State have found the way to bail themselves out. It was not easy or pleasant task, and it is not finished. It success depends on their determination in carrying out the plan.

Why then was <u>any</u> Federal help necessary? Because the City's tax receipts come late in the year, the City needs to borrow funds for a period of time early each year to ensure that essential services are provided. This seasonal borrowing is normal practice for most cities and is financed through borrowing in the private market.

But the private credit markets remain closed to New York City due to their past record of fiscal irresponsibility. This can only be corrected by time--time to demonstrate that they have returned to fiscally responsible management of their affairs. This is why the President asked the Congress for authority to provide a temporary line of credit. The seasonal assistance legislation provides for Federal loans to be repaid by the end of each fiscal year. The two-and-a half year revolving fund to meet New York's seasonal financing needs will be carefully monitored on a month-by-month basis to ensure strict adherence to the payment schedule. Failure to meet the terms of the loans will result in swift termination of the assistance. Congress has responded quickly and favorably to this proposal and the President on December 9 signed the authorizing legislation. We are all anxious to see New York implement and success with the plan that they have developed.

What lessons have we learned from the story of the "Big Apple?" First, no city, no state, no national government can spend beyond its means forever. I say "learned." Perhaps I should say, relearned or rediscovered. Edgar J. Levey in a pamphlet entitled "New York City's Progress Toward Bankruptcy" wrote these sobering words: "When a city is growing as rapidly in wealth and population as New York, the temptation to incur expenditures for any ends that seem god in themselves is generally irresistible, and the tendency is to refrain as long as possible from fixing any limit to the incurring of new obligations. But no community, however rich, can defy forever the operation of financial laws." Equally sobering is that Mr. Levey wrote this prophetic passage in 1908.

Second, we learn that when the need for fiscal responsibility is understood and believed--people act to restore responsible behavior.

Third, the "so-called" tough stand by the President, brought a responsible answer to this national problem. It was not a political victory--but a substantive one.

Hopefully rediscovery of the need for fiscal responsibility is also underway at the Federal level. It is the motivating force behind the President's proposal that the Federal Government view its financial situation like any soundly run economic unit and consider its expenditures and revenues at the same time.

Thus the President has proposed a permanent tax reduction of $28 billion coupled with a spending ceiling for fiscal year 1977 of $395 billion. The proposal recommends the largest single tax cut in American history. The spending ceiling represents a $28 billion reduction in the projected growth of Federal expenditures. The objective is to begin a program of fiscal restraint that will result in a balanced Federal budget within three years.

While the Congress has not yet accepted the President's plan, its acceptance is growing. Moreover, I believe the American people have not only accepted the need for a return to fiscal responsibility but will demand it. The New York City experience has been a lesson to the country. As the President asked when he reviewed New York City's problems, "When the day of reckoning comes, who will come to the aid of the United States of America?"

If that day comes, I think I can say who will help. Like New York, when the chips are down, all Americans will respond. But more importantly, due to the President's leadership, we have the example of the New York experience to teach us the importance of acting <u>now</u> to restore fiscal responsibility and thus to prevent that "day of reckoning."

THE PRESIDENT HAS SEEN.

WHAT'S WRONG WITH THE HOUSE BUDGET RESOLUTION

- It forces the members to agree they want $17 billion more in spending than the President recommends.

- It forces the members to agree they want to collect $10 billion more in taxes than the President wants.

- It forces the members to agree to a deficit of over $50 billion, at least $7 1/2 billion more than the President recommends.

- It forces the members to agree to keeping thousands of Federal employees and huge stocks of regulatory red tape which the President has proposed be eliminated by consolidating programs.

- It forces members to agree that more pork barrel public works projects are the way to create more jobs instead of following the balanced approach recommended by the President which emphasizes creation of real, rewarding and permanent jobs in the private sector.

What all of this means is:

- a greater danger of future inflation;

- Congressional failure to get on the track of a balanced budget by FY 1979 that the President is advocating;

- a failure to face squarely the need to get Government spending under control.

All of the fancy excuses in the world won't paper over these fundamental differences between the Budget Committee resolution and the President's proposals. Adoption of the Committee resolution would make it clearer to the voters than it has ever been before that:

- the Congress wants more spending

- the Congress wants higher taxes

- the Congress wants bigger deficits

- the Congress wants more Federal employees.

After briefly flirting with the notion that it might be a good idea to gain control over Federal spending, the majority of the House Budget Committee resisted temptation and reverted to the old politics-as-usual ploy of "...when in doubt spend, spend and spend some more!"

While some may call it a "ceiling", we all know that the Budget Resolution will probably turn out to be a floor under Federal spending.

By voting for this resolution, a Member will be telling the American people, in effect, that he or she favors:

- More Federal Spending
- Higher Taxes
- Higher Deficits
- More Inflation
- Bigger Government

Let's reject that rhetoric about the House Resolution being "very close" to the President's own budget for FY 1977, and instead consider the following facts:

MORE SPENDING -- specifically, $17 BILLION more than the President recommended:

- including a last minute add-on of $2.2 Billion for a program with a noble title "job creation" which hasn't even been defined yet; and
- including hundreds of millions which could have been saved by adopting the President's proposals to control runaway costs in such programs as Food Stamps and Medicare.

HIGHER TAXES -- the American people and American businesses will be paying more of their incomes to the government than the President wants because the Committee majority rejected his proposals for tax reductions totalling $10 BILLION; tax reductions which would have:

- benefited the most over-taxed group in America -- the average working family by better than $180 a year (even after offsetting any social security tax -- $227 before such offset); and

- stimulated the creation of more and better-paying jobs in the private sector by encouraging more capital investment.

HIGHER DEFICITS -- even with rejection of the tax cuts, the deficit produced by the Resolution would be at least $7.5 BILLION higher than that in the President's Budget.

- It probably will be substantially higher since:

  -- it is based on extremely optimistic estimates of revenue -- about $3.9 Billion higher than Administration estimates; and

  -- it counts as revenue, about $2 Billion of unidentified tax reform measures which, in the view of influential Members, will not be enacted.

MORE INFLATION -- the Resolution ignores and indeed effectively negates, the President's goal of reaching a balanced budget in 1979:

- budget authority, much of which would be spent 2, 3 or 4 years from now and add to the base in such out years, exceeds the President's request by about $25 BILLION when adjustments are made to put the two budgets on a comparable basis; and

- in the face of a strong and steady economic recovery, the Committee majority wants to lock in now even more stimulation 1, 2 and 3 years from now, financed by Treasury borrowing. Once public works-type contracts are signed, there is no way to make necessary course adjustments to fight inflation. It is then too late.

BIGGER GOVERNMENT -- not only have the President's proposals to scale down the size of the Federal Government been rejected, the Committee majority has thought up some new and even bigger jobs for the government to take on...

  -- the consolidation of 58 separate categorical grant programs into 3 broad block grants to states in the areas of health services, child nutrition and education would have led to a more equitable distribution of Federal aid and allowed the Executive Branch to reduce Federal employment by some 2300 positions in the health area alone.

- The Resolution goes even further by supporting new programs which would add substantially both to Federal spending and Federal control over major segments of our economy:

  -- by providing seed money for the Humphrey/Hawkins so-called "full employment" bill, the House would be letting a camel's nose under the tent, and within a few years it would be costing countless billions to feed that camel;

  -- more incredibly, Humphrey/Hawkins is a cop-out of the first order since the sponsors can't figure out how to reach their own goal without igniting a frightening round of inflation, so they take credit for spending the money while making the Executive Branch figure out how to make an impossible program work;

  -- by including $50 million for national health planning, the Committee majority is trying to commit the country to a tax-payer supported and yet undefined program of incalculatable costs;

  -- but, at the same time, the Committee majority was unable to agree on anything but the most timid measures to control the soaring costs of the medical programs already run by the Federal Government.

IN SHORT, there is a substantial and significant difference between the President's Budget and the House Budget Committee Resolution:

- the President wants to decelerate the growth of Federal spending; the Committee majority seeks to increase it;

- the President wants to give more authority and funding to state and local governments; the Committee majority seeks to further concentrate power in Washington;

- the President wishes to reduce the number of Federal bureaucrats; the Committee majority wants even more;

- the President believes our economic recovery, already well on course, could be permanently derailed by a new round of inflation; the Committee majority seeks even larger deficits and more Federal spending;

- the President wants incentive for the private sector to create more and better jobs for the American people through economic growth; the Committee majority seeks to use government make-work projects to provide jobs, paid for by deficits in the Federal budget for the foreseeable future and beyond; and

- the President believes the American people want to spend more of their own incomes; the Committee majority believes the government should take even more money out of the hands of working people and let the Congress decide how to spend it.