MUNICIPAL ASSISTANCE CORPORATION FOR THE CITY OF NEW YORK

Minutes of the Special Meeting of the Board of Directors

January 11, 1978

A Special Meeting of the Board of Directors of the Municipal Assistance Corporation For The City of New York was held at 10:00 a.m., on Wednesday, January 11, 1978, at the offices of Paul, Weiss, Rifkind, Wharton and Garrison, General Counsel to the Corporation, 345 Park Avenue, New York City.

The following Directors were present, but did not constitute a quorum of the Board:

Felix Rohatyn, Chairman
Frank Barry
Dick Netzer
Robert Weaver

Also present was Richard Ravitch, a nominee to the Board of Directors.

The following Representatives to the Board of Directors were present:

Leonard Nadel
Zane Klein

The following members of the Staff were present:

Eugene Keilin
Stephen Weinstein
Paul Giddings
Marilyn Friedman
Andrew Decker

Linda Seale
William Lithgow
Michael Smith
Linda Dinkin
James Brigham

Also present by invitation of the Board were: Allen L. Thomas of Paul, Weiss, Rifkind, Wharton and Garrison, General Counsel to the Corporation; Donald D. Kummerfeld, Executive Director of the Emergency Financial Control Board; Philip L. Toia, Deputy Mayor for
Finance of The City of New York; and Paul Angeli of the New York Federal Reserve Bank.

Public Session

City Financing

Mr. Rohatyn stated that the purpose of the meeting was to review the developing situation with regard to future financing for the City, and that no official action of the Corporation would be undertaken at the meeting.

Mr. Rohatyn reviewed the recent downturn in the market for the Corporation's bonds, due to the developments regarding future City financing, widely discussed in the press. Therefore, he continued, it appeared that the Corporation will be out of the market until the open City issues are resolved. The recent sale of the 1978 Series JJ Bonds, he stated, was affected, in that the underwriters have an unsold balance of more than $100 million of the $250 million issue.

Mr. Rohatyn indicated that a new crisis appeared to be building up for the City, without the definite deadlines of 1975, but with a very tight schedule of events over the next few months. He stated that there was a critical need for long-term financing from the Federal government. Such financing, he continued, would make it possible to solve the City's seasonal financing needs locally, and probably unnecessary to seek further Federal assistance. With only Federal seasonal aid, he concluded, the City would simply limp along for the period of such aid, be unable to arrange for needed long-term financing, and have to go back to Washington at the end of the
period. Mr. Rohatyn stated that these thoughts were set out in a Memorandum to the Board, which was being distributed at the meeting. A copy of that Memorandum is attached to these minutes.

A general discussion of these problems by the Board followed.

Mr. Kummerfeld stated that he agreed with the point that the critical need was for long-term Federal financing for the City, so that the City can eventually re-enter the credit market on its own. He stressed, however, that equally important are the issues related to the City budget.

Mr. Toia indicated that the City had not yet taken a position with regard to a long-term monitor for the City.

**Sinking Fund Installments**

Mr. Keilin stated that under provisions of certain of the Corporation's bond resolutions, approximately $34 million in Sinking Fund Installments were due by July 1, 1978, that such obligations could be met by open market purchases until mid-May, and that the Finance Committee would be considering authorizing specific purchases during that period with funds available to the Corporation.

**Adjournment**

There being no further business before the meeting, it was, upon motion duly made, seconded and carried, adjourned at 11:15 a.m.

Stephen J. Weinstein
Secretary
The purpose of this memorandum is to suggest that you "Fasten your safety belts", we are about to enter a storm fully as dangerous and unpredictable as any we weathered in 1975.

The basic factors we have to contend with are the same: City, State and Federal governments; City and State pension systems; labor and banks; and public credit markets. Some of the players on the scene are new: new administrations in Washington and New York City; and a changeover at the Federal Reserve. Some of the political realities are different: election year in New York State; election year in the House of Representatives.

At a meeting of our Finance Committee on January 5, 1978, we discussed the complexities of the forthcoming events in order to find a coherent strategy. It was suggested that I reduce these thoughts to writing in order to have a full Board discussion and policy formulation.

Our basic financing policy is still as set out in our memorandum to Governor Carey dated November 21, 1977. It is based on our analysis indicating that the key problem facing the City is long-term financing. The long-term financing needs of the City over the next four years are estimated to be $5.5 billion. This amount would provide for: financing a program of true capital expenditures; bonding out the $800 million State advance; refunding some City and MAC bonds coming due in the next few years; accelerating the elimination of expense items from the City's capital budget, and financing the expense items remaining in the City's capital budget.

Long-term financings sufficient to accomplish these purposes would enable the City to take steps to diminish substantially its need to do seasonal financing. Furthermore, they would furnish significant budgetary relief for the City, and provide a basis for a program of economic development.
B. SEQUENCE OF EVENTS -- An analysis of the probable sequence of events makes the problems more visible. The Treasury will have to arrive at a position in time to have an Administration position in place between January 20 and the beginning of the House hearings February 21. Realistically, the Treasury, in my judgement, can only adopt one of two approaches:

1. Support some variation of an extension of the seasonal loan program; or

2. Support some variations of long-term financing assistance.

The Treasury will insist, however, prior to committing itself, on hearing from the various parties what they are willing to contribute to the Plan. This may include:

1. City. Budget actions with respect to deficit; acceleration of expense item phaseout from its capital budget.

2. State. Possible additional State aid and/or creation of a special State fund as part of a plan to provide Federal guarantees for bonds; seasonal financing assistance.

3. City Unions. Outline of labor settlement with cost-estimate; possible additional investments by the pension funds, whether long-term or seasonal.

4. State Unions. Possible investments, either long-term or seasonal.

5. Banks. Possible investments, long-term and/or seasonal.

6. State/Legislative. Establishment of long-term fiscal monitor for the City; increase MAC borrowing authority and permit MAC to do capital financing for the City.

C. PROBLEMS -- The first problem is obviously the City-State plan to be submitted by January 20. Although MAC has proposed a City financing plan, the difficulties in developing a four-year City budget plan are enormous. Asking for agreed upon State actions within the framework of such a plan makes it more difficult still. Estimating Federal actions is difficult and totally speculative. We had suggested limiting the plan to a 1979 City budget and financing plan which would include accelerated phaseout of expense items from the capital budget, but, so far, we have not been successful.
MAC believes that these financings are necessary in order to make the City a viable financing vehicle capable of standing on its own without continuing Federal help. Without Federal assistance in the form of long-term loans or guarantees, neither MAC nor the City, alone or together, has the capacity to provide such financing. With appropriate Federal assistance in the long-term financing area, the seasonal financing problem becomes almost irrelevant; however, with only seasonal assistance from the Federal government, the City is likely to be unable to meet its financing needs in the 1979 to 1980 period and bankruptcy at that time, if not earlier, becomes a real possibility. With no financing assistance of any kind from the Federal government the City will run out of cash at mid-year.

A. TIMING -- A critical time problem confronts us. The Treasury has asked for a City plan by January 20, 1978. Based on this City (and presumably State) plan, the Administration will decide on the appropriate Federal role. This Federal role will then be the basis for legislative hearings in the House (Representative Moorhead) beginning February 21, and in the Senate (Senator Proxmire) beginning the latter part of March. Legislation would then be processed in both Houses in the May to June period.

Other actions, operating on their own schedule, will also occur. It is well to bear those in mind since one of the critical problems here will be a timely coordination of the various factors.

The State budget has to be adopted by March 31.

The State Spring borrowing, in the amount of about $4 billion, takes place around April 15, 1978. The Spring borrowing produces, among other things, the $800 million Spring advance to the City.

Labor negotiations will begin early in February. The Transit contract expires March 31, 1978; other major municipal labor contracts expire in June.

The City Pension systems are committed to purchase about $800 million in City bonds in the March-April period. This is the last of their $2.25 billion commitment to June 30, 1978.
Assuming successful resolution of the City-State plan by January 20, we now come to the problem of the Treasury's position. The challenge to negotiating commitments from the various parties during the period from January 20 to February 21 is enormous; it is rendered even more extreme by the fact that the commitments to be made could vary widely depending on the financing plan the Treasury will support. This is true because the choice between seasonal financing and long-term financing has definite budgetary implications. For instance, the financing plan outlined in our November 21, 1977 memorandum, which includes long-term Federal assistance, provides significant budgetary relief for the City which seasonal financing would not permit. It is obvious that the State, the unions, the banks and others will be required to take different positions depending on the Treasury's policy. It is difficult to see how this chicken-and-egg problem will be resolved.

Another which-comes-first problem involves the State Pension Systems. Until the State's Spring borrowing is completed, the State Comptroller is likely to withhold commitments by the State Pension Systems on the ground that they may be needed to finance the State. However, his refusal to give such commitments increases the uncertainty with respect to a City Plan, which in turn increases the possible risk to State public financing. Both Treasury and Congressional committees are insisting on a role for the State Pension Systems. Such a role, prior to April, may be very problematical.

For the City and the municipal unions to have an outline of both a wage settlement and investment commitment within this time frame appears equally difficult. Nor should one take for granted the City Pension System investment scheduled for March-April absent a Federally supported financing plan.

Accordingly, we believe that it will be necessary for the Treasury, after consultation with all parties, to announce that it will propose and support a specific Federal legislative program contingent upon all other parties agreeing to take specified actions to aid in the solution of the City's long-term financing problems.

D. POLITICAL AND ECONOMIC DEVELOPMENTS -- Since mid-December, the prices of MAC bonds have dropped by between 5 and 10 per cent. This price erosion began at the time of the Senate and House hearings and accelerated after the disclosure last week of the letter from Senators Proxmire and Brooke to President Carter. Our most recent $250 million
public offering was severely impacted and no further MAC financing can be envisaged until this whole situation is resolved, probably May-June at the earliest. Although the entire market erosion cannot be laid at the door of the Senate Banking Committee, there is no question that the hostility to New York, culminated by the recommendation to discontinue further aid, had a material impact.

This difficult situation is likely to continue for many months. Differences between the City and State on budgeting matters and between the City and unions on contracts, as well as difficulties with State financings, are all likely. These could take place against a backdrop of Congressional controversy and a deteriorating national economic picture.

It must be remembered that the continued crisis of the dollar abroad has potentially serious repercussions on our financing picture: increased interest rates to protect the dollar, a down-market and cutbacks by foreign central banks in their purchases of United States Treasury Securities. The resulting huge amounts of Federal financings, done at higher rates, domestically, could create a dramatically difficult environment for us to cope with.

In planning ahead to avoid events, such as City and even potential State insolvencies, of possibly massive negative economic and social impact, considerable margin for error should be built in to cope with the problems outlined above. This is true for time factors as well as estimates of best case -- worst case scenarios. It is most troubling to me that I see no such margins anywhere in these scenarios. On the contrary, the Proxmire-Brooke letter suggests a view of the problem that is so far removed from reality as to require a tremendous struggle and luck for the City to wind up with a program (i.e., seasonal loans) that is inadequate to do the job and that was initiated by a President who told the City to "Drop Dead."

E. MAC'S ROLE -- Under these perilous circumstances it behooves this Board to consider our policy carefully. We have two basic obligations:

1. The protection of our bondholders, owning over $5 billion of securities.

2. The financing of the City to maintain it as a viable social and economic unit.
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MEMORANDUM/F.G. Rohatyn
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I believe that we have built up, over the past three years, a kind of know-how and public credibility based on our independence from political pressures and the fact that we have no axes to grind. We will once more be put to a serious test. We must, at all costs, continue to be totally independent of political considerations while being alive to political realities; we must be willing to be catalysts, bearing in mind that catalysts sometimes turn into lightning rods.

I believe that we should continue to explain and emphasize our belief that only long-term Federal financing assistance will allow us to say that this is our last request of the Federal government. Within that framework we should be as flexible and innovative as possible. If long-term loans are unacceptable, we must try guarantees. The State, and probably the City, should participate in any program to provide Federal guarantees for MAC bonds. In order to limit the precedent, guarantees might be limited to those securities purchased by the City and State pension systems. We might, within the framework of a plan such as we propose, be able to eliminate seasonal requirements entirely. But the basis of the plan has to be long-term financing.

As I indicated above, the political conventional wisdom seems to indicate that enormous struggle will be required to achieve a mere extension of the seasonal loan. It bodes ill for our system to think it cannot come up with any answers other than the least common denominator which everyone knows will not work, but may buy a little time. If that is the ultimate result, the record must clearly show that we did not believe in it. The New York financing problem can be solved; it is not that complicated. It needs leadership from the Administration and political courage on the part of Congress. It will not be done by pretending that a band-aid is therapy.