The Honorable G. William Miller  
Secretary  
H. S. Department of the Treasury  
Washington, D.C.

Dear Mr. Secretary:

The Committee on Banking, Housing and Urban Affairs held oversight hearings on the New York City Loan Guarantee Act on January 28 and 29 and February 7, 1980. The purpose of the hearings was to determine whether the requirements of the Act are being met and to assess what progress New York City is making toward balancing its budget in accordance with generally accepted accounting principles and toward regaining access to the credit markets. Witnesses at the hearings included the Assistant Treasury Secretary for Domestic Finance, the Mayor of New York City, the City Comptroller, the President of the City Council, the Governor of New York State, the Chairman of the Municipal Assistance Corporation, officials of the various New York City oversight agencies, City employee labor union leaders, and representatives of the municipal bond rating agencies and the financial community.

We understand that New York City is scheduled to receive $100 million in Federal guarantees on February 21, the final allotment of the $750 million of the "upfront" guarantees committed to be issued under the financing arrangements pursuant to the Act. Since you are required to make a number of determinations before providing these guarantees, we thought it advisable to share with you as soon as possible our views with respect to New York City's financial situation, based on information obtained in the oversight hearings.
The Honorable S. William Miller

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We are pleased to learn from the Treasury testimony and from other witnesses that New York City is not likely to need any additional Federal guarantees beyond the $750 million already committed. It is our understanding that the remaining $200 million in guarantees authorized will be held in stand-by and that under the Act, further guarantees can be provided only in the event that both the City and the Municipal Assistance Corporation are unable to market their bonds in the necessary amounts, or in event that the Treasury does not foresee occurring. We view this both as an indication of the City's progress toward financial recovery and as a welcome limitation on the extent of the Federal government's exposure.

At the same time, however, we want to make it very clear that we expect the Treasury to continue to monitor New York City's operations closely in order to ensure continued compliance with all of the conditions of the Act and to protect the Federal government's financial interest. It is evident that the Treasury's authority to require changes in the City's Financial Plan or other actions pursuant to the Act does not end with the last issuance of Federal guarantees, but rather continues so long as the guarantee program is in existence, and beyond that, there is a responsibility to assure repayment of any guarantied loans outstanding. We expect the Treasury to be vigorous in its exercise of this authority, just as the Committee will continue to take seriously its responsibility to oversee the administration of the Federal loan guarantee program.

In our view, the most important and positive development in New York City's financial situation since the last round of oversight hearings a year ago is the Mayor's decision, announced in his January 16, 1980 Financial Plan for Fiscal Years 1980-1981, to balance the City's budget in accordance with generally accepted accounting principles (GAAP) next year, fiscal year 1981, a year earlier than required by both State and Federal law. We commend the Mayor for his decision, as did other members of the Committee and most of the witnesses at the oversight hearings. At the same time, however, we see this step as more than commendable. It is absolutely necessary. The testimony given in the hearings made it clear that real budget balance in 1981 is essential, both to enable the City to eliminate large budget deficits projected for 1980 and subsequent fiscal years, and also to place the City on a course toward regaining access to the long-term bond market.
The important question which remains is whether New York City can actually accomplish that GAAP-balanced budget in fiscal year 1981. This depends to a large degree on actions by other parties, including the City Council and the State Legislature. It also depends on the achievement of a modest labor settlement for fiscal years 1981 and 1982, along the lines of that agreed to in 1978.

We believe it is vital that the GAAP-balanced budget projected for fiscal year 1981 be achieved. The Committee was told that failure to do this would be a serious setback to the City's prospects for regaining access to the long-term bond market. Since the purpose of the Federal Loan guarantee program was to give New York City time to get its financial affairs in order, and since there is little disposition on the part of the Committee or the Congress to provide additional guarantees after June 30, 1982, it is essential that the City make steady progress toward regaining market access. Accordingly, we recommend that the Treasury work closely with City and State officials to see that the Financial Plan scheduled to be approved by the Financial Control Board on February 21 gives strong assurances that New York City will achieve a balanced budget in accordance with generally accepted accounting principles in fiscal year 1981 and will maintain such a balanced budget in 1982 and in subsequent years.

In order to obtain such assurances, there are certain problem areas in the Mayor's January 16 Financial Plan which need to be addressed. These include the assumptions of additional State and Federal aid in fiscal years 1981 and 1982, the projected reductions in spending for certain non-agency agencies, and the potential impact of the labor contract settlement to be negotiated this spring for fiscal years 1981 and 1982.

The January 16 Financial Plan projects additional Federal and State aid for budget-balancing purposes in the amount of $170 million in fiscal year 1981 and $410 million in fiscal year 1982. With respect to the $170 million for 1981, the Committee was told that the City expects $70 million to come from the State. However, the Mayor has claimed that not only is the $70 million in additional aid not in the proposed 1981 State budget, but also that State plans to cut aid to the City by some $75 million, leaving a potential shortfall of $148 million. The Governor, on the other hand, told the Committee that this was not the case and that the $70 million in additional State aid would be forthcoming, although not necessarily in the form expected by the Mayor. We urge
As regards Federal aid, the City has indicated that it expects $100 million in additional aid for budget balancing purposes, and the Treasury testimony indicated that that amount was realistic. However, the Committee was told that the major portion of that $100 million would come from the countercyclical aid legislation now pending before Congress, which was expected to yield somewhere in the neighborhood of $45 million, or half of the expected amount. Subsequently, the House of Representatives passed a countercyclical bill which could cut the expected amount in half. We believe that the Treasury should weigh the consequences of that potential reduction in countercyclical aid in determining the likelihood of the City's obtaining the projected $100 million in additional Federal aid in fiscal year 1981.

As regards the $410 million in additional State and Federal aid for fiscal year 1982 (the $340 million more than in 1981), witnesses at the hearings were more doubtful as to whether this could be achieved. Given the fact that the State is facing financial problems and the Federal government is under strong pressure to reduce the budget deficit, it may not be realistic to expect substantial increases in aid to New York City in each succeeding fiscal year.

In the course of the hearings, the Committee was told that the Financial Control Board, in its approval of the January 16 Financial Plan, would require the establishment of reserves to cover any potential shortfalls in State and Federal aid. We recommend that the Treasury scrutinize carefully the amount of reserves required for this purpose to determine whether they are adequate to provide strong assurance of a balanced budget in 1981, prior to the issuance of the Federal guarantees in late February. Any increase in reserves would, of course, require that the City show equivalent reductions or other budget savings elsewhere in the Plan.

Another problem area in the January 16 Financial Plan concerns certain agencies which are not directly under the Mayor's control, notably the Board of Education and the Health and Hospitals Corporation.
The City is projecting savings of $10 million in the Board of Education budget in Fiscal Year 1981 and a reduction of $20 million in the deficit of the Health and Hospitals Corporation. Similar reductions were projected for the present fiscal year, 1980, but instead the City ended up spending more than anticipated. Thus, it is questionable whether the projected savings in these agencies can be achieved.

We know that the Treasury has long pressed for substantial reductions in spending in these areas. Also, the Financial Control Board has required the City to impose additional controls on these agencies in the current fiscal year. The Treasury should examine closely the financial plans approved for the Board of Education, the Health and Hospitals Corporation, and any other non-rayal agencies, in order to determine whether the budget savings projected for fiscal years 1981 and 1982 are likely to be achieved. In particular, there should be a determination as to whether adequate reserves have been established to cover any potential shortfalls in the realization of such savings, prior to the issuance of the Federal guarantee.

Another major problem for the City's budget-balancing efforts is the new City employee labor contracts, which are now under negotiation and which will cover the fiscal year 1981-1982 period. The January 16 Financial Plan allows for a four percent annual increase, along the lines of the present contracts. However, the City labor union leaders stated they would push for far higher increases. The Committee was told that any increase beyond the projected level would cost the City an additional $50 million in each fiscal year. According to the Special Deputy State Comptroller, a 7 percent annual increase in pay rather than a four percent could cost the City $200 million more in 1981 and $375 million more in 1982, and could raise the projected 1984 budget deficit to over $1 billion. Thus, it is vitally important that the cost of the new labor contracts fall well within the City's ability to pay.

We realize that the collective bargaining process has just gotten underway. However, in view of the importance of this matter, we believe it is essential that the Treasury obtain some assurances that the labor settlement reached will not impose the City's ability to achieve real budget balance. Under State law, the Financial Control Board has the authority to reject any contract which is not in consonance with the City's Financial Plan. Therefore, we urge that the Treasury obtain from the Financial Control Board a commitment to reject any labor contract settlement which could cause the City to fail to achieve a balanced budget in accordance with generally accepted accounting principles in Fiscal year 1981 or 1982, as a condition for providing the Federal guarantee.
It appears that the achieving of a GAAP-balanced budget is a necessary but not a sufficient condition for the City’s regaining market access. The purpose of the New York City Loan Guarantee Act was to assist the City in meeting its short-term seasonal and long-term capital financing needs over the four-year period ending on June 30, 1982, after which the City was expected to be fully back in the credit markets and able to meet all of its financing needs on its own. In order to stimulate the City to make progress toward this goal, the Act requires the City to sell its short-term notes in the public markets in fiscal years 1980, 1981, and 1982, and to do public sales of its long-term bonds in fiscal years 1981 and 1982. The City is required to do this unless the Secretary determines that it would be inconsistent with the City’s financial interest.

In the course of the oversight hearings, the Committee found that New York City has made considerable progress toward meeting its short-term seasonal financing needs in the public market. First, it has, by various means, reduced those needs substantially -- from $2.1 billion in fiscal year 1977, under the Federal seasonal loan program, to $600 million in the current 1980 fiscal year. Second, the City sold $275 million in notes last year, 1979, a year earlier than required by law. Third, the City has sold $375 million in notes this year, and expects to meet the full $600 million in seasonal financing in the public markets, without having to resort to a back-up financing facility provided by a consortium of financial institutions. Barring any serious, adverse developments in the markets, it is anticipated that the City will continue to meet all of its seasonal financing needs in the public market in fiscal years 1981 and 1982, although back-up facilities will continue to be arranged.

It should be pointed out, however, that thus far the City has only been able to market revenue anticipation notes (RAN’s), which are issued in anticipation of State aid payments to the City and, therefore, are more a reflection of the State’s credit than the City’s. The Committee was told that the City had explored the possibility of selling tax anticipation notes (TAN’s), which would be backed by City real estate tax collections, but that this had not been encouraged because of the prospect of receiving a satisfactory rating on those notes. It was stated further that strategic goals for fiscal year 1981 could include: a note sale through competitive bidding by underwriters, rather than through negotiation; a sale of TAN’s; and obtaining a better rating on the City’s notes. We believe that the Treasury should encourage the City to make efforts to accomplish these goals, in order to show a record of continual progress toward improving its access to the market for short-term notes.
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The City's ability to meet the requirement of public sales of its long-term bonds in 1981 and 1982 appears to be more problematical. The January 16 Financial Plan projects sales of $300 million in City bonds in 1981, $645 million in 1982, and then $1,177 million in fiscal years 1983 and 1984, after the Federal Loan guarantee program has expired. In addition, the plan includes private placements of MAC bonds in the amounts of $537 million in 1981 and $323 million in 1982, and it indicates that public sales of additional MAC bonds will be carried out should sales of City bonds fall short of projections.

The Committee was told that there is probably some market for City bonds at this time, largely of a speculative nature, but that full market access for substantial amounts of long-term City bonds is not likely to occur until after the City obtains an investment grade rating on its bonds. These bonds are currently rated "B" by Moody's Investors Service -- two notches below the lowest investment grade rating (Baa) -- while the other agency, Standard and Poor's, suspended its rating in 1975 and has not yet reinstated it. Witnesses from both of these agencies told the Committee that New York City will probably have to establish a record of consecutively balanced budgets in accordance with generally accepted accounting principles over at least a three-year period in order to regain an investment grade rating on its bonds.

Testimony at the hearings revealed differences of opinion as to whether New York City should attempt a bond sale in the absence of an investment grade rating and what amounts could be sold under those conditions. The Mayor and the City Comptroller indicated that the City intends to comply with the requirements of public bond sales in 1981 and 1982 and that efforts toward this would proceed next fall, after the City has an audited financial statement for fiscal year 1980. However, the view was expressed that a sale of less-than-investment-grade City bonds to a basically speculative market would not be a real measure of market access and could even be counterproductive.

The Committee has generally taken the position that it is vital for New York City to do public sales of its bonds as soon as possible in order to establish a track record. However, it is reasonable to contend that this should be done in a context which will enable the City to make real progress toward regaining full access to the long-term bond market. Accordingly, we urge the Treasury to work with the City and its financial advisors to explore fully the potential for complying with the bond sale requirement in the Act, while recognizing that the requirement can be waived if it is determined that compliance would not be consistent with the City's financial interests.
The possibility that the City bond sale targets for 1981 and 1982 may not be met raises the question of whether the projected $1.277 billion in City bond sales for fiscal years 1983 and 1984 will be accomplished. Witnesses at the hearings said this was doubtful even with an investment grade rating, and probably impossible without one. In view of the fact that there are not likely to be additional Federal guarantees authorized after 1982, it is imperative that New York City find alternative means of meeting its long-term financing needs during the transition to full market access after the loan guarantee program ends. In the course of the hearings, several potential alternatives were discussed.

First, the Municipal Assistance Corporation could continue to aid the City in meeting its long-term capital financing needs, as it has done since 1973. The Committee was told that an increase in MAC's borrowing authority from $6.8 billion to $10.1 billion would enable the Corporation to do all of the City's long-term financing through fiscal year 1984, and that there is sufficient economic capacity in the revenues supporting the MAC bonds to permit such an increase. Both the Governor and the Chairman of MAC stated they would recommend that the New York State Legislature approve such an increase in MAC's borrowing authority. We believe that such legislation be enacted as soon as possible, and we urge the Treasury to work with New York State and City officials to accomplish this. This would give the City a "safety net" to back up sales of its own bonds. We also feel, however, that it is in the interests of all concerned that the City regain the ability to finance itself fully as soon as possible. Accordingly, the MAC borrowing authority should only be available as standby, to be used to the extent that City bond sales fall short, and it should be made clear that MAC is not intended to replace the City as a long-term borrower on a permanent basis.

A second alternative which the Committee was told the City could pursue is the establishment of special enterprise agencies, such as a water and sewer authority, which would do revenue bond-type financing for their own purposes. It was stated that this device had been successful in other cities with fiscal problems. On the other hand, the Committee was also told that there were certain legal problems connected with this approach. We urge the Treasury to encourage the City and State to explore the possibility of establishing such enterprises and to deal with any legal problems involved, so that the City will have other means available for meeting its long-term financing needs after the Federal loan guarantee program ends.
Another alternative to explore would be the possibility of obtaining commitments from New York City financial institutions and pension funds to purchase additional amounts of MAC and/or City bonds during the transition period after 1982, along the lines of the present four-year financing plan pursuant to the Act. If the City continues to make progress toward financial health, there would seem to be little reason why the financial institutions could not make such additional commitments, at least on a stand-by basis, given the growth in their own financial capacity over the four-year period. Additional City pension fund commitments would present some special problems, since this would require extension of the current Federal legislation providing certain tax law exemptions for this purpose. Nonetheless, it is also true that the pension funds' investment in New York City obligations will have been reduced considerably by the end of the four-year period, thus making the assumption of any new commitments relatively less onerous. While the latter prospect appears more remote than that of additional commitments by the financial institutions, it should not be ruled out. We recognize that it is too early for the City to obtain any such financing commitments for the post-1982 period, and that the need has not yet been established. Nevertheless, we believe it is important to suggest the possibility of doing it at this point, since this would be a logical extension of past practices.

In considering New York City's ability to meet its long-term capital financing needs, questions can be raised about the City's projections of those needs. With a GAAP-balanced budget in 1981, the City will be borrowing long-term only for "true" capital purposes. And while the need for upgrading the capital plant is undeniable, the Committee has long questioned whether the City has the capacity to carry out its full $2.5 billion capital plan by 1982, in view of the fact that its actual capital spending has continued to lag far behind projections. This has implications for the post-1982 period as well, since it means that the spending on the City's ability to raise over $1 billion a year in the bond market should be coupled with questions as to whether it can really spend that amount in any event. However, the City continues to claim that its capital spending projections are correct, and the Mayor pointed to improvements made in the capital planning process and to recent monthly increases in capital spending figures to back up this contention.
We continue to be skeptical about the City's ability to achieve its full $2.3 billion capital plan by 1982 and to sustain the levels projected for succeeding fiscal years. While it would be premature to require the City to revise its projections at this point, if the prevailing trend toward underspending for capital programs does not turn around within the next fiscal year, then the Treasury should encourage the City to reduce its capital spending and long-term financing figures to a more realistic level. Given the questions about the City's ability to raise $1 billion a year in the market in any case, it would seem counterproductive to project such amounts if they are not likely to be needed.

The Committee was told that the basic test of New York City's ability to regain access to the bond market will be its ability to sell bonds outside of the New York area. Without access to a nationwide market, there is no way that New York City can meet all of its projected long-term financing needs. Witnesses at the oversight hearings stated that there are various steps that New York City can take to enhance its appeal to out-of-state investors. In addition to the steps mentioned above -- achieving and maintaining a balanced budget, successfully concluding the labor contract negotiations, and rehabilitating its capital plan -- the Committee was told that the City needs to build a more credible and vigorous economic development capability, in order to provide greater assurance of future financial health. We urge the Treasury to work with City officials to ensure that such an effort is in place and ongoing, as a necessary support to the city's efforts to regain market access.

Sincerely,

[Signatures]

William Proxmire
Chairman

Joe Carn
Ranking Minority Member
TESTIMONY BY
FELIX G. ROHATYN, CHAIRMAN
MUNICIPAL ASSISTANCE CORPORATION FOR THE CITY OF NEW YORK

BEFORE
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE

FEBRUARY 7, 1980
Mr. Chairman, Members of the Committee:

I would like to report on the status of the Four Year Debt Issuance Plan and MAC's participation in that financing package, as well as our view of the City's budget and our future prospects. We are reaching the halfway mark of this program which was constructed in 1978. The aggregate 4-year financing package amounting to $4.5 billion called on MAC to raise $2.8 billion through public and private sales of MAC Bonds, for the City to sell $750 million in federally guaranteed bonds to union pension systems and New York City bonds in the amount of $950 million to be sold publicly in the last two years of the Plan. As backups for contingencies were $900 million of guarantees available under the law and significant additional economic capacity of MAC which I will come back to later in my Testimony.

The financing plan is evolving on schedule. As called for in the timetable, MAC has so far issued a total of $1.8 billion of its bonds-- $901 million during fiscal year 1979 and $948 million to date during fiscal year 1980. The $1.8 billion has been raised from the following sources:

--$938 million from private placement to various financial institutions and City Pension Funds according to the terms of the November 1978 Agreement,

--$64 million from an exchange with the New York State Insurance Fund, and
--$847 MILLION FROM PUBLIC SALES

As a direct result of these financings, the City's seasonal borrowing requirements have been reduced from approximately $1.9 billion required in 1978, to approximately $650 million required during fiscal years 1979 and 1980. The short-term credit market viewed this development positively, enabling the City to sell publicly, for the first time since 1975, $275 million of its Notes to meet a portion of its 1979 seasonal financing requirements.

To date, during fiscal year 1980, the City has sold $350 million of its Notes publicly, and expects to meet the balance of its 1980 seasonal requirements from public sales.

A portion of the Corporation's issuances under the plan aggregating $642 million have been for refunding. The refundings have produced a more stable debt service structure which will assist MAC in meeting possible shortfalls in the City's own long-term financing program. They have also been accomplished so as to reduce MAC's average interest cost for the refunded debt by over 100 basis points at a time of an unprecedented climb in the level of interest rates. The refundings have also produced approximately $250 million of net budgetary savings for the City for the period 1980 to 1985, ahead of the schedule committed to at the time of the first Four Year Plan. During
The 1975-76 period, as you will surely remember, MAC had to refinance some $5 billion of City short-term Notes and to finance the City's operating deficits and capital programs. This occurred during difficult markets and under conditions that were often chaotic. The resulting debt structure included many short-maturity, high interest series of bonds which created enormous budgetary pressures at the time of greatest fragility for the City. This is what we have been dealing with in our overall program to level out our maximum debt service at roughly the $650 million per annum level. Although we have not yet reached that level, it is noteworthy, that, with $6.18 billion in presently outstanding bonds, MAC's maximum debt service in any future year is approximately $780 million while New York City, with about $6 billion in bonds outstanding has current debt service of about $1.1 billion per annum. Lowering our maximum debt service obviously gives MAC greater economic capacity to carry the City in times of need. Furthermore, as long as it remains obvious that inflationary expectations will remain at or near double digit rates, stretching out our debt instruments to 20-25 years at 8-9% interest rates seems to me to be a clear and simple duty. If current trends continue we may, in a few years, no longer have viable markets for long-term, fixed interest rate bonds in this country; we need only to look to Europe for examples.

With regard to the City's budget, it has been the position of the Corporation for some time that the adoption of those
MEASURES WHICH ARE ULTIMATELY REQUIRED TO ACHIEVE BALANCE SHOULD NOT BE POSTPONED UNTIL THE FINAL YEAR OF THE PLAN. WE HAVE BEEN CONCERNED THAT GAPS NOT BE CLOSED PRIMARILY ON THE REVENUE SIDE OF THE BUDGET. A SERIES OF NONRECURRING REVENUES, AS WELL AS REVENUE INCREASES RESULTING FROM INFLATION, PROVIDE AN INSECURE FOUNDATION ON WHICH TO BUILD CREDIBLY BALANCED BUDGETS. THEREFORE, WE APPLAUD THE DECISION OF THE MAYOR TO SUBMIT A BUDGET BALANCED ACCORDING TO GENERALLY ACCEPTED ACCOUNTING PRINCIPLES ONE YEAR BEFORE IT IS REQUIRED. IT IS A SINGULARLY IMPORTANT STEP. IT IS AN ACTION FOR WHICH THE MAYOR SHOULD BE COMMENDED, FOR IT DEMONSTRATES CLEARLY A RECOGNITION BY THE CITY OF THE NEED TO ACT WITHOUT DELAY AND THE WILLINGNESS TO IMPLEMENT PAINFUL, BUT NECESSARY, BUDGET CUTS.

Further, the City has to date not succeeded in ministering to its own physical needs. The resources made available to it in this Four Year Financing Plan have not yet been fully applied to those deteriorating streets, sewers, bridges and parks which require immediate attention. The City, together with the State and its agencies, must develop the capacity to plan and execute the restoration of its physical plant. The City and State together must put greater focus on the job-creating, revenue-producing side of the economy that, in the long-run, is going to be the key to our success or failure.

The achievement by the City of a GAAP balanced budget now, and the prospects for repeated balanced budgets in the future, continue to be the single most important test for gaining entry into the credit markets. It is the mark of fiscal stability toward which the investment community has looked since the City's crisis began. While the City does not now have market access for its bonds, the adoption and implementation of a balanced budget for fiscal year 1981, and, the adoption in June 1981 of a balanced budget for fiscal year 1982 should encourage those agencies which rate municipal bonds to recognize the progress which the City has made and assign an investment-grade rating to long-term City securities.

It comes, however, as no great surprise that investment rating services such as Moody's would be more than normally skittish with respect to rating City bonds. The history of the City,
THE MASSIVE AMOUNTS INVOLVED, THE ECONOMIC TRENDS CLEARLY ADVERSE TO THE NORTHEAST, THE CURRENT TRAVAILS OF CHICAGO, CLEVELAND, PHILADELPHIA, ETC. ALL CONTRIBUTE TO THEIR RESERVE. IN EARLIER TESTIMONY IN FRONT OF THIS COMMITTEE I STATED MY VIEW THAT 2 OR 3 CONSECUTIVELY BALANCED BUDGETS UNDER GAAP MIGHT BE REQUIRED TO PROVIDE FULL MARKET ACCESS TO THE CITY. I BELIEVE MY PREDECESSOR, GEORGE GOULD, GAVE A SIMILAR VIEW IN TESTIMONY LAST YEAR. ALTHOUGH THE FOUR YEAR PLAN CALLS ON THE CITY TO SELL $300 AND $650 MILLION OF LONG-TERM BONDS IN FISCAL 1981 AND 1982 RESPECTIVELY, IT WAS ALWAYS RECOGNIZED THAT THIS MIGHT BE OPTIMISTIC AND THAT MAC SHOULD BE THERE AS THE FIRST BACKUP, BEFORE THE AVAILABLE LOAN GUARANTEES. THIS IS THE CASE, NOT ONLY THROUGH 1982 BUT, FROM AN ECONOMIC CAPACITY POINT OF VIEW, INTO 1984 AND POSSIBLY BEYOND. DURING THIS PERIOD OF TIME, THE MUNICIPAL ASSISTANCE CORPORATION IS PREPARED BOTH TO FULFILL ITS OWN PART OF THE FOUR YEAR DEBT ISSUANCE PLAN, AND TO ISSUE SUCH ADDITIONAL DEBT AS MAY BE REQUIRED BY THE CITY'S CAPITAL PROGRAM, WHICH WAS TO BE MADE UP OF CITY BONDS.

AS YOU ARE AWARE, MAC'S ABILITY TO ISSUE DEBT IS CONSTRAINED ON SEVERAL LEVELS:

- THE ECONOMIC CAPACITY TO ISSUE AND SUPPORT DEBT IS LIMITED PRINCIPALLY BY TWO TESTS. THE CORPORATION HAS COVENANTED NOT TO ISSUE ADDITIONAL FIRST RESOLUTION BONDS IF THE MAXIMUM ANNUAL DEBT SERVICE PAYMENTS UNDER
that Resolution in any future year would exceed $425 million. MAC has further convenanted not to issue additional Second Resolution Bonds unless available revenues would cover maximum annual debt service payments under that Resolution in any future year at least two times.

It is difficult to give you an exact estimate of MAC's additional economic capacity (as opposed to market acceptance) to carry debt. The obvious variables are revenue assumptions on the one hand, and assumptions as to the type, maturity and interest rates on our bonds on the others. It would be reasonable to assume at this point, that by 1984, given continued satisfactory market acceptance, MAC could comfortably support an aggregate in excess of $10 billion of outstanding long-term debt.

MAC's statutory capacity to issue debt (exclusive of the bonds issued for refunding) is $8.8 billion. To date, the Corporation has issued $6.8 billion.

The Bond Purchase Agreement (under which $2.8 billion of MAC bonds are to be sold as part of the Four Year Debt Issuance Plan)
also limited the level of outstanding bonds to $8.8 billion. That agreement further prohibits MAC from issuing other than First or Second Resolution Bonds until such time as the City has an investment-grade rating.

The capacity of the credit market to absorb new MAC debt limits the amount we can issue in any year. This is especially true in markets as irregular as the ones we are now experiencing. We are told by our managing underwriters that $600-$750 million of new debt is the maximum we should attempt to sell in one year.

Despite these constraints, MAC has the capacity to assist the City beyond the scope of the current Plan. The Corporation is already scheduled to place, pursuant to the Bond Purchase Agreement, $537 million of its Bonds in 1981 (of which $353 million is for capital purposes) and $324 million of its Bonds in 1982. It is our estimate that the City’s needs will require that MAC issue approximately $675 million in fiscal years 1981-82 over and above the Plan in order to fund both the City capital and the Corporation’s debt service reserve requirements, if the City fails to market its own securities. This would bring MAC to the end of the Four Year Plan with an aggregate $8.3 billion of debt issued.

Beyond 1982, we anticipate that the City’s capital needs will be in the range of $850-$900 million per year. If MAC were required to finance 100% of the City’s capital needs through
1984 on this schedule, our total issuance would rise to about $10.1 billion. I do not anticipate this happening. If the City continues on track, within a reasonable economic environment, the City capital funding requirements of 1983 and 1984 could be met through a combination of MAC issuances supplemented in ever-increasing amounts by the City's own debt. It is entirely plausible that the City, having implemented four consecutive GAAP balanced budgets and having successfully issued ever-larger amounts of debt for two years, would then be able to fully meet its own capital needs.

A scenario such as I have just outlined requires that MAC issue debt in 1981 and 1982 beyond that which is currently planned. We are prepared to do so. It also requires MAC to issue debt beyond its current statutory authorization. We are prepared to recommend to the Governor and to State Legislature that MAC's authority to issue debt be extended through fiscal 1984 and its ceiling raised by approximately $1.2 billion to $10 billion, thereby sustaining the City and its vital physical reconstruction activities without any additional Federal assistance.

Even though MAC carries the moral obligation of the State, I do not believe such an increase would adversely affect the State's credit. MAC is viewed by credit rating agencies and
INVESTORS AS ESSENTIALLY SECURED BY ITS REVENUE STREAM OF SALES TAXES AND PER CAPITA STATE AID. THIS STREAM OF REVENUE LAST FISCAL YEAR AMOUNTED TO $1.9 BILLION AS AGAINST MAXIMUM DEBT SERVICE REQUIREMENTS IN 1989 OF $786 MILLION. MAC, THEREFORE, SHOULD NOT BE A BURDEN AGAINST THE STATE'S GENERAL CREDIT. THE STATE'S GENERAL CREDIT SITUATION HOWEVER, DOES AFFECT MAC. WE WERE CONCERNED RECENTLY, WHEN UNCERTAINTIES WITH RESPECT TO THE STATE'S BUDGET CAUSED A SLIGHT DOWNGRADE IN THE STATE'S GENERAL OBLIGATIONS BY STANDARD & POOR'S. THE STATE'S CREDIT RATING, AS A PRACTICAL MATTER, CONSTITUTES A CEILING AGAINST WHICH MAC HAS TO OPERATE. IT IS VITAL TO MAC, AND TO THE FINANCING PLAN, THAT THE CREDIT AND BUDGETARY POSTURE OF THE STATE REMAIN IMPECCABLE. I HAVE SO STATED TO THE GOVERNOR IN THE STRONGEST POSSIBLE TERMS.

WE BELIEVE THIS PROGRAM SHOULD SEE THE CITY THROUGH. HOWEVER, WE MUST REMEMBER THAT, BY NOW, MAC HAS BECOME THE LARGEST ISSUER OF LONG-TERM MUNICIPAL BONDS IN THE COUNTRY, HAVING PASSED THE STATE OF CALIFORNIA SOME TIME BACK AND WE DO NOT REACH TO INFINITY.

A PERSUASIVE CASE CAN BE MADE FOR SUCH A SCENARIO AS I HAVE JUST DESCRIBED; BUT, IN LIGHT OF SOME OF THE TESTIMONY MADE TO THIS COMMITTEE ONLY LAST WEEK, WE MUST ALSO BE PREPARED FOR SOME ALTERNATIVE SET OF EVENTS. THEY MIGHT INCLUDE THE FOLLOWING:
A sharply deteriorating national economic and international monetary environment,

revenue assumptions included in the City's budget which fail to materialize,

expenditure reduction targets which are not fully met

a slower than anticipated process of restoring investment-grade ratings to City bonds, and

debt markets so tight that credits perceived as weaker, such as New York City, are denied full access

If some pattern of events similar to these were to materialize, the need to support the City's capital spending program might extend for a couple of additional years. While MAC might have ample economic capacity to do so, this should not be equated with unlimited market access. In such a case, --in order to avoid seeking additional Federal assistance beyond 1982 by extending MAC's ability to assist the City over a longer period-- it might become advisable to utilize some portion of those Federal guarantees which are available in 1982 under the current law. These guarantees, in supplement to MAC's issuing debt under the two Resolutions, and possibly issuing pursuant to a new Resolution, could carry the City even under this more severe set of circumstances, until such time as it could support itself.
Under normal circumstances this should not be necessary. We live in unusual times, however, and while I do not anticipate the necessity to make use of the guarantees in 1982, I cannot rule out that this second set of circumstances might occur. However, regardless of which one materializes, given a combination of:

--resolve on the part of elected City officials, to act decisively now, to bring the budget into balance,

--the cooperation of those governments which reside in Albany and Washington, and

--a viable economic environment for urban America

I do not anticipate that either the City, the State or MAC would turn to Washington after 1982 in search of additional financing assistance.
SUMMARY POINTS

Statements submitted to the Senate Committee on Banking, Housing and Urban Affairs

Ed Koch, Mayor
Harrison Goldin, Comptroller
Carol Bellamy, President,
City Council
Comer Coppie, PCB
Sidney Schwartz, OSDC
Stephen Berger, Consultant,
City Budget

MAYOR KOCH

1. Balancing the Budget

The accelerated plan for a GAAP balanced budget will do three things: early action will help close the enormous gap in 1982; the City's market reentry will be accelerated; with a balanced budget and market access the City will be financially self-sufficient and service delivery will be stabilized.

Persistent budget imbalance is caused, on the expenditure side, by mandated programs and inflation. The revenue side is hampered by sluggish growth locally as well as from the Federal and State governments.

The new Financial Plan includes substantial expenditure reductions as well as recognition of the need to increase local revenues. Expenditure reductions have been aimed at not reducing service delivery while revenue increases include those least likely to hurt the local economy.

Additional Federal and State aid called for in the Program to Eliminate the Gap (PEG) is less than called for in the 1978 Plan. The Governor is publicly committed to additional State aid for the City.

2. Financing

The bulk of the City's financing is being provided through local efforts. The City plans to use less than half of the $1.65 billion of Federal guarantees.
The financing plan is on schedule.

During FY 1979 the City sold $275 million of Notes publicly, one year ahead of schedule in Guarantee Act.

Seasonal borrowing needs have decreased by almost 70% since 1977 to $650 million in 1979.

We have expanded the credit facility negotiated with private lenders as a back up to public Note sales. Forty banks are now included and the need for Pension Fund participation has been eliminated.

3. Capital Spending

While I have not been pleased with past performance, planning and reporting systems are being overhauled and I am encouraged. A recent analysis has shown that while interim spending forecasts have required significant corrections, the $2.3 billion four year target remains our best estimate.

4. Market Access

Accelerating a GAAP balanced budget by one year should help significantly.

If we stick to the current Plan, our bonds will deserve an investment-grade rating.

I am committed to a public bond sale at the earliest possible date, however, the first sale must be a success.

I believe a successful bond sale will be possible in FY 1981.

If the City does not have full market access by the end of the Financial Plan then I will consider:

-creation of special purpose authorities, such as for water and sewer;
-authorization of additional MAC sales; and
-reduction of City's capital program

This program will not require additional Federal presence in City financing.
5. The Economy

A recession now should not have the disastrous impact of the one five years ago.

Since my election, 63,000 jobs have been added in the City.

Retail sales have shown surprising growth, 12% since 1978.

Construction sector has been strong—offices, apartments, the Convention Center.

Tourism is up.

Local inflation rate has been below national rate.

City is in a better position for recession, but its effects cannot be ignored.

HARRISON GOLDIN

"it does not follow as the night the day that once the City achieves GAAP balance everybody's uncle will be willing to lend the City whatever it asks for and needs."

The City has made enormous progress: operating deficit has been reduced from $1.87 billion to $422 million by June 30, 1979; there have been no rollovers of temporary debt; market reentry for short-term debt has been achieved; and the credit rating on City Notes has been upgraded by Moody's from MIG-4 to MIG-3. The State advance was eliminated, cash flow has improved dramatically, we had a cash surplus in 1979, the real estate tax collection rate in 1979 was 94% and a four year decline in assessed valuation of property has been reversed.

Goals the City has reached for FY 1980. The seasonal loan agreement has been negotiated with more banks than last year, the City has not needed this standby credit facility and the City is in the process of doing a fixed asset inventory.
31 January 1980
SUMMARY POINTS
Page Four

Goals the City has not reached: The City has not secured a rating upgrade on their Notes; all the Notes sold to date have been RAN's not TAN's; and the City has yet to sell Notes through competitive bidding by underwriters.

No doubt GAAP balance in FY 1981 will help City's fiscal position, but may not assure investment-grade rating for bonds.

The City has no choice but to be optimistic. The Financial Plan requires we try to sell $300 million of bonds in FY 1981 whether GAAP balance is achieved or not; whether the bonds win a good rating or not. Current plan is to offer $75 million each quarter starting July 1, 1980.

Other contingencies we must prepare for in selling City bonds--1) general market conditions, 2) general municipal market including impact of other troubled cities, 3) development of New York City market in light of Wharton forecast that the impact of a recession will be worse in New York City than in either the region or the nation, 4) the spread between MAC bonds and City bonds.

Steps Congress can take to help NYC sell its securities publicly: 1) amend the Bankruptcy Reform Act of 1978 to protect the rights of holders of municipal general obligation's, 2) in establishing the Energy Security Corporation, allow eligible projects from public entities, 3) develop Urban Bank bill that provides loan guarantees/direct loans to businesses in economically depressed areas.

We are also exploring steps we can take on our own to improve City's fiscal position: 1) create a truly funded Contingency Reserve Fund, 2) City to issue water and sewer revenue bonds, 3) possibly expanding the City's existing General Debt Service Fund to include an entire year's debt service requirement.
31 January 1980
SUMMARY POINTS
Page Five

CAROL BELLAMY

On balance I think our prospects for full market reentry by 1982 are good.

We have taken many steps, some of you on the Committee said we wouldn't so I'm confused why Senator Proxmire is taking us to task once again for seeking to balance our budget "on the back of the Federal Government".

Although we see some promising signs of growth in the City's revenue base, we see gains eroded by increasing costs for social services, housing, health and energy.

We have wittled our budget down to the core (32% reduction in personnel).

We can't say record for our partners has been good as our own. (i.e. State and Federal governments) It is time the Federal government recognized its obligations to us in the City's Four Year Plan -- in areas of unrestricted aid, reimbursements for Welfare, Health, Transportation, energy, and in funding Federal mandates we must have full assistance from intergovernmental sources.

Other cities are facing the same problems.

COMER COPPIE

Pleased to endorse Mayor's strategy in moving to GAAP balance one year early.

Past PEG programs have relied heavily on OTPS reductions and unspecified actions. New PEG outlines specific expenditure reductions for 1981 and 1982 and presents a sense of priorities.

Nevertheless, the City still faces major problems. Can PEG be implemented? FCB will extensively analyze the Plan.

Critical outstanding issues include: 1) State and national economy -- while the City appears to be regaining health, the recession may be deeper than projected in City budget; 2) Cost of upcoming labor settlements -- uncertain - vital that labor settlement can be funded within City's Plan; 3) City's methods for monitoring HHC and BE have not proved effective -- accordingly the FCB has taken a series of actions including a requirement that
HHC establish a special reserve fund. We will require the City to plan for HHC deficits ahead of time. HHC has also implemented our recommendations to improve revenue collections. Both HHC and BE have experienced significant cost overruns during the first quarter of 1980. The FCB has insisted the City develop plans for monitoring and controlling these agencies; 4) the new Financial Plan anticipates substantial recurring increases in Federal and State aid which may prove unattainable. We will require the City take further action should such shortfalls occur.

The City's ability to make expenditure reductions is increasingly limited by mandated services.

City's success will also depend on making management improvements and increasing productivity. The restructured productivity council should help.

A number of observers have recently questioned whether market reentry in FY 1981 is realistic. Certainly GAAP balance in 1981 will help.

We are continuing to monitor the capital program. We are insisting the City detail the steps necessary to attain its goals for the capital program.

SIDNEY SCHWARTZ

I would like to praise the Mayor for submitting a Financial Plan that goes to GAAP balance by 1981. It deserves recognition for three reasons: 1) It provides a more orderly process of retrenchment than if major expenditure reductions were left until 1982. I believe however, the City should estimate the impact of expenditure reductions on services as well as the economic effect of the program to increase revenues. 2) it demonstrates the City's commitment to meeting its budgetary obligations. If accomplished, it allows the City to test market reentry when financing alternatives are available, rather than later on (after 1982). 3) by eliminating the need to borrow in fiscal 1981 for capitalized operating expenses, the City has reduced the need for new debt issuances.
Two financing situations that may result in 1982: 1) If the City gains full market reentry then I recommend that in 1982 the City attempt to finance some of its 1983 capital requirements, and 2) the second less desirable situation results if the City does not regain full market access. There would still be time, in this instance, to develop financing alternatives.

In spite of these positive developments, serious fiscal problems remain.

- the Plan relies on significant tax increases which require legislative action

- the Plan depends on the following uncertainties:
  a) the realization of increased amounts of Federal and State aid
  b) the impact of inflation and recession
  c) the size of the projected deficits in the covered organizations
  d) the City's continued failure to resolve managerial shortcomings
  e) the size of future labor settlements

No City standby program if it fails to get increased Federal and State aid.

Substantial deficits loom in covered organizations, particularly in the HHC where revenue collection performance remains poor.

City has not reformed management problems in capital program nor have they established procedures for review and implementation of outside recommendations.

Upcoming labor settlements constitute the largest uncertainty.

Long-term problem exists in that the City projects gaps of $250 million in 1983 and $300 million in 1984. Also increases in labor costs after 1982 are not included in the Plan.
While expenditures are responding to inflation, the real estate tax and State and Federal aid are not showing comparable growth.

Federal and State aid for budget balancing purposes has declined over the last two years.

Mandated programs adding to burden—must be fully funded.

STEPHEN BERGER

Having urged continually that the City balance its budgets through the use of recurring revenues and savings, balance its budget according to GAAP, institute management reform and improve its control of the capital program, I endorse the Mayor's new strategy in the new Financial Plan.

Major uncertainties remain, however:

1) the cost of labor settlements
2) HHC projects rising deficits in the City's Plan and performance hasn't improved. The Mayor's hospital closing plan must be implemented.
3) The Board of Education, under increasing Federal mandates projects larger expenditure increases not offset by intergovernmental aid. It will also be difficult for the BE to effectuate the large cuts called for in the Mayor's Plan.
4) Increased Federal and State aid to balance the budget will be difficult to get. Even where increases are apparent, additional aid tends to be on the categorical side not of the budget balancing type.
5) Legislative action on proposed tax increases is uncertain.
6) The City's Plan may be negatively affected by national economy.
7) The City has failed to develop a capacity to plan and execute a viable capital program.
Senator Proxmire, Members of the Senate Banking Committee:

Today I appear before you to make my second report on the City's progress toward financial stability and independence. In making my first report to you a year ago, I thanked you and the Congress for passage of the New York City Loan Guarantee Act, and I will now thank you again. The guarantees have made it possible for us to obtain the financing we need as the City moves toward a truly balanced budget. I believe the City can and should accelerate its budgetary objectives by a full year: my goal is a City budget balanced in accordance with generally accepted accounting principles, starting next July 1 -- less than six months from today. I have presented a revised financial plan that will achieve this. There is no more important step the City can take to ensure that at the end of the four year plan, on July 1, 1982, the City will be able to stand on its own. Before I bring you up to date on the City's financing program, let me describe the new budget plan.

**BALANCING THE BUDGET**

The financial plan presented to Secretary Blumenthal and the Congress in January 1978, which was the basis for the Loan Guarantee Act, called for the City to balance its budget by fiscal 1982. The financial plan presented on January 16 establishes a program for the City to balance its budget under generally accepted accounting principles in fiscal 1981, a year ahead of
schedule. The purposes of achieving a fully balanced budget a year in advance are clear: First, the City will address its fiscal condition realistically by taking early action to close the enormous deficit projected for 1982. Second, the City's reentry to the public credit markets will be accelerated. Finally, with market access and a balanced budget the City will become financially self sufficient, enabling it to deal more effectively with the problems of government and stabilize the delivery of services.

This plan continues the trend of financial accomplishments by the City over the past few years. The budget deficit has been reduced by about $1.5 billion since fiscal 1976, from $1.9 billion that year to $422 million in the 1979 audited statements. The remaining deficit will be totally eliminated next year, and the City workforce will have been reduced by over 25 percent, from 254,000 at the start of fiscal 1976 to 188,000 at the end of fiscal 1981.

It is important to understand the basic sources of the persistent imbalance between the City's projected expenditures and revenues. On the expenditure side, mandated programs and inflation have increased the City's costs enormously. For example, the cost to the City of Medicaid, public assistance and special education -- all mandated by State and Federal law -- was over $1.1 billion in fiscal 1979; by fiscal 1982 these costs will have increased by about one-third, to $1.5 billion. Energy costs will have more than doubled during this period, reaching $450 million in fiscal 1982.

As has been true in the City for the past two decades, such mandated costs have absorbed an increasing portion of the City's locally raised funds. The result has been a continuing reduction in the portion of City funds available for personnel who perform services -- policemen, firemen, sanitationmen, schoolteachers and the like.
The growth of City revenues has been insufficient to fund such costs, requiring continuing cuts in City agencies. Net revenues from the real estate tax, the City's major tax source, have not increased significantly since 1976; the yield from this tax has declined from 51 percent of locally raised taxes in 1976 to 47 percent in 1980. The City's other taxes, principally the personal income tax and sales tax, can be expected to grow at roughly the same rate as inflation, but these taxes amount to less than half the City expenditures that are driven upward with inflation. State and Federal revenue sharing programs, a major source of City funds, have not grown significantly and are projected to remain about constant.

Having outlined the fundamental reasons for our persistent budget gaps, I will now turn to the gaps we face in fiscal 1981 and 1982: $677 million in 1981, rising to $1.14 billion in 1982. These gaps reflect the cost of a new labor settlement comparable to the settlement negotiated in 1978, although negotiations have not begun with the municipal labor unions and no such offer has been made. The gap for 1981 also reflects the one-time $278 million cost of balancing the budget under generally accepted accounting principles: $150 million to eliminate capitalized expenses, and $128 million to fund City pension liabilities on the accrual basis.

To close these gaps, I have proposed City actions amounting to $507 million in fiscal 1981 and $729 million in fiscal 1982. The plan has two essential components -- a major expenditure reduction program and limited, though not insubstantial, tax increases.

I propose to cut back expenditures in 1981 by $299 million and in 1982 by $461 million. The 1981 cut will be twice 1980's, and, taken together, these reductions will be more difficult than any taken since 1975. Every agency will
be cut. But we have attempted to target reductions to reflect basic City goals, and we have tried to make cuts in a way that reduces service delivery as little as possible. To make clear our commitment to service delivery we have imposed, where possible, a 10 percent cut in administrative costs, even for the highest priority agencies. And we have imposed dramatic reductions in the Cultural Affairs, Consumer Affairs, and Buildings Departments -- all important agencies but with lower priority than some others. The Department of Ports and Terminals will be eliminated -- along with many other actions.

To illustrate my earlier point about the effect of mandated costs: of the massive cuts required for 1981 and 1982, more than half will take the form of personnel reductions, which will total over 7,800; of these reductions, more than two-thirds will be in police, fire, sanitation and -- most of all -- education.

In addition to these expenditure reductions, the plan would raise certain local taxes and user charges, which will yield an additional $175 million annually in revenues for fiscal years 1981 and 1982. In reviewing the tax options, I rejected increases in the City's personal income tax and corporate earnings tax because of their likely impact on the local economy; I believe the City was right in 1977 to have lowered taxes. Instead, I am seeking actions that are equitable, bring tax receipts in line with inflation, and establish user charges at appropriate levels. For example, I propose to increase the real estate tax by 10 cents per $100 of assessed value; to increase water and sewer charges by about 15 percent; and to increase excise taxes on beer and liquor. These kinds of revenue measures are not expected to have any significant negative effect on the City's economy.
Even with all the cuts and taxes I have proposed, the City will still need the additional aid from Washington and Albany now in the Financial Plan. The State and Federal governments must continue to be partners in solving New York's budgetary problems.

We are expecting increases in State and Federal aid, but such increases are less than half of the $1.2 billion the City itself is undertaking in expenditure reductions and tax increases during fiscal 1981 and 1982. The plan assumes $170 million in additional Federal and State aid in fiscal 1981 and $410 million in fiscal 1982, for a combined total of $580 million over the two fiscal years. This is less than the amount originally included in the 1978 plan.

With respect to State aid, the Governor has pledged -- publicly and privately -- that the additional aid we require will be forthcoming. With respect to Federal aid, while we have made some progress in obtaining additional aid through administrative actions, the major initiatives will have to be approved by Congress as part of the Federal budget. I think the record demonstrates that we have been able to obtain the additional State and Federal aid we need to meet our budgetary objectives.

The January 15 plan is by no means easy to implement. The tax increases and expenditure reductions proposed will be the subject of continuing analysis and controversy. But I believe that the job of balancing the budget must and will be undertaken in 1981. Putting an end to the City's years of fiscal dependency will carry rewards fully commensurate with the struggle we now face.

FINANCING

Status of Financing Plan: As you know, the $4.5 billion four-year financing package we developed in late 1978 is one of the largest, most complex financings ever arranged. Less than 20 percent of this financing -- or $750 million -- is
scheduled to be implemented with Federal guarantees. The remaining $3.75 billion -- over 80 percent -- is to be provided by issuing unguaranteed bonds of the City or the Municipal Assistance Corporation (MAC). This means that the City plans to use less than half of the $1.65 billion of Federal guarantees now authorized. In line with my wishes, as well as yours, the bulk of the City's financing is being provided through local efforts. Local financial institutions, as well as State and City employee pension funds, are participating in this financing plan, and New York State is playing a major role through MAC debt issuances.

I am pleased to report that the financing plan is on schedule. To date, $1.79 billion of MAC bonds have been sold, of which $938 million were issued to financial institutions and City employee pension funds under a four-year bond purchase agreement made in November 1978; the other $847 million on MAC bonds were sold to the public in six separate issues, the most recent of which has just closed. In addition to the $1.79 billion of MAC bonds, $650 million of Federally guaranteed City bonds have been issued to City and State employee pension funds. Another $100 million of guaranteed bonds is scheduled to be issued on February 21. This will be the final planned sale of guaranteed bonds under the four-year plan.

Public Note Sales; Seasonal Financing: During fiscal 1979, the City was able to sell short-term notes to the public for the first time since March 1975. The first public note sale was in January 1979, for $125 million; it was followed by another public issue the next month, for $150 million. All these notes were paid on time. These public sales were accomplished one year ahead of the schedule set by the Guarantee Act. The remainder of our $650 million of seasonal financing needs was met by a credit facility with local banks and City employee pension funds.
In connection with the City's short-term borrowings, you should be aware that our seasonal borrowings have decreased by about 70 percent, from $2.1 billion in fiscal 1977 to $650 million in fiscal 1979. During the current fiscal year, we project that seasonal borrowing needs will drop to $650 million. To date, the City has met these fiscal 1980 needs with two public note sales for a total of $375 million -- already an improvement of $100 million over the fiscal 1979 total of publicly issued notes. As a back-up to public note sales in fiscal 1980, we arranged another credit facility with private lenders. The lending group in the facility was expanded to include forty local, foreign and out-of-state banks, eliminating the need for participation by the City's pension funds in meeting this year's seasonal borrowing needs. I consider these developments as important steps toward securing sustained access to the public credit market.

Capital Spending: As I reported to you last year, capital spending for the initial year of the four year plan was below the level we originally anticipated. Because of the urgent need to restore the City's capital plant to sound condition, I instituted a series of measures to ensure that we spent promptly and prudently the capital funds available to us. While I cannot be entirely satisfied with the progress of our capital program, I am greatly encouraged to see that we have been begun to meet our spending targets in programs that are consistent with our priorities.

Before we presented the City's new budget program on January 16, we reviewed the City's entire four-year capital program. Part of meeting our spending targets, as we have begun to do, is to set those targets at appropriate levels.
I believe we have done so. The systems for planning and reporting capital expenses are being almost completely overhauled. This major effort is the final phase of the process that made our expense budget auditable by independent accountants. As the capital budget is brought fully on line with the new system, our ability to analyze and forecast capital expenses is steadily improving.

The results of our recent analysis showed that, while interim spending forecasts require significant corrections, the overall $2.3 billion estimate of capital spending during the four year plan remains our best estimate. We will continue to monitor spending results and regularly reevaluate our projections. As we move closer to the half-way mark of the four year plan, our projections can become progressively more firm because of increased information and experience with the capital program. The monthly financial plan statements to the Treasury Department, as well as our quarterly financial plan modifications, will continue to keep the Federal Government and the public fully informed of any changes in our projections.

Market Access -- Outlook: When the four year plan expires in mid-1982, the City will have to obtain capital funds without any Federal presence in our financing. Whether we can then stand on our own -- without Federal guarantees -- will be the real measure of our success. I have underscored my commitment to this goal with my decision to balance the City's fiscal 1981 budget in accordance with generally accepted accounting principles, a year ahead of the schedule set forth in the Guarantee Act. This program should significantly improve our prospects for access to the long-term credit market; it is a clear signal to potential investors, as well as the rating agencies, that the City has both the will and the ability to finish putting its financial house in order.
Any discussion of market access must acknowledge the importance of improving the City's bond rating. An investment grade rating appears to be essential for the City to achieve true market access. No municipal issuer has been able to sell bonds in significant amounts, on a regular basis, without the minimum investment grade from one of the rating agencies. In the case of short-term notes, the City was able to succeed after a one-grade advancement by Moody's, from MIG-4 to MIG-3. In the case of bonds, no comparable advance has been made. The City's bond rating was suspended by Standard and Poors in 1975 and has not been restored; Moody's continues to give our bonds a B rating. For City bonds to be of investment grade, the Moody's rating would have to advance two steps, to Baa, and Standard and Poors would have to rate the bonds as BBB.

A truly balanced City budget, one year ahead of schedule, should accelerate the process. If we stick to our program to balance the City's budget -- under the most stringent financial auditing and reporting standards applied to any municipality in this country -- the City's bonds will deserve an investment grade rating. As you know, the Guarantee Act and the financial plan require that the City attempt to sell bonds during the coming fiscal year, unless any such attempt would be against our financial interests. I am firmly committed to achieving a public sale of City bonds at the earliest possible date. It will clearly be a step of enormous significance in the City's continuing effort to regain full market access. Therefore, it is vital that the City's first bond sale be a success -- that it be favorably received by the marketplace as the beginning of a renewed City presence in the municipal bond market. An unsuccessful attempt, like the aborted City note offering in 1977, will only serve to set back the City's long-term goal of full market access. Having
Having made this point, I will now say that I believe a successful bond sale should be possible in fiscal 1981, and I stand ready to move ahead with it as soon as the City's financial advisor and underwriters advise me that the time is right.

If the City begins to sell bonds in fiscal 1981, as I believe will be the case, we will have begun to set the stage for the period after the end of the guarantee program. The prospects for market access in fiscal 1982 are even better because we should by then have an audit confirming that the City balanced the budget a year in advance. Nonetheless, prudence requires us to deal with the possibility that the City will not have full market access before the expiration of the four year plan. We are beginning to assemble the elements of a financing program for the period after fiscal 1982, in order to ensure that the City will be able to obtain long term capital without resort to Federal guarantees. Last November, I outlined three general areas for consideration:

- the creation of authorities that would issue special purpose revenue bonds, such as water and sewer bonds, which would be backed by user charges.
- authorization of additional MAC bond issues.
- reduction of the City's capital program.
A combination of measures such as these can be taken and will be taken to ensure that, even if the City's market reentry is incomplete, we can nevertheless function without Federal guarantees after the four year plan expires. The City, MAC and other local parties will work together, as we have in the past, to put such a program in place well before the June 30, 1982 deadline. This program will not assume or require any Federal presence in City financing.

THE ECONOMY

Since we are counting on local revenues to fund a large portion of our budget, the state of the City's economy is critical to the success of the four year plan. During the second year of my administration, the City's economy continued to show progress, due to the City's improved business climate, as well as the long upswing the nation's economy. We are forecasting that the nation will experience a recession in 1980, and the January 16 plan takes into account the impact a national recession could have on our local tax revenues.

However, a recession now should not have the disastrous impact of the last recession five years ago. At that time the City was on a declining path. Even in 1973, a relatively prosperous year for the national economy, the City lost 160,000 jobs. The situation is different now. During the year after my election in November 1977, jobs in the City increased by 53,000, reversing a seven-year decline. In the following year, between November 1978 and 1979, an additional 13,300 jobs were added, mostly in the private sector. The bulk of these new jobs are in business services, and the finance, insurance and real estate businesses. These industries are not as sensitive to downturns in the economy as manufacturing, which now makes up a smaller proportion of the jobs in the City.
Retail sales have shown surprising growth. Sales advanced about 12 percent above 1978. This is far above the City inflation rate, implying that the City's real growth for 1979 was greater than that shown for the nation. Among the reasons for the extremely good showing in sales are the Sunday openings of stores, the attractiveness of prices expressed in dollars for foreign tourists, and the additional expense of using automobile transportation to trade outside the City. These factors, which increase the attractiveness of urban area shopping, will continue into the future.

Another strong sector has been construction. Additional residential housing is in the works. A recent survey has shown that 6,800 new apartments will go on the market by the end of 1980. American Telephone and Telegraph, Continental Insurance, IBM, and Phillip Morris are constructing new headquarters buildings in the City. The strong flow of foreign investment has led to increased demand for space as a result of their corporate presence here. Other projects in the works include a new office tower on Wall Street for the American International Group, and the new American Exchange at Battery Park. The Convention Center will help revive the far west side at midtown. Since the financing is already arranged, the work will go forward even if there is a recession.

The City's tourist industry had a particularly good year, with hotel occupancy rising to over 90 percent, the highest level since the 1964-65 World's Fair.

The relative improvement in the local rate of inflation has been an important ingredient in our economic recovery. The City's inflation rate has been below the nation's since 1974, with the cumulative increase since 1967 below the national average. In 1979, our average inflation rate was 8.9
percent, compared with the national increase of 11.4 percent. This has put us
in a better position to compete with the rest of the nation for new business and
new jobs. The rise in available jobs has caused the City's unemployment rate to
drop to 7.2 percent as of last December, our lowest unemployment rate since the
beginning of 1975.

Of course, in view of the national recession expected in 1980, we have
projected downturns in all of these areas. And even now, our unemployment rate
is higher than the national average of 5.9 percent. While the City is now in a
much better position to withstand a recession, without the enormous damage we
experienced in 1974-75, the adverse effects on our economy and budget cannot be
ignored.

On balance, I think we have good reason to believe that the long term outlook
for the City is encouraging. We are dealing with the fiscal problems that for
so long have clouded the City's credit. Of course, many of the actions required
are controversial and difficult. But despite the controversy, despite the
difficulty, one fact should be apparent: the program we brought to you in 1978
is succeeding. Since our achievements would not have been possible without
Federal loan guarantees, you have every right to be satisfied with the role
played by this Committee in bringing them about.

Again, I thank you.
SUMMARY

Statements Before Senate Committee
on Banking, Housing and Urban Development
January 28, 1980

Bigel

* contrasting state of affairs in 1975 vs. current: issuance of less than $600 M in short-term debt, surpluses in 1978 & 1979 with GAAP-balanced budget in 1981, City has one of leading municipal accounting and budgeting systems in the U.S.

* bankruptcy threat is gone; no more need to fund daily operations with long-term proceeds; should the City fail access to fund capital in 1983, daily functions will not suffer.

* NYC's current problems are in transit, health care and education, which are not unique but size of City magnifies them; Fed has failed to provide funds or comprehensive solutions.

* GAAP-deficit reduction progress since 1975; expenses kept behind inflation rate (better than other larger cities); from 7/1/75 6/30/80 City workforce will have declined by 23% while other cities show increases.

* substantial progress made by NYC in terms of financing: obtained seasonal financing from credit markets, reduced seasonal needs, eliminated $800 M State advance, ended 1978 and 1979 with high working capital, reduced interest expenses, improved beginning cash balances with decreased dependences on pre-paid revenues, elimination of outstanding short-term debt at 7/1/75.

* Federal aid from '76-'80 has not kept pace with inflation; Federal policies are negative-excessive public and medical assistance burden on the City and special ed costs for City increase at higher rate (almost twice) than Federal aid, all are mandated programs; federal discrimination in transit also against urban areas, but especially NYC; NYCTA only gets small percentage of aid in proportion to ridership.
SUMMARY
January 28, 1980
Page Two

* Bankruptcy threat triggered investments by retirement systems; participation of pension funds significantly strengthened those systems; fire department pension fund dispute should be solved; retirement systems do not intend to purchase any further City-related paper past 1982.

* Market access is hampered by the rating agencies, oversight agencies and the size of the financing.
  
  **Rating agencies:** inaccurate reports; fail to consider progress of NYC; unresponsive to public needs; City has acted on major recommendations based on issues identified by rating agencies but it was ignored; their standards are inconsistent and constantly raised.

  **Oversight agencies:** given the weight of their prognostications, their accuracy must be judged; their judgment has not been better than the City's but it is given more weight.

  **Size of financing:** massive capital needs, as much as $4 billion per year per Comptroller's report, but that's overestimated and so is City's $2.3 billion; City should revise capital plan based on spending.

* City workforce has had gross increase in spendable wages but real decline annually; fiscal crisis period was time of sacrifice for workforce (a detailed listing of wage and fringe benefit deferrals and cuts is shown); though settlements elsewhere were higher, NYC had fewer "labor actions".

**NOTE:** MAC's response to program Planners report in December refuted a number of the points which have been repeated here . . . . Program Planners fails to recognize contribution of State aid, as well as the actual methodology by which NYC reduced its budget gaps largely by way of Federal/State revenues, debt service reductions primarily reached through MAC restructuring, and tax rate increases with significantly less involvement of City expenditure reductions.
Grossman, STANDARD & POOR'S

* what Harries said two years ago holds true (City will be unable to borrow meaningfully unless it can demonstrate fiscal stability through balanced budgets with an outside monitoring system), but one year isn't enough.

* free access is still elusive; note sale is no test of credit because of State revenue basis; a small ($50-70 M) 15-year bond sale could have reached the market at a reasonable cost last August-September but this isn't possible now at a reasonable rate (15-year yield for NYC would have to be well in excess of the current scale, but not far off from Chicago-10% range).

* NYC is slowly and painfully meeting expenditures with more reliable revenues, but huge governmental sector makes retrenchment difficult.

* real progress is evidenced by 1/15/80 plan to move to GAAP in 1981 especially in light of gap reductions since 1976; short-term needs were reduced, but monitoring is needed and should be continued.

* January plan reflects deficit elimination largely by City actions (like Board of Ed, which is difficult); difficult situations loom (labor); inflation compounds the gap; Federal/State aid is still a major part of plan; Federal/State and City should move to synchronized cash flow calendars so all could reduce anticipatory borrowings; water and sewers should be moved to a self-supporting systems on an enterprise basis in light of large needs in that area; with MAC providing back-up financing and City's economy showing some signs of life, City could make a serious attempt to test the market by late 1982.
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Ackerman, MOODY'S

* for credit analysts, evaluation of trend data is key to formulating credit assessments; NYC's financial and economic distress has parallels in other cities; NYC, however, has not been able to demonstrate an ability to manage its broad scope of operations within its limited resources.

* the end of FY 1982 will be the first real benchmark when City must GAAP balance its budget by law, when safeguards of the past will no longer be available, when MAC's debt limit is approached and loan guarantees expire along with pension fund and banks commitments, and oversight will not be over the wage settlements.

* the continued use of stop-gap measures and one-shot revenues is not acceptable; control has not been demonstrated over Board of Ed, Transit Authority and Health and Hospitals Corporation; outstanding litigation threatens, costly solutions may result effecting the very composition of the income base; capital needs are enormous with no plan to address them.

* relationship of MAC to the City needs clarification, MAC's scope and longevity raises questions; indefinite perpetuation of MAC's powers and debt-incurring ability could have a deleterious effect on NYC; the segregation of capital financing from the major governmental unit is not sound and could have serious ramifications.

* proposed amendments to Federal Bankruptcy Law hampers City's efforts to regain market access; NYS's willingness to give blanket consent to all its municipalities to file petitions under Chapter IX is disturbing.

* NYC has disregarded the sound precepts of public administrations and violated elementary principals of maintaining solvency; both the magnitude of problems yet to be addressed and the past history of poor performance must be considered in any calculation of future credibility; the City permitted a default in 1975 and the psychological impact of a default defies quantification but will be a long time in overcoming; regardless, a favorable opinion by a rating agency does not necessarily guarantee investor confidence.

* the City has made progress toward fiscal goals as recognized by improvement in bond ratings from Caa to B and the assignment of ratings to note issues; a definable positive trend has yet to be established, but in general, 3 years of sound balanced budgets would be called a trend.
Moody's expects the end of FY 1981 or 1982 to mark the beginning of such a trend which, due to NYC's past shortcomings as an issuer, would require much longer than the general rules would indicate reflecting the fact that near term plans don't reflect structural defects and long-term remedial measures.
Rousseau

* successful sale of BANs due to perception of NYS backing - transfer of State aid to NYC from the State Comptroller directly to paying agent.

* the City has established itself in the lower range of acceptable credits in the market place and is subject to all the perils of lesser regarded credits.

* presently it is more a function of the severe stress in the bond market than of NYC's relative standing in that market that makes further NYC note sales uncertain.

* market acceptance is as much a matter of psychology as it is of budgets and balance sheets.

* the investing public will require four things:

1. a debt service fund mechanism (investors should be exposed to the Debt Service Fund created by the State Legislature in late 1978).

2. a record of achievement in budget balancing (confidence is elusive even in light of NYC's accomplishments; very high standards are set; early move to GAAP should contribute a great deal; creation of 4-year plan a positive innovation but calls attention to the large budget gaps in the out-years, although most other State/ municipal budget projections would have them, too; we must more clearly define gap as opposed to deficit for success).

3. a capital facilities plan (realistic and believable capital plans to maintain and upgrade the capital stock are a must; slim prospects of City raising $1 billion in a single year ('82) in the tax-exempt market, it would be a feat - NYC should have a detailed contingency plan; some projects should be funded on pay-as-you-go basis).

* a water and sewer entity charged with the operation of those services is recommended, similar to ECP and HDC - and why not hospital, equipment leasing - and retain MAC as an issuer for certain defined capital purposes. Disadvantages to this might be loss of operating flexibility if new revenue streams were restricted by bond covenants; legal structure involved may diffuse political power of Mayor and City Council; potential negative reaction of investors if too many revenues are diverted from General Fund or if it's too confusing.
(4) improved bond ratings (City needs at least minimum grade rating to market several hundred million per year under normal conditions; needs an A/A rating to do so in uncertain markets. City shouldn't rush to market; to insure lasting success, care and caution is required; fewer bonds than market could absorb, generous pricing of early issues).
Beason

* NYC has shown substantial achievements: more stringent accounting and budgeting procedures, reducing annual deficits, achieving a degree of public market acceptance.

* move to GAAP—balance early is crucial since pension funds and financial institutions are nearing saturation point for MAC and unguaranteed City bonds. (practical limitations and legal roadblocks).

* MAC cannot be depended on for long-term financing since it has a debt-ceiling, restrictive covenants, and additional issuances would increase contingent NYS debt; investors have viewed MAC as interim measure for NYC, otherwise perceptions of any lack of effort on City's part would negatively effect market acceptance of MAC debt.

* investment grade rating is key; continuing efforts by City are high priority, strong commitments must be made in the face of labor, budget review, audits and elections; recommend showing raters first-hand how City copes with critical matters to prove its ability to produce predictable financial results.

* NYC is stronger now than in 1975, and meaningful actions have been taken; further improvement is still required, but market re-entry is in sight.
Gotbaum

* workers suffer greatly in time of fiscal austerity; sacrifices imposed on them from all levels of government; small wage increases well below inflation and CPI; there is no optimismism regarding future CPI and inflationary trends.

* family income of City workers does not compare favorably to Bureau of Labor Statistics low and intermediate family budget; women with dependent children are especially hard hit.

* workers have suffered from take-backs and lay-offs since FY 1975: changes in work rules, reduction of overtime and summer hours, deferral of wage increases, reduction of ITHP benefits, deferral or reduction of fringe benefits and COLA payments, 30,000 lay-offs, strict attrition policy and non-replacement have caused ever-increasing workloads.

* ever-increasing workloads must be accomplished with old, poorly-repaired equipment, in facilities that are dangerous and deteriorated, creating counter-productive conditions with little City effort to improve them; NYC workers' accident rate is almost 4 times greater than that of all U.S. private business; it's bad workplaces not bad workers that impair productivity.

* union has cooperated with City on broadbanding civil service titles; they have supported flexibility in internal transfer of personnel; pressed Mayor to institute City-wide productivity council; in general, City and labor have long-standing tradition of cooperation.

* Federal government has not taken lead on productivity; National Productivity Council has made no suggestions; many U.S. cities are going down the tubes, NYC is not unique - it just got there first; stressed need for American Urban Policy; NYC's burden of Medicaid and welfare translates into high unemployment, abandoned property, burdened school systems, postponed capital improvements and repairs.

* while we appreciate loan guarantees, they cost the Feds nothing but they cost NYC a great deal; treatment of NYC as unique has only served to put off dealing with the fundamental inequalities of today's cities.
Altman

* since 1975, NYC has achieved each of its major fiscal goals; financial accomplishments such as reduction of GAAP-deficit, elimination of deficit entirely during FY 1981, independent audits, reduced borrowing needs and successful sale of notes in 1979 and 1980 deserve recognition.

* the remaining guarantee authority of $900 M will only be used if the City and MAC can't finance long-term needs over the next two years; U.S. has received prompt quarterly payments on the guarantee fee for bonds issued thus far.

* regarding compliance with the guarantee act, the City's continued fiscal reform enhances the security of guaranteed debt thereby meeting the "reasonable prospect of payment"; the financing commitments of financial institutions, pension funds and MAC have been honored; the independent fiscal monitor (FCB) continues; and two years of independent audits were accomplished.

* NYC's budget has shown improvement; 1979 results represent a year of true progress; 1980 budget balanced according to State Law; City has been able to cover problems in Board and Ed and Health and Hospitals Corporation which developed during this year through stronger than expected economy and further expenditure reductions.

* currently proposed City plan of 1/15/80 has not been evaluated although certain monitors place "worse-case" gaps at far greater than plan; NYC has historically ended with smaller than projected budget gaps so this trend may continue.

* even though the FY 1981 budget gap has expanded over projections of such gap last June, several factors can be cited: earlier achievement of GAAP-balanced budget, Federal and State laws already required City to adjust pension costs by $50 M and capitalized operating expense phase-out of $132 M for FY 1981, the inclusion of a provision for wage settlement, increased medicaid, special ed and energy costs, all offset somewhat by increased revenue projections for 1980 and 1981.

* NYC's deficit reduction program (PEG) is ambitious; some actions will be difficult as they require legislation and will be unpopular; overall job reductions appear possible (except maybe Board of Ed) and OTSP cuts appear attainable.
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* PEG uncertainties include ability of Board of Ed to sustain reduction in light of need to maintain services and evaluation of success of new control procedures; present projections of HHC revenues are uncertain and City may be pressed for greater funding; expenditures for energy have rapidly escalated so conservation may not offset costs; and it is too early to judge if increased Federal/State aid is realistic.

* FY 1982 will be a more difficult year for NYC; the FY 1982 deficit may not be realistic since it depends on eliminating gap in 1981, negotiation of restrained labor contracts, the City’s ability to make necessary cuts and the uncertainty of prospects for increased Federal/State aid; because of carry-over value of FY 1981 PEG actions, it is disconcerting that alternative programs do not exist.

* recent State budget proposals threaten increased State aid although State commitment is not diminished; preliminary indications of Federal aid to NYC are that it will continue to increase although some increases require legislation; Federal aid is at least less limited than prospects for increased State aid.

* other areas of concern in City's road to fiscal self-sufficiency include uncertainty in the national and local economy, wage settlements, capital spending (past 2 years' slippage in light of recent signs of progress in coordinating and accounting throughout the capital budget system, and restoring access to the bond market through better bond ratings (the City has prepared a strategy for market re-entry with the cornerstone being the achievement of budget stability, management objectives and achieving an investment grade rating). Current limited market for City bonds is insufficient, and it probably couldn't be tapped until FY 1981 anyway.

* if City can't meet its financing needs in FYs 1981 and 1982, MAC has sufficient bonding authority so as to preclude the need for stand-by guarantees.

* the next 12 months will be pivotal for the City's self-financing quest: conclusion and outcome of labor negotiations, whether the City can actually produce a GAAP-balanced budget for 1981, whether a successful sale of a limited amount of City bonds can be accomplished to demonstrate investor confidence; these factors should all facilitate the attainability of an investment grade rating.
I offer some preliminary thoughts on the Mayor's Program to Eliminate the Gap and the new financial plan for fiscal years 1980-1984. I do so by way of initiating discussions that will go on for six months, and I stress the necessarily tentative nature of my comments.

Philosophically, I stand in accord with the decision to balance the budget in accordance with GAAP in fiscal year 1981. This is the clearest signal the Koch administration has given of its determination to meet the City's fiscal crisis head on. And our partners in this unhappy endeavor -- the investment community, organized labor, and lawmakers in Washington and Albany -- should take heed.

Still, I find myself questioning many of the specifics of this plan. It projects a gap of $677 million in fiscal year 1981. Of the total actions proposed to close that gap, nearly half (44 percent) are reductions in expenditures, and most of the remaining are equally distributed between tax increases (26 percent) and increased State and Federal aid (25 percent). I differ with some of the assumptions on which these figures rest, and some of the priorities by which they are set.

**SIZE OF THE GAP**

On the question of the very size of the gap itself, the Mayor offers this new plan as a blueprint for solvency and "financial independence;" I fear we celebrate the "fiscal Fourth of July" too early.
The plan puts the fiscal year 1981 gap at $677 million, ($213 more than previously projected, with most of the increase a result of the GAAP adjustments, $150 million in elimination of expense items from the capital budget, and $128 million in accelerated pension payments.) Added to these GAAP adjustments are an additional $254 million in increased expenditures, including labor costs funded at a 4 percent increase, energy costs, additional needs of the Board of Education and increased mandated expenditures in social services. Offsetting these increases are projected revenue increases: $86 million in taxes, $155 million from ECF and the sale of right-of-way for Westway, and $14 million in other revenues.

On the revenue side, the $100 million from Westway is questionable, to say the least. For three years we have anticipated payment for Westway, and for three years it has failed to materialize. There is no better reason this year than last to treat Westway as an anticipated revenue. Overly optimistic forecasts of intergovernmental aid may also present a problem (see a later section of this document for more detail). So too, because no supporting data accompanies the Mayor's tax package, it is too early to assess the accuracy of the revenue projections that accompany it, or what alternatives might suggest themselves should the tax package or any part of it run into trouble in the City Council or State Legislature (also see a later section of this document for explication).
The gap may also expand because of continuing revenue problems in the Health and Hospitals Corporation. The State Deputy Comptroller, in a study of the City's most recent financial plan, concludes that we could be forced to increase our operating subsidy to HHC by as much as $238 million in FY'81. While an increase of that magnitude may be unlikely, the volatility of HHC revenue collections raises the prospect of some increase in HHC's operating subsidy. None is projected in this plan. In addition, the $16 million in savings projected as a result of management affiliation contracts at Queens and North Central Bronx Hospitals are entirely speculative. Studies of the cost-effectiveness of these contracts will not even be completed until June of 1980.

On the expenditure side, we must also be prepared for possible increases in such economically sensitive expenditure categories as energy, Medicaid, AFDC and other public assistance programs. The Mayor's plan accommodates a $33 million increase for social services, but when unemployment increases, as is forecast for 1980, medical indigency and welfare caseloads increase proportionately, and here again, the Mayor's projections need to be tested.

On the question of energy, the plan projects an increase of $92 million in energy expenditures in FY'81 and $141 million in FY'82. Unfortunately, these estimates are based on optimistic assumptions about the increases in fuel costs (25 percent annually for fuel, 15 percent annually for electric).
But as I pointed out last month, fuel costs rose almost 50 percent in the past six months alone, and cannot confidently be expected to rise only 25 percent annually over the next two years.

I applaud the Mayor's effort to reduce energy costs by increasing consolidation and sales efforts in the in rem housing program and by launching a citywide investment in conservation. We could go even further, however, to upgrade the energy efficiency of in rem buildings by dedicating capital funds to increased weatherization efforts.

There is also the thorny problem of transit. The absence of any detailed analysis of the Transit Authority budget in the face of its projected deficits of $104 million in FY'81 and $129 million in FY'82 (without consideration of increased labor costs on restoration of deferred maintenance) ignores a critical fiscal situation which may affect both City revenue projections and expenditure levels currently forecast.

The Governor has committed to maintain the fifty-cent bus and subway fare through 1981; this commitment places the burden for increased aid on either State or Federal funds, or a new dedicated transit revenue at the regional or State level. The prospects for either solution are problematic.
And because fare adjustment would have detrimental implications for the City's economy as a whole, programs that lie within our control to reduce the T.A.'s projected deficit must be established now. The City's capital budget should assume all true capital costs now carried in the T.A.'s operating budget, as well as fund a new $35 million subway car overhaul program which will reduce maintenance costs. I will continue to urge that the City take advantage of available capital funds for these purposes. The only actions proposed by the Mayor involve civilianizing the 100 percent City funded T.A. Police Force. The commitment to convert 50 police positions to civilian titles is inadequate; I have previously pointed out that the T.A. police is capable of converting at least 150 positions this year.

Finally, on the subject of labor, little more need be said than we are funding a 4 percent wage package -- a figure arrived at merely on the basis of a single and perhaps unique historical precedent.

In sum, then, our heroic efforts this fiscal year may still leave us short of our goal, a prospect that compels us to look more closely at the Mayor's packages of expenditures, cuts and new revenues.

**EXPENDITURE REDUCTIONS**

I have argued in the past for distributing painful service cuts over time, and I support the Mayor's actions and his courage in taking them. No one can deny that we are asking New Yorkers to make extraordinary sacrifices.
There may, however, be some positive aspects to the reduction program. For example in the Police and Sanitation Departments, large savings can, indeed, be achieved if management is improved. In fact the Mayor now calls for implementation of two recommendations I made last April to reduce NYPD's budget. These reductions involve stepped-up civilianizing, reducing the number of personnel performing management and administrative services and eliminating ranking NYPD staff. We cannot be too sanguine, however, about agency commitment to such management initiatives.

For example, the 1980 PEG program called for the return by January '81 of 366 officers to patrol as a result of civilianization. To date, only 94 officers have been so reassigned. So too, a reduction of 480 uniformed Sanitation personnel was to be offset by a variety of management improvements. But there have been several delays in the implementation of these improvements, and the Mayor's Management report shows no increase in the efficiency of the Department to offset its loss of manpower.

The Mayor's plan also incorporates the major recommendations I recently made to the Parks Department involving increased supervision and redeployment of personnel, as an example of how to maintain services in the face of budget reductions.
There are some positive signs that agency reductions are moving towards program oriented cuts. Specifically, the elimination of duplicative services by reallocating the work of Ports and Terminals and the Community Board Assistance Unit (CBAU) is a move in the right direction. However, many of the recommended City actions remain, as has characterized past actions, percentage reductions of staffing level with no real knowledge of impact. For example, why propose a 10 percent cut in the Criminal Justice Agency appropriation with an expectation it will be offset by increased productivity. Why not, instead, examine the priority of the entire $3.5 million program as contrasted to the need for basic services in sanitation, police, fire and education? So, too, I challenge the Mayor's recommendation to increase tuition in community colleges by another 10%. Coming on the heels of recent substantial tuition hikes, this is another example of a random budget cut without careful assessment of impact. Until we get a budget proposal which has cutbacks based on the cost effectiveness and priority of a service, we will continue to whittle away bits and pieces and end up with half-staffed agencies limping along.

BOARD OF EDUCATION

The most nagging problem in the Mayor's reduction proposals and the necessary focus of our attention is the Board of Education.
This year the Board seriously underrepresented its expenditures and flagrantly overspent its budget. Only a few months ago we funded a $90 million deficit in transportation and special education, and we narrowly avoided cuts to classrooms through the layoffs of a substantial number of teachers. Now, as the City meets obligations of $299 million in Financial Plan Savings, we demand another cut of $111 million in the Board of Education, and again the Board raises the spectre of layoffs.

The Mayor is arguing that while he is calling for $111 million in cuts, he is adding $56 million, on top of the $90 million already provided, for a net gain over the FY '80 baseline of $26 million. What he neglects to explain is that like most of the $90 million already spent, the additional $56 million increase is entirely mandated: 70 percent in special education, the rest in competency requirements and collective bargaining costs. Though the Mayor maintains that the Board is only absorbing a $55 million cut, the bottom line remains: $111 million still must come out of the regular classroom and central administration.

I support proposed reductions in administrative staff. The Board must continue its administrative hiring freeze and must be prepared to take a 10 percent cut in district and high school administration.
Further administrative actions should address allegations of duplication of services at the Board of Education. I have previously suggested that the duties of the Office of Auditor General can better be performed by the City Comptroller's office; that the Board of Examiners can be disbanded and its responsibilities assumed by the State. The Mayor proposes percentage cutbacks in these areas -- the question of whether they should be eliminated altogether must be addressed. Serious consideration should also be given to subsuming the Board's Bureau of Supplies under the City's Department of General Services. The Comptroller has carefully scrutinized OTPS expenditures and purchasing policies at the Board. This action would give the City greater control over what appear to be lax policies.

I endorse the Mayor's proposals to consolidate underutilized schools but question OMB's list of 40 schools to be shut. For example, the list includes PS 125 in Harlem, one of the few elementary schools in the City with an elevator, a high priority given the number of handicapped children the Board is compelled to mainstream. Does this make sense? P.S. 41 in northern Queens, a school surrounded by limited access highways and Little Neck Bay, is also on the list. But closing this facility would necessitate high additional costs for transportation. In sum, the Board's Building Review Committee ought to be consulted as part of a responsible policy on school closings.
Finally, the central issue in rising education costs is that special education is taking an increased share of the budget, and thus compelling cutbacks in resources serving the regular school population. As the Mayor points out, expenditures in the Division of Special Education have increased 55 percent from $220 to $332 million from FY'75 to FY'80, while the entire educational budget increased less than 4 percent.

It is time we devise a strategy to cope with the increased costs of Federal and State mandates. Clearly the Federal and State governments have been remiss in appropriating funds to pay for these mandates. As I have explained on numerous occasions, the Federal government has indicated that instead of 30 percent in Federal aid to the handicapped for FY'81, we will only receive 12 percent. We received slightly over $100 million from the State for FY'80, an increase of 8 percent over last year. But the state aid formula, which reimburses special education expenditures on a prior - rather than a current - year basis, seriously discriminates against school systems actually meeting their mandates and adding large numbers of new handicapped youngsters to their roles. The fact is that the increased costs of 9,450 additional handicapped children in New York City's school system this year were largely absorbed by City tax levy dollars.
What is needed on the Federal level is fulfillment of a legislative and judicial commitment made to our handicapped population. What is needed on the State level is targeted aid based on actual costs for services. In December, I discussed with the Assembly Task Force on the Handicapped the prospects for categorical State aid to help New York City meet unique projected levels of growth in special education over the next three years.

I am therefore unwilling at this point to endorse any Board of Education budget that will compel substantial teacher layoffs or any increase whatsoever in classroom size. We have six months to explore options before such drastic measures are necessary. While the Mayor may argue that recent educational research disputes the argument that either dollar expenditures per pupil or classroom size affect instructional quality, I personally remain convinced that they are crucial factors particularly in the elementary school years.

REVENUES

Devastating as PEG's expenditure reductions may be, even deeper cuts would be necessary without additional revenues. The Mayor proposes an additional $378 million in revenues for FY'81 and $678 million for FY'82. Of the $378 million, $175 million is projected from increased taxes and fees. The major increases are water and sewer charges ($39 million), the real estate tax ($36 million), the excise tax on beer and liquor ($35 million), and a revision of the financial corporation tax ($20 million).
I support reasonable tax increases and commend the Mayor's courage in proposing them in this City. We have cut expenditures to the point where further reductions will be counter-productive. They will disrupt essential services and diminish the City's attractiveness as a place to live and work. No one wants tax increases, but most citizens will, I'm certain, prefer a marginally more expensive City to a wasteland.

Again, however, I question the specifics of the Mayor's tax proposals. What he proposes is a grab-bag of miscellaneous revenues -- a kind of Chinese menu of taxes and user fees -- one from Column A, one from Column B, etc. This may be shrewd short-term strategy, but it reflects no long-range philosophy about the City's economic future and the revenue base from which we shall draw over the next decade. Real estate taxes today comprise just under half the City's tax base, with the remaining half drawn predominantly from sales, personal income, general corporate and business taxes, and only marginally from the kinds of sources identified in this package. There is no supporting evidence for the projected yields of these tax increases at the amounts determined. We need a clearer rationale for our actions.

The only philosophy that appears to inform this tax package is that the business and income taxes identified with the code words of "economic development" are inviolable. Here again the assertion has no support in data.
Indeed, the tables that do accompany the Mayor's plan indicate that personal income and corporate wealth in the City will rise substantially from 1979 to 1983, with the City receiving a handsome dividend from this growth. There is nothing to suggest, however, that marginal increases on the taxes on this growth, as so often claimed, would discourage continued residence and economic growth here. Indeed, if New York City is providing fertile soil for income and profits, then City government ought to share even more in these developments.

It is, also, more important to remember that just as income and business taxes are sensitive to economic change, so the yield of the taxes and charges the Mayor proposes will change little over time because their base is relatively inelastic. As a result, the gains they yield next year will be rapidly eroded by inflation in the years to come. If tax increases are needed, it may be more prudent to target them on economically sensitive portions of the City's revenue base.

I am particularly distressed by the Mayor's failure to address the problem of tax expenditures in this plan. As we ask citizens to pay higher taxes, we must also reduce the excessive tax benefits we now offer to real estate developers under such programs as J-51, ICIB, 421(a) and IDA.

According to our estimates the City will forego $60 million in revenues through tax exemptions and $30 million through tax abatements in FY'81, and another $70 million through exemptions and $35 million through abatements in FY'82.
Although these exemptions and abatements are irrevocable, the programs under which they were granted are not. If we are serious about increased revenues as an alternative to service cuts, we must redesign, and perhaps in some cases eliminate, these tax incentive programs. Programs that served a valid purpose during recent declines in the City's economy may simply no longer be appropriate or deserving of public subsidy. To cite several examples, a total of $5 million in real estate tax exemptions was granted in FY '79 to support construction of three luxury apartment buildings: the Galleria and the Olympic Tower on Manhattan and the North Shore Towers in Queens. Why when the luxury housing market is stronger than ever are we still subsidizing developers' profits?

INTERGOVERNMENTAL AID

The Mayor's assumptions on intergovernmental assistance are perplexing for a number of reasons. First, the plan continues to assume unrealistic levels of Federal and State gap-filling assistance. Increases in intergovernmental revenues sought just for this purpose will account for 25 percent to 30 percent of the gap to be closed. In FY's '81 and '82, a total of $580 million from Albany and Washington is projected just to fill the gap!

But the Financial Plan not only incorporates these high levels of "gap filling" intergovernmental aid -- it also counts on total amounts of intergovernmental assistance that may be unrealizable, if history is a useful guide.
In fiscal year 1979, actual receipts of total intergovernmental aid have fallen short of the City's estimates in the 1978 Four Year Plan by 10½ percent, a difference of over a half billion dollars.

A look at the Mayor's annual "wish list" of Federal and State assistance is instructive. For example, the Mayor identifies $506 million in potential new funds for New York City during FY'81 and FY'82 as a result of the recent legislation to change the Medicaid formula, at my suggestion by Senator Moynihan. I support this legislation wholeheartedly, but fear we are a long way from banking the dollars! Similarly, the possibility that addicts and alcoholics will be included under SSI benefits, for a local savings of $10 million, is a remote one.

Such skepticism however, is not meant to excuse the State and Federal governments from fulfilling their commitments. In part, it is the failure of Washington and Albany to maintain the levels of funding to which they committed themselves in our Four Year Plan that has brought us to where we are today. As the Mayor wisely notes, the City has lived up to its commitments -- in fact, we've exceeded them. Albany and Washington have not.

The Federal and State governments renege on gap-filling commitments. They cut back on categorical aid and, adding insult to injury, they pile new mandates on top of the City's current work programs without adequate funding. Mandates for special education, clean air, sludge removal, handicap accessibility, water pollution et al. are legislated without matching financial support.
Finally, a movement is, I fear, afoot at the State and Federal level to shift what have been traditionally their responsibilities to local governments. For example, my office recently projected that additional Medicaid outlays by the City for community-based mental health services to deinstitutionalized State patients could cost the City $146 million over the next five years. I continue to emphasize that localities must be held harmless from these increased costs for mental health care.

CAPITAL PLAN

The City's Four Year Plan of 1978 emphasized the urgency of attending to our infrastructure. It committed $2.3 billion dollars over a four year period (FY'79-FY'82), dollars we have been able to raise because of federal loan guarantees. But within a year, it was clear we had underspent our FY'79 capital improvement program by $118 million dollars or 30 percent.

The Mayor's budget report of 1980 argued that original projections had not taken into account "the long lead time needed to instate a large capital program." FY'79 was a year of "gearing up."

The Mayor now reports again, however, that the FY'80 capital program of $582 was also overstated -- for the same reason cited a year ago. The current estimates place underspending in FY'80 at $393 million, or 32.5 percent less than projected. In other words, after a year of "gearing up," we did even worse.
Nonetheless the new financial plan insists that "total spending in the 1979-1982 fiscal year will reach the $2.3 billion initially forecast." The current plan is to spend $650 million and $970 million in fiscal years 1981 and 1982 respectively.

I seriously question our ability to meet these levels of expenditure unless stricter controls are placed on the construction pipeline.

A few quick additional comments on the Capital Plan:

-- The Capital Plan makes it seem as though the City will realize savings in debt service cuts due to capital underspending in 1979 and 1980. What it fails to mention is that the savings are temporary; delaying capital spending until later years simply means that the City is putting off, not saving, debt service costs. In fact, the delay may end up costing the City money if interest rates continue to rise. Borrowing later to finance capital projects may be more expensive than borrowing now.

-- The Capital Plan also fails to mention that delays of capital expenditures result in a loss of purchasing power. In FY'79 alone, the Citizens Budget Commission has estimated, delays cost the City approximately $40 million in purchasing power.
-- Delaying projects increases the number of contracts in future years and creates a buyer's market among contractors. This, in turn, reduces the City's ability to obtain competitive bids and indirectly erodes the purchasing power of our capital funds.
FROM:
State of New York
Financial Control Board
270 Broadway
New York, N.Y. 10007

FOR RELEASE:
Tuesday, January 29, 1980

TESTIMONY

OF

Comer S. Coppie
Executive Director

BEFORE
The Committee on Banking,
Housing and Urban Affairs
Washington, D.C.
Mr. Chairman and Members of this Distinguished Committee:

I am pleased to be here today to discuss New York City's Financial Plan and to share my perspectives on the problems which, I believe, continue to face the City. Federal guarantees of New York City bonds were requested nearly two years ago in order to provide the City with necessary time -- time to develop and implement a budget balanced in accordance with Generally Accepted Accounting Principles and time to demonstrate to the credit markets that it had reformed past fiscal practices. In concert with the establishment of the Federal Loan Guarantee Program, the New York State Legislature continued the responsibility and authority of the Financial Control Board under the Financial Emergency Act to assure the City's adherence to those fiscal objectives through the financial planning process.

The staff of the Control Board is currently in the midst of a review of the City's program to close the budget gaps for FY 1981 and FY 1982. This submission represents an important policy initiative by the City to accelerate the timetable for a GAAP-balanced budget. Mayor Koch has demonstrated the commitment of his administration to the goals of fiscal reform and market reentry by going beyond the requirements of the Financial Emergency Act and the Loan Guarantee Act of 1978 and proposing to achieve a GAAP-balanced budget in FY 1981.

Past presentations of the PEG program have relied heavily on City-wide attrition, O.T.P.S. expenditure reductions, and unspecified management improvements. By contrast, this program outlines agency specific expenditure reductions for both FY 1981 and FY 1982, and presents a sense of priorities with regard to expenditure reductions. In addition, the Mayor has attempted to target tax increases so as to minimize economic disincentives. I believe that the initiative to accelerate the movement to GAAP deserves the support of all the partners in the City's financial recovery program.

Nevertheless, New York City continues to face major problems in achieving its fiscal objectives. The questions remain whether the actions proposed by the City in this PEG program can be effectively implemented and whether these actions will be sufficient to achieve true budget balance as projected. These questions will be extensively analyzed as part of our review of the PEG program. My staff will examine the underlying social, economic, demographic and workload assumptions, checking both their internal consistency and their relationship with similar projections made by other governmental and private organizations. We will also evaluate the methodology used to relate these assumptions to the projections of revenues and expenditures.
In analyzing the specific proposals to close projected budget gaps, we will focus on the salient factors that are likely to affect the potential success or failure of the proposals. These include: (i) the degree to which the actions are within the City's administrative control; (ii) the service impact of the proposed actions; (iii) the City's record in implementing similar proposals in the past; (iv) the quality of the City's description of the actions and the timetables for implementing them; and (v) the practicability of the proposed actions.

The Control Board's staff report reviewing the December modification of the Financial Plan identified what continue to be the most critical issues in evaluating the feasibility of the City's proposed plan. The factor over which the City has least control is the state of the national and local economies. During the first half of the 1970s the City's private sector contracted sharply, eroding the tax base and contributing to the City's developing fiscal distress. A gradual recovery has occurred since 1976, in part reflecting the general national prosperity. The staff of the Control Board monitors key economic indicators, such as employment, retail sales, and consumer prices, and consults with economists from the City's major commercial banks, the Regional Plan Association, the Port Authority and the Federal Reserve Bank of New York. There is increasing agreement among these economists that the City's economy is regaining its health and should be able to avoid significant losses from the moderate national recession that is expected to occur this year. However, it is possible that this recession could be more severe and lead to greater revenue losses in the City than are currently projected. The City and the Control Board must be prepared to take appropriate action should this occur.

A second major uncertainty facing the City is the cost of the labor settlement which must be negotiated this Spring. It is impossible to quantify the costs of future collective bargaining agreements with precision. However, given the magnitude of the amounts potentially involved, the need to plan realistically for the cost of future collective bargaining agreements is an issue of serious concern. A reasonable labor settlement, one that can be funded within the City's Financial Plan, is necessary if the City is to achieve and maintain a GAAP-balanced budget.

In order to provide some coverage for these problems, the Financial Plan modification approved by the Control Board in December contained an unallocated general reserve of $180 million. We will continue to be mindful of these problems as we review the pending modification and the ways in which that modification proposes to deal with these issues.
Another critical problem is the potential of two covered organizations -- the Health and Hospitals Corporation and the Board of Education -- to significantly and adversely affect City finances. The December modification of the Financial Plan reflected a serious deterioration in the financial positions of these two huge agencies whose combined annual expenditures exceed $4 billion. The City's methods of monitoring and controlling these agencies have not proved effective.

Accordingly, the Board has taken a series of actions with regard to the covered organizations. The Health and Hospitals Corporation has developed a pattern of deficits largely because of its inability to collect sufficient third party revenues to meet Financial Plan targets. The Board has required that the City establish special reserves allocated to cover potential HHC deficits projected by the Board's staff. In FY 1979 a $28 million reserve was established before the Financial Plan was approved. This reserve was adequate to offset the revenue shortfall for that year. The reserve in the current plan for FY 1980 is $54 million, which we project will again be adequate to cover the projected shortfall. In this fashion, through our review process, we have been requiring the City to plan for projected HHC deficits in advance rather than attempting to deal with those deficits in the last quarter of the fiscal year.

In addition to requiring increased reserves for HHC, the Board's staff initiated an extensive review of HHC's revenue collection problems. This special study was undertaken because of the enormous drain on City funds created by HHC's chronic revenue shortfalls. Our report, which was issued last September, was highly critical of the implementation of HHC's new computerized collection system and presented twenty-one recommendations to improve the collection process. We have since received commitments from HHC management and from the City that these recommendations will be implemented, and HHC has retained Touche Ross and Company to assist in improving its revenue collection procedures.

On the expenditure side, both HHC and the Board of Education experienced significant cost overruns during the first quarter of FY 1980. Both organizations were unable to schedule by operating program the proposed total expenditure reductions reflected in the Mayor's Executive Budget. These developments underscored the need for the City to strengthen its methods of monitoring and controlling the finances of these agencies, both of which have traditionally exercised significant degrees of operational and fiscal autonomy. As a result, the Financial Control Board insisted that the City develop and implement control plans for these agencies in order to maintain the viability of the Financial Plan. The control plans which have been developed provide for improved reporting and monitoring procedures and require prompt and effective action to correct any significant variances which develop.
The latest submission of the Financial Plan which is currently under review depends heavily upon the City's ability to improve revenue collections in the Health and Hospitals Corporation and to control expenditures in both agencies. Implementation of the control plans will be closely monitored by the Financial Control Board in the coming months.

The City's plan also requires substantial annual increases in recurring intergovernmental assistance to close the budget gaps in FY 1981 and FY 1982. Because of the pressures to contain expenditure at all levels of government, this additional aid may prove unattainable. The Control Board will monitor the progress of the City's intergovernmental aid proposals carefully and realistically. We will require that the City undertake further action if shortfalls in projected intergovernmental assistance occur.

I must, nevertheless, point out that the City's capacity to make expenditure reductions is increasingly limited by mandated service levels in a growing number of agencies. The recent court decisions on Special Education provide an excellent example of the escalation of this trend. Program restructuring has been required within the plan to fund Federal and State mandated programs and at the same time to achieve the level of expenditure reduction currently estimated by the City.

The success of the City's effort to reduce expenditures while maintaining adequate service levels will also depend upon efforts to make necessary management improvements and to increase productivity. As we stated in our year-end report on the New York City Productivity Council, the Council has initiated no significant productivity programs to date. The record of productivity efforts in New York City during the last decade, however, reflects innovation and, in varying degrees, general accomplishment. It is our hope that the recently restructured Council will make a more effective contribution in the future.

The ultimate goal of New York City's financial planning process is full market reentry. This fiscal year the City has already made two successful public offerings of Revenue Anticipation Notes and is planning a third offering next month. If successful, as expected, the City will meet its total seasonal borrowing needs of $600 million for this fiscal year in the public market.

However, a number of observers have recently questioned whether the schedule for reentry into the long-term public market in FY 1981 is realistic. This skepticism has been based
on the difficulty of obtaining an investment-grade rating for City bonds before GAAP budget balance is achieved in FY 1982, and upon the possibility that credit analysts may require the City to show more than one balanced budget. In view of those concerns, the City's prospects for reentry into the bond market may be improved by the recently announced acceleration of the City's timetable for achievement of a GAAP-balanced budget.

Contingency plans exist to meet the financing needs of the City in FY 1981 and FY 1982 if the City does not achieve reentry to the public bond market in those years. However, the Proposed Financial Plan for FY 1983 reflects no assured source of financing for the City upon the expiration of existing agreements. In spite of the significant progress to date on budget problems, there remains the possibility that the City may not be able to meet all of its long-term capital requirements through the public sale of City bonds in FY 1983, and contingency plans should be developed for that period as well. It is important to recognize that failure to regain full access to the public credit markets no longer poses a threat to the City's solvency, although it will limit the size of the City's capital program.

The City continues to experience chronic difficulties in realizing its original capital expenditure projections. The Financial Plan originally approved by the Control Board in November, 1978 projected an aggregate of $2.3 billion in City-funded capital expenditures during the four year period ending June 30, 1982. Annual expenditures in that plan were expected to almost double from $382 million in FY 1979 to $749 million in FY 1982. However, actual expenditures during the first year were only $264 million, a decrease of approximately 30% from the original projections.

In the proposed Financial Plan modification, the City continues to project that capital spending over the four year period will aggregate approximately $2.3 billion. However, the projection of cash spending for the current year has been reduced to $394 million, approximately 18% less than the projections originally made in November 1978. In view of the spending shortfalls experienced during the last two years, maintenance of the $2.3 billion spending objective has required a dramatic increase in projected capital spending for FY 1982. The proposed modification contemplates a spending level of $970 million for FY 1982, more than twice the level of spending currently projected for this year and nearly 30% more than the City's original spending projections for FY 1982.

The City has begun an in-depth analysis of its capital program and the methodology used to develop and monitor capital commitment and spending projections. We have been closely monitoring the progress and results of that analysis in cooperation with representatives of the Municipal Assistance Corporation and will continue to do so.
It is all too obvious that realization of the City's very ambitious capital spending objectives will, at a minimum, require a major commitment to capital planning and management that has already been too long delayed. We are insisting that the City make that commitment and that it begin to detail the steps necessary to realize its goals. The analysis of the capital program recently begun is just the beginning of an effort which we believe could result in more reliable projections of capital commitments and spending and in a vastly increased capacity to realize those projections.

In conclusion, I wish to underscore the importance of the recent decision to accelerate the timetable for achievement of a GAAP-balanced budget. During the complex process leading to the final adoption of a new City budget, modifications in the Mayor's intricate package of expenditure reductions and revenue increases will undoubtedly be required. However, the critical factor is the commitment of all of the participants in the process to the Mayor's goal of a GAAP-balanced budget in FY 1981. Realization of this objective would represent a truly significant milestone toward the achievement of full fiscal recovery for the City of New York.
Mr. Chairman and distinguished members of the Committee: thank you for this opportunity to present some of the views of my office as they relate to New York City's fiscal situation. As you may know, in the past I have had a reputation as one who prodded the City most strongly to do more to help ensure a balanced budget, and to take the necessary budget actions earlier in light of the financial problems that lay ahead. At this point, however, it gives me satisfaction to be able to give praise to the City and its Mayor.

The City's decision, as evidenced in its Financial Plan submission presented on January 16, 1980, to accelerate by one year the statutory timetable for balancing its budget in accordance with Generally Accepted Accounting Principles, or GAAP, is a significant action. It deserves recognition for three very important reasons:

1. First, it can provide for a more orderly process of retrenchment than would be possible if the major expenditure reductions were left until fiscal year 1982. This more graduated timetable should allow the necessary cost reductions to be phased in, so as to minimize, to the degree possible, the impact of those reductions on the City and its residents. State Comptroller Edward V. Regan has repeatedly urged the City to formulate detailed gap-closing programs on a multi-year basis, and to implement a more systematic and rational expenditure reduction process. I believe that the most recent Financial Plan submission shows an intent to provide this much needed fiscal discipline. However, I believe there is a need for the City to present to the public its best estimate of the service impact of
the proposed budget reduction, and the estimated economic
effect of its programs for increased revenues. Here, too,
State Comptroller Regan has taken the position that this type
of fiscal planning is for the ultimate benefit of the
government involved.

Second, the accelerated plan for achieving a budget balanced
pursuant to GAAP demonstrates to the City's oversight bodies and
to the financial community the City's commitment to meeting
its budgetary obligations. If successfully accomplished, the
City will be able to test the long-term credit markets - after
having met all the goals of the Four-Year Financial Plan - at
a time when alternate means of financing are still available
from the sources provided for in the City's four-year financing
plan. Thus, the City's planned reentry into the markets would
occur in an atmosphere of order and discipline. In contrast, a reentry
program would be more strained if it occurred without the alternative
of other financing options available, and with the prospect
of insufficient cash to meet obligations if market entry proved
more difficult than anticipated. During fiscal years 1979 and
1980, the City's reentry in the short-term market occurred within
such a controlled environment, at a time when loan agreements were
in place to assure the City the short- and long-term financing
it needs. In my opinion, the existence of this facility was
a most significant factor in the City's successful reentry into
the short-term credit markets last January.

Third, by eliminating the need to borrow in fiscal year 1981 for
capitalized operating expenditures, the City has reduced the need
for new debt issuances. This, in turn, will reduce the budgetary
pressures in future fiscal years, and increase the debt restructuring
options.
In this same positive vein, and assuming a successfully balanced budget in fiscal year 1981, I would like to discuss two financing situations that may result in fiscal year 1982.

The first and best situation would be that the City achieves full entry into the long-term public credit market - something we all hope for. In that event, I would recommend that in fiscal year 1982 the City also attempt to finance some or all of its fiscal year 1983 capital spending requirements. Until a solid history of continuing access to long-term financing is assured, it would seem desirable to take maximum advantage of borrowing opportunities in order to help assure continuity of capital funding. This advance bonding is one of these expedients. The proceeds of such financing must by law be set aside to be used only for their intended purposes.

A second and less desirable situation would be if the City is unable to achieve entry into the public long-term market in fiscal year 1982, or if such entry is limited to only a portion of the City's needs. Even in this instance, however, there would still be time for those most responsible for managing the City's finances to develop alternate financing strategies for fiscal year 1983 and beyond, to ensure that the City's capital funding requirements can be met.

In spite of these positive elements, however, one should not be deluded into believing that the City's major fiscal problems have been resolved. Therefore, my testimony would not be complete if I did not continue to carry out my responsibilities by pointing out not only the positive aspects of the City's proposed financial plan modification, but also some of the significant risks the City faces in continuing to achieve a balanced budget.

First, the plan submission relies on significant tax increases whose enactment is dependent upon local and in some cases State legislative actions - actions which are far from assured at this time.
Second, accomplishment of the plan is subject to a number of other major uncertainties, including:

1. The realization of the increased amounts of State and Federal aid anticipated in the plan;
2. The impact of inflation and recession on the revenue and expenditure estimates;
3. The size of the projected deficits of the City's semi-autonomous agencies, known as covered organizations;
4. The City's continued failure to resolve managerial shortcomings; and
5. The size of future labor settlements.

I would like to elaborate on each of these items.

The plan submission anticipates the receipt of $170 million in increased State and Federal assistance in fiscal year 1981 and an additional $240 million in fiscal year 1982. Previous City submissions provided for standby cost reduction programs in case those levels of aid were not achieved. However, no such standby program is either contained or proposed in the most recent submission. In light of the pressure for fiscal restraint evident at both the State and Federal levels, and absent an absolute commitment by these levels of government that they will fulfill the City's expectations, the lack of a standby program is a matter of concern.

The City's plan could also be adversely affected by the negative economic events that are now forecast on a national basis. Economists are predicting an inflation-driven recession having potentially serious adverse affects. The City's plan already anticipates substantial expenditure increases as a result of inflation, particularly in the field of energy. Even greater increases, however, may result if the inflationary pressures of the last calendar year are not abated. For instance, the plan assumes a 25 percent annual increase in fuel costs in fiscal years 1981 through 1984; however, in calendar 1979, such costs increased by about 75 percent.

In addition, the problems of the covered organizations have yet to be
solved. Substantial deficits still loom in the Transit Authority and Health and Hospitals Corporation, and if these deficits materialize, they could place the City's plan in jeopardy. This is particularly so insofar as the Health and Hospitals Corporation is concerned. In the past the City has substantially increased its operating subsidy to meet the Corporation's budgetary shortfalls, and our preliminary analysis of the most recent plan for the Corporation indicates that subsidy increases may be needed in future years as well—unless the Corporation's revenue collections improve over current levels. The resolution of the Transit Authority's financial woes is also being debated, and the City's Financial Plan does not contemplate that the solution will impact on its budgets.

The City's plan would also be adversely affected by the continued failure on the part of the City to resolve managerial shortcomings that must be eliminated in order that City operations be conducted in a climate which fosters fiscal responsibility. During the past four months my office has issued the first two in a series of reports that focus on various aspects of the City's management controls. These reports have been developed in special consultation with State Comptroller Regan, who has expressed his concern over the need for improvements in the management of City operations. The first of these reports, which focused on the City's implementation of its capital development plan, noted that the methods currently used by the City to formulate and manage its capital program are seriously inadequate, and proposed several major changes in the existing capital processes. The second report noted that the established City procedures for the review and implementation of outside recommendations aimed at improving City operations are not being followed. It is imperative that these recommendations be followed up if the City is to achieve maximum benefit from these efforts. The first of these reports, which focused on the City's implementation of its capital development plan, noted that the methods currently used by the City to formulate and manage its capital program are seriously inadequate, and proposed several major changes in the existing capital processes. The second report noted that the
established City procedures for the review and implementation of outside recommendations aimed at improving City operations are not being followed. It is imperative that these recommendations be followed up if the City is to achieve maximum benefit from these efforts.

The largest and most immediate uncertainty relates to the upcoming labor settlements. If the settlements are greater than the amount currently provided for in the financial plan - an amount equal to the cost of the settlement that was negotiated in the 1978-80 period - the City's deficits will increase. For example, a 7 percent annual increase, in line with the original Federal guidelines, could increase the City's deficits for fiscal years 1981 and 1982 by approximately $200 million and $375 million, respectively. Each additional 1 percent annual increase would cost $50 million in fiscal 1981 and over $100 million in fiscal 1982.

These concerns, of course, have a material impact on any assessment of the City's near-term financial prospects, and will be considered in my office's review of the City's proposed Financial Plan submission. There is also a long-term concern that I would like to highlight. The City's projections for fiscal years 1983 and 1984 indicate potential gaps of $250 million in fiscal 1983 and $300 million in fiscal 1984. As noted in the City's submission, however, these gaps do not reflect any further labor cost increases beyond 1982. A 7 percent annual increase, for instance, could raise the 1984 gap to over one billion dollars. The possibility of such a large gap only two years after a presumed successful balancing of the City's budget in accordance with GAAP is due to a basic imbalance in the City's revenue and expenditure structure. Most of the City's expenditures can be expected to increase as a result of inflation (average salaries tend to increase in periodic leaps, based on the negotiated pattern). However, there are no assurances that two significant sources of City revenues, which together comprise more than half of the City's revenue stream, will perform similarly. One of these sources is the real estate tax. This tax, in recent
years, has not exhibited significant growth despite continued inflation. The other revenue source – State and Federal aid – also does not necessarily increase with inflation.

While the City itself must deal with the sluggishness of real estate tax revenues, this Committee will have significant input into the availability of increased intergovernmental assistance to the City. In the last two years despite a substantial surge in inflation, Federal aid to the City available for budget balancing purposes has actually declined by several hundred million dollars. For one, the City lost countercyclical aid which totalled $140 million in fiscal year 1978. The amount of CETA funds that the City can use to fund municipal employees has also declined; resulting in the reduction of the City's CETA funded workforce by some 11,000 people in fiscal year 1980 as compared to the fiscal year 1978 levels. Moreover, at the same time that such aid has been declining, the Federal government has been mandating substantial increases in City expenditures as a result of new initiatives in special education, medical assistance, and environmental protection. You are all aware of the mandate to improve the quality of education for the handicapped. While this action may have social benefits, it has an adverse impact on the City's budget because the Federal government did not provide the funds to implement the increased services.

In a previous appearance before the Committee in April 1976, I urged that the Federal government revise its procedures for providing aid to local governments. I noted that the Federal government had in many instances imposed new mandates without providing the funds necessary for implementation. I recommended then, and I reiterate now, that the Federal government consider an "all or nothing" standard in setting local mandates, namely, that if it truly believes that a program is necessary, then it should provide full funding for it. Alternately, the institution of the program should be left to local discretion.
I further suggest that the funding provided by the Federal government should be made responsive to inflation, and that the Federal government be prepared to bear the responsibility for many of the costs now borne by local governments, costs which result from national problems, and which should be addressed at a national level. These new initiatives are critical if the City's financial plan objectives are to be accomplished.
PROXMIRE: Why the change of heart since last year to making cuts and raising taxes. Last year you said you didn't need to do this.

KOCH: Going to GAAP one year early forced this. It is better to take these actions over two years, more gradually, than waiting to do it all in 1982.

PROXMIRE: Can you achieve it? What about the need for additional Federal and State aid in PEG.

KOCH: We have managed it before when Federal and State aid didn't come through. We will either increase revenue or reduce expenditures. Governor Carey is publicly committed to State aid to help the City.

PROXMIRE: Labor was screaming yesterday that a 4% increase is not enough. Federal guidelines allow 7½% to 9½%. What happens if labor comes in higher?

KOCH: We can't pay more than we have.

SENATOR FROM INDIANA: What can you do about performance in the capital area?

KOCH: Our capital program is not in disarray. We will live up to our commitment to spend $2.3 billion.

QUESTION: Are City services being hurt by these cuts?

KOCH: We prioritized the cuts. Although every agency took some cuts, essential services: Police, fire, sanitation were left largely intact.

QUESTION: What are the administrative actions that you include to help the budget on the Federal/State levels?

KOCH: I will submit a detail backup to you.

QUESTION: Health and Hospitals Corporation cuts--can they happen?

KOCH: We will close hospitals. We also have new management systems.

PROXMIRE: Mr. Goldin, what are you doing to get ratings up to investment grade. Should you request a ratings upgrade now?

GOLDIN: Rating agencies have not been very reassuring. We have done many things to help; moved up timetable on GAAP, moved up timetable on OC's sold notes publicly, etc.

PROXMIRE: You have done impressive things. You should push the rating agencies.

GOLDIN: Our consultants, Dillon, Reed, do not advise it at this time.

PROXMIRE: Can you give us a statement from Dillon, Reed as to why this is imprudent?
PROXMIRE: What are your contingency plans if you fall short of selling City bonds next year?

GOLDIN: 1) MAC would take up part; 2) reduce City needs...

PROXMIRE: What about Water and Sewer Bonds? The rating agencies responded very favorably yesterday...

GOLDIN: We are considering it now. It certainly is not advisable to reduce City capital needs.

PROXMIRE: Last Fall, Goldin, you said New York City would need some more guarantees after 1982.

GOLDIN: That is not realistic.

PROXMIRE: Carol Bellamy, what is your sense as to whether the City Council will pass the new tax package?

BELLAMY: Generally the attitude is that it will pass. Maybe with different details.

PROXMIRE: The Treasury said yesterday that the City won't need any more guarantees. Is this accurate?

KOCH: No. I am not abandoning the Standby's, but we are expecting not to need them.

PROXMIRE: The Unions say you simply haven't talked to them about productivity.

KOCH: That is B.S. We are making productivity moves.

MOYNIHAN: Federal mandates are killing us--decreasing Federal Aid. Feds went back on commitment.

PROXMIRE: What Federal commitment that was from the President, Congress has lived up to our part.

TESTIMONY--MONITORS PANEL  (Schwartz, Coppie, Berger, Brigham)

PROXMIRE: Rating agencies very negative about New York City budget. You haven't really balanced it yet?

BRIGHAM: They ignore our progress. GAAP in '81 is within our grasp. But expenditures are growing faster than revenues. We have addressed expenditures about as much as we can. Part of the problem has to be addressed on the revenue side, productivity.

PROXMIRE: Berger, what do you think?

BERGER: City has to eat all it can.

SCHWARTZ: If Mayor can do it, he will, but much is not under his control.

PROXMIRE: Coppie, what do you think? They haven't done much with major budget problems, HHCC, BB...

COPPIE: I would give a qualified yes as to whether they can accomplish the proposed expenditure reductions.

CHR/pfs/1/30/80
Mr. Chairman and distinguished members of the Committee. Thank you for providing me this opportunity to express my views regarding New York City's fiscal situation. I join with the Chairman of this Committee and the representatives of agencies charged with the responsibility for overseeing the City's financial condition in endorsing the direction charted by the Mayor in his January 16th financial plan. In my various roles since the fiscal crisis in 1975 in monitoring the City's fiscal affairs, I have continually stressed the need for the City to avoid delaying difficult budgetary decisions which remain ultimately necessary for the City's successful re-entry into the public credit markets. Among other issues, I have expressed concern that the City balance its budgets through the use of recurring revenues or savings, recognize the costs of pensions on an accrual basis, institute management reform and, more recently, improve the capacity to control and direct its capital programs.

The Mayor's most recent Financial Plan begins the shift away from the pattern of the 1978, 1979, 1980 Financial Plans which avoided major retrenchment decisions and accelerates the difficult process of confronting the need to achieve and maintain a budget balanced according to Generally Accepted Accounting Principles. I would like to applaud the Mayor in this effort.
In endorsing the Mayor's strategy, however, I must still express caution and reservation regarding many pieces of the new Plan and the methods by which the City hopes to achieve its goals. With the Mayor's plan to move to a GAAP balanced budget just six months from now, which necessitates closing larger budget gaps in fiscal 1981 than originally planned, a number of uncertainties remain. The cost of upcoming labor settlements, while impossible to predict, remains a major uncertainty with regard to the City's Plan. Labor increases in excess of that which is provided for in the current plan could require additional City actions not yet contemplated.

The Health and Hospitals Corporation (HHC) continues to overspend its budget and will require increasing City subsidies. Although the HHC may benefit during the current fiscal year from greater than anticipated State rate increases for Medicaid and possibly substantial rate appeal settlements, a $50 million budget gap in HHC for fiscal 1980 will have to be closed by an allocation from the City's General Reserve Fund. While there have been some small improvements recently in the HHC's baseline revenue collections, expenditures are projected to increase from 1981 through 1983 creating larger gaps to be closed in those years. A significant portion of the City's plan to reduce future budget deficits in the HHC is contained in the Mayor's Plan for hospital closings and reorganization which must be implemented in the near future in order for the Plan to have the required positive budgetary impact in fiscal 1981 and 1982.

The Board of Education (BE) also continues to cause concern. The new Financial Plan projects expenditure increases for the BE of almost $300 million from fiscal 1980 through 1983. These expenditure increases result largely from State and Federal mandates and Court orders with regard to the education and transportation of handicapped students. These growing costs are not projected
to be offset significantly by intergovernmental aid. In addition, the plan assumes increasing levels of State and Federal education grants from 1981 to 1983 which must be regarded with uncertainty in the current fiscal climate. A significant portion of the Mayor's Plan to eliminate City-wide budget gaps is dependent on large expenditure reductions in the Board of Education ($111 million in 1981) which almost certainly must involve school closings and teacher and other personnel layoffs. As a semiautonomous agency, under pressure to meet Federal mandates, the BE is not directly under the Mayor's control and the proposed cuts in the BE budget will, by their nature, be difficult to achieve.

Although the new Financial Plan begins a strategy which includes City-wide expenditure reductions, the City's Program to Eliminate the Gap in 1981 and 1982 includes the need for additional State and Federal actions of $170 million and $410 million, respectively. It is becoming increasingly evident that both the State and Federal governments are moving into a period of budgetary retrenchment. Even where additional aid appears to be forthcoming, the pattern seems to be a shift from general revenue sharing to categorical assistance, which will make the City's goals for additional intergovernmental budget balancing aid difficult to achieve. The current Financial Plan makes no provision for additional City actions, should this aid fail to materialize.

In order to move to a GAAP balanced budget in 1981, the Mayor has proposed a series of tax increases including a small increase in the property tax, excise tax on beer and liquor, revision of the financial corporation tax,
extension of taxes on gasoline and hotels, and a rate increase for water and sewer services among others. Most of these proposals will require legislative action and therefore must be regarded as uncertain at this time.

The City's Plan may also be negatively affected by national economic events. Although the City's Plan provides for the impact of a mild recession during 1980, it is possible that this recession may be deeper or more prolonged than anticipated. This situation could cause a reduction in revenues which could occur in the face of continued inflationary pressure or expenditures.

Another area of concern to me is in the City's management of its capital program. While it is clearly evident that the City's physical plant is rapidly deteriorating, the City has failed to fully utilize the resources made available to it in the four year plan for bricks and mortar. While the Mayor is correct in pointing out that recreating a viable capital program after three years (1976-1978) of forced inactivity takes time. Management improvements in the capital program have lagged more than those in other areas. The City is not yet at a point where it is meeting its capital needs and there has been a lack of major progress with regard to directing and controlling the capital budgeting and planning process. The ultimate economic viability and habitability of New York City is dependent upon a capacity to plan, finance, and execute restoration of its physical plant.

I will continue in my role in assisting the Municipal Assistance Corporation for the City of New York to monitor these and other areas of the City's fiscal situation with the clear goal of helping to ensure that the Mayor succeeds in a strategy that is on the right road to fiscal health of New York City.

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STATEMENT BY CITY COUNCIL PRESIDENT CAROL BELLAMY
BEFORE THE
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE
WASHINGTON, D.C.,
TUESDAY, JANUARY 29, 1980

I am pleased to testify again before this distinguished committee.

Ten days ago Senator Proxmire congratulated Mayor Koch on his decision to bring the City's budget into balance according to generally accepted accounting principles a year ahead of schedule, congratulations that our Mayor and City richly deserve, for we have taken a great leap forward. While others have been talking about fiscal austerity, we have been living it in the City of New York. While others have become recent converts to balanced budgets, we have made them an article of faith. Our past has chastened us, and the last four years have toughened us. We can stand up to fair judgment.

As the Mayor has just reported, we ended fiscal year 1979 with a financial plan surplus of $216 million, exceeding the budgetary goals of the federal and State governments. We reduced our budget deficit, as defined by Generally Accepted Accounting Principles, by $290 million since fiscal year 1978. We reduced our annual borrowing needs from $1.875 billion in 1978 to $650 million in 1979. We publicly sold $275 million worth of short term notes at interest rates below the cost provided by a loan agreement with private lenders.

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We obtained this financing in part because of the Federal loan guarantees you passed -- and again, we thank you for them. On balance, I agree with the Mayor and the Comptroller, that our prospects for full market reentry by 1982 are good -- it's unlikely that we'll be back to you again for any loan guarantees. That, by no means, however, is meant to suggest you won't be hearing from us any more.

Indeed, we in New York have taken many steps that some of you on this committee said wouldn't be taken. So I am puzzled that along with his congratulations, Senator Proxmire last week insisted on once again taking us to task for seeking to balance our budget "on the back of the Federal government." Allow me, Senator, not only to differ with this characterization ... but to say that if the emperor of this drama is the Federal government, then it may well be the emperor who wears no clothes.

The 1978 plan to save New York City, though not written in stone, made a number of basic assumptions about prospective actions on the part of the Federal, State and City governments. The City, has made good on its part of the plan, buffeted by some favorable economic trends, but also in the face of some adverse ones.

Yes, it is true that our jobs picture, which as much as anything was key to the decline of the late sixties and early seventies, is now beginning to turn around. We lost 600,000 jobs from 1969 to 1976, but payroll employment in the City has risen marginally in the years since --

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as has personal income -- and the city reaps the benefits of these developments in the growth of that substantial portion of our tax base derived from personal income and corporate profits.

So too, Manhattan's commercial and residential real estate is booming -- with evidence of some spillover effect on our outer boroughs. We're experiencing a growth in retail sales; tourism is at record levels; 17.5 million people visited our city in 1979 -- spending more than ever before, and producing an estimated $180 million in direct tax revenues. Foreign capital continues to pour across our shores -- in part a response to the happy fact that our consumer price index continues to rise at a slower rate than elsewhere in the nation and abroad.

But it is also true that New York's overall employment rate continues to lag behind national growth levels. The future is particularly unpromising for the large numbers of blue-collar and unskilled workers in our city whose inability to find jobs has severe implications for a city treasury that pays out billions of dollars each year in welfare, medical and housing costs for the poor. So too, it should not be forgotten that Manhattan's skyscrapers cast shadows on acres of abandoned housing in our city -- the burden of which falls on local government to maintain.
In sum, even as we see promising signs of growth in the City's revenue base, we see those gains eroded by burgeoning costs for social services, housing, health and especially for energy -- costs that even the most pessimistic of our forecasters find difficult to reconcile.

The City then has found it necessary to meet our budgetary goals not just by growth but also by severely cutting services -- laying off police officers, firefighters, sanitation workers and teachers. In 1975, New York City employed 282,858 workers. Today that figure is 193,626, a decline just short of 32%. And our financial plan for 1981 proposes 5,000 additional workforce reductions. Regrettably the full force of these reductions is not reflected in a parallel budgetary decline because of the impact of inflation, wage hikes and pension costs.

Those who continue to believe that New York City is a model of profligacy thus clinging to a fiction. We have whittled our budget down to the core. Any more severe cuts may damage the essence of what it seems to me a City must provide in order to survive -- basic police and fire protection, education for our children, an energy-efficient public transportation system which is essential to the continued health of our economy.

Of course we in New York City are not without fault. Management improvements, such as further civilianization of our uniformed services, and reduced manning in sanitation -- still elude us.

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We still lag behind in our capital program, an inexcusable waste of valuable financing. But we are paying locally for these failures by coupling expenditure reductions with proposed tax increases. As we ask our citizens to get along with less, we also demand that they pay more.

What then can we say about the records of our partners in the endeavor to assure New York City's future? We are, after all, not an island unto ourselves. Are we wrong to point out that Washington has fallen woefully short of its commitment to the Four Year Plan? And Albany, a valued partner in the past, now plays coy with us, saying on the one hand that the State expects to balance its budget at the expense of localities, while hinting of other dollars hidden away to close our gap?

Honorable Senators, it is time the federal government recognize its obligation to New York City's Four Year Plan. The dollars we seek represent money to which, by any reasonable standard, New York City and the rest of Urban America are entitled. In three critical areas -- unrestricted gap-filling aid; reimbursements for welfare, health, transportation and energy; and, finally, as the Mayor has so clearly demonstrated -- in the full funding of federal mandates -- we must have the full assistance to which the Federal and State governments have in the past committed themselves.

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Last week I challenged the Mayor's financial plan for fiscal years 1981 and 1982, because it incorporates a total of $580 million just in "gap-filling" assistance from Albany and Washington. What is more, it counts on total amounts of intergovernmental assistance that may be unrealizable, if history is a useful guide. Rough calculations by my staff -- determined that in fiscal year 1979, for example, the City's actual receipt of total intergovernmental aid fell short of projections in the 1978 plan by 10-1/2 percent, a difference of over a half billion dollars.

My skepticism, however, was not meant to excuse Washington and Albany from its commitments. I say again, New York City has lived up to its commitments -- in fact, we've exceeded them. Albany and Washington have not.

Permit me just a few examples:

First, with respect to "gap-filling" aid, there is little more to say than that general revenue sharing for localities must be continued at a minimum of current levels, while, at the same time, a countercyclical program is reinstituted.

Second, in the area of mandates, last spring my office released a study on the costs of Special Education for the Handicapped. The number of handicapped children processed by New York City's Board of Education has grown by 20,000 over the last five years. Local costs of special education have increased 55 percent, while our general education budget grew only four percent.
Regrettably, federal assistance to cope with this growth is being phased in at a snail's pace; instead of federal aid to the handicapped for FY '81 covering 30% of our costs, we now expect to receive only 12 percent. So too, while we received slightly over $100 million for special education from the State for this current fiscal year, an increase of 8% over 1979, this figure, which was calculated on the prior year's expenditures, still fell far short of our actual costs. The fact is that the increased costs of the additional handicapped children in New York City's school system this year and next will largely be absorbed by City tax levy dollars. And what that means is quite simply that $114 million in administrative and pedagogical cuts are now being proposed for the Board of Education -- cuts that some say will translate into a dramatic impact on regular classroom size.

Third, on the subject of health and welfare costs: I have said that New York City's total receipt of federal dollars is falling substantially behind projections. Let me further explain how federal formulas in our major social welfare programs discriminate against us.

My office last year commissioned research on inequities in the current Medicaid financing formula. Washington spends $10 billion annually in local and state reimbursements, that vary substantially from state to state, ranging from a base of 50 percent in New York and 14 other states to more than 70 percent elsewhere.

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Senator Moynihan has since introduced legislation to equalize this formula and remedy an antiquated and unjust system. The implications of such a change for New York City alone would be $200 million a year in increased funding. Increased federal costs nationwide would be $2.1 billion.

We are spending nearly $2 billion a year in New York State out of our own resources just to pay for what is termed our share of the national Medicaid program—and hundreds of millions more to cover the full costs of health care for needy individuals and families not eligible for the federal program.

This is an exact parallel to our situation with respect to the federal welfare program (AFDC). Yet the Carter Administration's current "welfare reform" proposals, while they cost a total federal $5.7 billion nationwide, would yield New York at most $150 million in "fiscal relief," -- a return of about 22¢ on our federal tax dollar, and just ten percent of what New York State and its counties currently spend on cash assistance -- out of our own resources.

The fact is we cannot even maintain our programs on this basis, much less improve them. Our welfare benefits, frozen since 1974, as a consequence of the State's fiscal difficulties, lose more of their purchasing power to inflation every year. Our Medicaid program, which cannot, and ought not be "frozen" grows more expensive every year.

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I repeat:

The federal government has reneged on gap-filling commitments. You’ve cut back on categorical aid. You’ve piled new mandates on top of the City’s current work programs without adequate funding. Mandates for special education, clean air, sludge removal, handicap accessibility and water pollution are legislated without matching financial support.

As Mayor Koch said last Thursday to a conference of mayors from 28 cities, these burdens are not New York City’s alone. They now plague cities across the country.

When we approached you back in 1975, our circumstances were, indeed, very special. Today the questions of New York City and its relationship to a nation are questions of the relationship of a nation to all of its aging urban centers.

We are seeing a scenario all too familiar to us in New York replayed in Chicago, Detroit and Philadelphia. Fiscal nightmares, unmet payrolls, massive layoffs. Until and unless we develop new mechanisms for municipal finance -- mechanisms free of categorical strings or costly mandates -- all of us in these cities will continue to perform precarious balancing acts.

We must begin now to plan together for the future of America’s cities. For unless we plan now, we will discover that the quality of life in our cities will not be determined by us, but by events beyond our control.

Thank you very much.

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Senator Proxmire, members of the Senate Banking Committee:

Hello again. We are here today to meet the City's continuing obligation under the Loan Guarantee Act of 1978 to explain our past progress, present problems and future prospects.

Last year, in urging further extensions of loan guarantees by the Treasury pursuant to the Act, I presented the consensus that the City's full financial recovery would be signaled by its ultimate full re-entry into the public credit markets.

That is still true.

I also presented the prevailing view that the City would regain full and unrestricted, albeit disciplined, access to public credit by fiscal year 1982 when its expense budget would be in GAAP balance, that is, in balance according to Generally Accepted Accounting Principles.

That can still be true and most of our strategies are still premised on that accepted wisdom.
But it ain't necessarily so. It does not follow as the night the day that once the City achieves GAAP balance everybody's uncle will be willing to lend the City whatever it asks for and needs. What does follow is that certain steps can be taken that will give the City a better chance to re-enter the credit markets and that we must plan for the contingency that while the City will complete its fiscal reforms, lenders will not flock to our doors.

Much affecting New York City and the restoration of its credit has changed since we last testified nearly a year ago. Unsettling world events, national reactions and local economic conditions everywhere have engendered a jittery urgency which has affected all markets with a deep uneasiness and uncertainty.

Indeed, as far back as October, at an Arden House Conference on municipal priorities, I suggested that market psychology may have changed sufficiently for us to need to plan for the contingency that a balanced budget will not ipso facto immediately pry open the doors to public credit.

By the end of the year we had received enough signals from the investment community to warrant my stating flatly that the City's two major fiscal goals, a GAAP-balanced budget and complete access to public credit, can no longer
be considered to follow quickly one from the other. We must now recognize the possibility that despite the City's achievement of GAAP budget balance, it may not be able to re-enter the public credit markets to the extent and within the time frame contemplated. On the other hand, I would emphasize that there would be no possibility for the City to accomplish the second goal, the re-establishment of public credit, without achieving the first, GAAP budget balance.

We must acknowledge the possibility of less than full re-entry and plan for it despite our pride in the extraordinary fiscal accomplishments of the City since the crisis began in 1975, accomplishments conceded both by the City's severest critics and outside independent auditors:

1. An operating deficit estimated at $1.87 billion in 1976 was cut to $422 million by June 30, 1979.

2. Almost $6 billion of short-term debt was either repaid or exchanged for long-term MAC financing.

3. All subsequent seasonal financing--Federal, negotiated or public--was repaid before June 30 of any given year; that is, we have had no more rollovers of temporary debt.

4. We have achieved limited re-entry to the short-term credit markets. The City raised $275 million in two note sales to the public in fiscal year 1979.

5. The credit rating on City notes was upgraded by Moody's from MIG-4 to MIG-3.
6. The State's annual $800 million advance was eliminated, half through the sale of MAC bonds and half through a much improved cash position.

7. Our cash flow has improved dramatically: the City borrowed only $650 million short-term during fiscal year 1979, compared with the high of $2.1 billion under the Federal Seasonal Loan Program.

8. Our budgetary situation has improved markedly: the City finished fiscal year 1979 in a budgetary position some $200 million better than planned.

9. Despite the need to finance our deficits, our net outstanding debt, including City bonds, MAC bonds and capital lease obligations, is actually $480 million less than it was as of June 30, 1976. (The net debt figure takes into consideration the specifically defined reserves that exist under law for payment of some of the outstanding gross debt.)

10. The real estate tax collection rate in 1979 was 94%, up for the third consecutive year.

11. A four-year decline in assessed valuation of taxable real property was reversed.

12. Obsolete accounting procedures and uncoordinated accounting practices have been eliminated; for the second year in a row the City's financial statements, which my
Office prepares, have been certified by independent accounting firms.

In spite of all this, we now know that none of these improvements alone, nor all of them together, will necessarily guarantee full City access to the public credit markets at any early date.

In light of this, what has been our strategy for fiscal year 1980? We have laid out a number of intermediate goals in a drive toward full market re-entry. Let me tell you first about the goals the City has reached:

1. We negotiated a seasonal loan agreement this year with many more banks than last year. Last year, 11 Clearing House Banks and the City's pension funds participated in our standby credit facility. This year, the pension funds (certainly not a traditional money source for tax-exempt securities) were not needed; 12 Clearing House banks joined 28 other City banks, out-of-town banks and banks representing 11 different foreign counties.

2. So far in fiscal year 1980 the City has met its goal of not using this standby $600 million credit facility; we have gone directly to the public for $375 million in two note sales. If conditions stay favorable, we will obtain the remaining $225 million of our short-term needs from the public, rather than from the credit facility--a further indication of growing investor confidence in the City.

3. The City is now in the midst of the largest physical inventory of fixed assets in municipal history. Once the
inventory is complete, a General Fixed Asset Group of Accounts can be established and the City will be able to meet the last remaining requirement of accounting according to GAAP. My Office will complete this requirement in time for inclusion in the City's financial statements for fiscal year 1980—a year earlier than required.

In addition to meeting GAAP requirements, we are also developing an inventory of the City's water distribution and sewage collection systems which will lay the groundwork for future billing and financing decisions in this vital life-support area. As a planning tool, we will establish replacement costs for the City's fixed assets to help in the development of priorities in the City's effort to reconstruct its deteriorating physical plant. The use of replacement cost will enable us to measure our progress or lack of progress in replacing our plant.

On the other hand, I must report on goals we set for this year, but have not yet achieved, largely because of unsettled market conditions. First, the City has not yet secured the rating improvement that we need for our notes. Second, all the City's short-term notes sold to date have been Revenue Anticipation Notes. These RANs are backed by specially set aside state aid revenues. So far, the City has not sold any Tax Anticipation Notes backed only by City real estate tax collections.

Third, the City has still not yet sold notes through competitive bidding by underwriters; thus far, notes have been
sold only through negotiations.

What then are our strategic goals for fiscal year 1981? Obviously, at the very least, to accomplish whatever goals we fail to accomplish this year; they may include competitive bidding by underwriters, TAN sale and a better note rating.

Beyond that, we will seek to improve the standby short-term credit facility—even if we never have to use it—by having more lenders participate and by winning a better deal for the City.

But now, what about long-term bonds? As you know, the City's Four Year Financial Plan requires it to enter the long-term market during fiscal year 1981 and try to sell $300 million of City bonds to the public without a Federal guarantee. One of the reasons Mayor Koch proposes that GAAP budget balance be accelerated from 1982 to 1981 is to hasten the achievement of long-term market re-entry and enhance the likelihood that the 1981 goal of $300 million sold long-term in the public credit markets can be achieved.

One thing is clear: without a GAAP-balanced budget in fiscal year 1981, the City bonds in the $300 million sale planned for that year are not likely to bear an investment grade rating. If the bonds do not carry such a rating, many banks and other institutional investors may not be able to buy them under internal regulations or as a matter of law.

That means the $300 million of bonds will have to be sold to a more speculative class of investor willing to take
a chance on unrated securities. It's hard to say how many such investors there are, and what determines their risk-taking or risk-avoiding posture at any given moment.

Furthermore, in the case of a city seeking to regain investor confidence, one can question the wisdom of the first sale of long-term bonds in six years being labeled risky by independent rating agencies. Maybe speculators would buy them, but how easy would it be to shuck that image the following year when the City must appeal to a different category of investor: one more conservative and less disposed to risk.

Would it promote restoration of New York's credit for its first bond sale in six years to be considered speculative by Moody's or Standard & Poor's? I think not. Would such a rating tend to make it more difficult to broaden the market the following year when more bonds must be sold? I think yes.

There is no question that GAAP balance in 1981, as the Mayor proposes, rather than a year later will improve the City's fiscal position. But will it mean that the $300 million in bonds to be sold next year will assuredly be given an investment grade rating?

We have to answer again--we hope it will, but not necessarily so.
Speaking optimistically, should the credit rating agencies award those bonds an investment grade rating, we have a better chance of selling them to institutional as well as individual investors in fiscal year 1981. This will be an important first step for a City which aspires to the re-establishment of regular market access. On the other hand, many experts feel that investors may want to see GAAP balance in place and working for at least a full year, maybe more, before they put their money in size on the line.

That could mean--on the side of melancholy—that City bonds could not be sold in significant quantity before fiscal year 1982 at the earliest and that the full extent of the $650 million contemplated under the Plan might not be realized.

Should we be optimistic or pessimistic? Without more facts or visible trends, it's hard to say right now and one is left with one's own outlook or attitude.

The optimist could say that the subways are running, the Statue of Liberty is attracting more tourists than ever and the Rockettes are happy. The pessimist could say that the subways are in a hole, the Statue of Liberty is on the rocks and the Rockettes are kicking. Same reality, different viewpoint.
The City has no choice but to be optimistic. Our Financial Plan requires that we try to sell $300 million of bonds in fiscal year 1981 whether GAAP balance is achieved or not, whether the bonds win a good rating or not.

At the moment we are thinking of offering for sale $75 million of bonds in each quarter beginning next July 1. One positive effect of such regularized sales is that the market knows where it stands vis-a-vis the City, investors know the issue will not change in size and other municipal bond issuers, particularly those in New York State, have some flexibility in scheduling their own sales.

Assuming GAAP balance in the next budget, assuming real investor interest in buying City bonds before a second consecutive GAAP-balanced budget is developed and even assuming an investment grade rating for the bonds, we must still consider various contingencies as we prepare to sell City bonds:

1. General market conditions: wild gyrations in the stock, bond, commodities, metals and money markets—no longer an improbable textbook hypothetical—could undermine any of the four proposed issues at any given moment.

2. General municipal market: this particular market could be seriously impacted by bullish or bearish disruptions in the other markets, as well as by certain factors affecting both issuers and purchasers. For example, the fiscal problems of other cities have a probable impact on the saleability of
New York City bonds. Among many urban difficulties, Cleveland, as you know, defaulted; Chicago's fiscal condition is a troubled one and Mayor Byrne flew to New York just last week to seek a favorable bond rating from Moody's and Standard & Poor's. We cannot simply dismiss other cities' problems and say investors will not consider the nation's overall urban crisis when New York City offers its bonds for sale half a year from now.

3. Development of a New York City market: as I noted, no matter how great the City's fiscal progress, investor perception of it may not be favorable enough for the creation of a sizeable market for New York City bonds. This could be affected by many factors, including, for example, the forecast last week by the Wharton Econometric Forecasting Associates that in the coming recession job losses, output of goods and services, retail sales and personal income would all be worse in New York City than in either the region or the nation. Correct or not, the prediction cannot be overlooked as a factor in any contemplated New York City bond sale.

4. The spread between interest rates and the difference in likely maturity schedules of MAC bonds and City bonds: even if all signals are "go" for a City bond sale, the cost differential could be too high a price to pay for the pleasure of entering the long-term market. The City will be sensitive to any differentials between MAC and City bonds and their
implications for the budget.

What will the City do if it fails, for whatever reason, to sell its bonds in fiscal year 1981, or 1982 for that matter, as contemplated by the Financial Plan? As you know, the Plan provides for this contingency, if in fact the City cannot obtain credit in the public credit markets in amounts and on terms sufficient to meet its financing needs: the Plan provides for MAC to take up the slack. If MAC cannot, then the Federal guarantees come into play for sales of City bonds to the pension funds. If even the guarantees are denied to the City, then the City will simply have to reduce its spending for capital purposes.

Of course, there are steps which Congress can take to make it easier for New York City to sell its securities in the public markets:

1. Amend the Bankruptcy Reform Act of 1978 to protect the position and rights of holders of municipal general obligation revenue securities in the event of a bankruptcy.

2. In establishing the new Energy Security Corporation, allow eligible projects sponsored by public entities, as well as private sector firms, to be considered for Federal financing.

3. Develop a final version of the Urban Bank bill that calls for loan guarantees and/or direct loans to businesses located in economically depressed areas; it also provides grants to states and localities for various economic development purposes.
The first step would be of great help to the City in its efforts to sell securities publicly. Senate Bill 658 proposes to amend the Bankruptcy Reform Act of 1978 to protect specifically only the holders of straight revenue bonds and not the holders of general obligation bonds which additionally have defined revenues earmarked for repayment.

The short-term debt recently issued publicly by the City of New York has been in the form of "general obligation" revenue anticipation notes. As provided by State law, the monies earmarked for repayment of these notes are segregated for the benefit of noteholders. However, given the "hybrid" nature of these obligations, they would not be protected by the proposed amendment to the Bankruptcy Act.

Were the City, all of whose debt must by law be general obligation debt, able to represent to prospective lenders that its debt instruments would remain in a protected position in the event of bankruptcy, such a representation would significantly improve the City's ability to market its bonds. Indeed, the amendment we seek would improve materially the ability of all municipalities to meet both their long and short-term financing needs in the public credit markets.

We agree with and support the Public Securities Association, which represents about 280 dealers and dealer banks providing underwriting and financial advisory services to state and local governments, in its call for Federal protections for holders of general obligation revenue bonds.
Congress can help our credit problem in a second way by making cities, as well as private firms, eligible for energy conservation financing through the Energy Security Corporation.

New York City is considering the construction of eight resource recovery plants over the next ten years at a cost of $1.25 billion. An achievement of this magnitude would not only satisfy the City's solid waste disposal needs, but would also produce energy for both heating and the generation of electricity.

As I understand it, as now contemplated, the Energy Security Corporation would not be able to assist the City in building direct waste-to-energy resource recovery plants. Yet, the generation of energy that causes a reduction in the use of oil does not differ from the development of synthetic fuels which the ESC is empowered to assist.

Federal assistance for such projects which obviously fulfil a national need would permit the City either to reduce the amount of money it must try to borrow on its own or to use some of its borrowed money for other urgent capital purposes.

Finally, I hope that the Urban Bank legislation will come out of the Senate-House Conference—the sooner the better—with its two major purposes intact. As the nation slides into
recession, cities need a Federal program that provides loan guarantees and direct loans to businesses located in economically depressed areas and that would permit grants to states and localities for various economic development projects.

It should be clear that any action that improves New York City's economic climate will make it easier for its government to market its notes and bonds.

These are some areas in which Congress can be helpful. But I want to make clear that we are also exploring the possible additional actions we can take on our own to accelerate improvements in the City's fiscal position.

First, the creation of a truly funded Contingency Reserve Fund is under consideration. We will have $25 million to $30 million available in June, 1980 after redemption of bonds in one of the City's Sinking Funds and there will be more redemptions in the future.

As a trustee, I do not intend to allow this money to be "used up" or dribbled away; instead, I have introduced local legislation to place it into a special funded reserve which will have only two uses: reduction of seasonal borrowing needs and financing unexpected deficits which might occur after 1982. Moneys borrowed in this manner will have to be repaid to the Fund.

Second, we are studying the potential issuance by the
City of revenue bonds, particularly in the water distribution and sewage collection areas. As I mentioned before, we are in the midst of a physical inventory of these particular fixed assets. Once the accounting is complete, we will be able to consider an appropriate financing mechanism.

Third, we are studying the feasibility and potential effectiveness of expanding the City's existing General Debt Service Fund (GDSF). As you know, this Fund was established under the Financial Emergency Act on January 1, 1979. It is funded throughout the year by the direct deposit of City real estate tax collections, as well as any additional funds that may be required, and has as its custodian the State Comptroller. Under the law, amounts necessary to pay monthly debt service must be deposited in the GDSF in advance of the month in which the debt service is payable.

We would like to see this General Debt Service Fund expanded to the point where an entire year of debt service, principal and interest, would be funded from the City's first collections of real estate taxes. In this way investors would be reassured at the beginning of each year respecting the availability of cash sufficient to pay all principal and interest payments due at any time during that year. With this kind of protection in place, the City's chances for unrestricted access to the public credit markets should improve significantly. Under the current real estate tax
collection procedures implementation of this concept would exacerbate our seasonal borrowing needs. However, if the Mayor's plan to accelerate real estate tax payments from a quarterly to a semi-annual basis is implemented, beginning in fiscal year 1982 this approach could become feasible.

In conclusion: we continued to make fiscal progress during the past year; we are actively moving to make even further improvements in the City's fiscal position; but unsettling world events and a poor national economic outlook have clouded the City's prospects for re-entering the public credit markets; we are, therefore, planning ahead respecting these additional steps that may be necessary to help us achieve the goals of the City's Financial Plan.

Thank you.

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Mr. Chairman and distinguished members of the Committee: Thank you for providing me this opportunity to express my views regarding New York City's fiscal situation. I join with the Chairman of this Committee and other heads of agencies charged with the responsibility for overseeing the City's financial condition in endorsing the direction avowed by the Mayor in his January 16th financial plan. In my various roles since the fiscal crisis in monitoring the City's fiscal affairs, I have continually stressed the need for the City to avoid delaying difficult budgetary decisions which remain ultimately necessary for the City's successful re-entry into the public credit markets. Among other issues, I have expressed concern beginning with the 1978 expense budget, that the City balance its budgets through the use of recurring revenues on savings, recognize the costs of pensions and an accrual basis institute management reform and more recently improve the capacity to control and direct responsible capital program. The Mayor's most recent Financial Plan began the shift away from the stasis of the 1978, 1979, 1980 Financial Plans and initiated the difficult process of confronting the need to achieve and maintain a budget balanced according to Generally Accepted Accounting Principles. I would like to applaud the Mayor in this effort.
In endorsing the Mayor's strategy, however, I must still express caution and reservation regarding many pieces of the new Plan and the methods by which the City hopes to achieve its goals. With the Mayor's plan to move to a GAAP balanced budget just six months from now, which necessitates closing larger budget gaps in fiscal 1981 than originally planned for, a number of uncertainties remain. The cost of upcoming labor settlements, while impossible to predict, remain a major uncertainty with regard to the City's plan. Labor increases in excess of that which is provided for in the current plan could require additional City actions not yet contemplated. The Health and Hospitals Corporation (HHC) continues to present serious budgetary problems and may require increasing City subsidies unless revenue collection and enhancement programs improve dramatically over current performance. Although the HHC will benefit during the current fiscal year from greater than anticipated State rate increases for Medicaid and possibly substantial rate appeal settlements, a $50 million budget gap in HHC for fiscal 1980 will have to be closed by an allocation from the City's general Reserve Fund. While there have been some small improvements recently in the HHC's baseline revenue collections, expenditures are projected to increase from 1981 through 1983 creating larger gaps to be
closed in those years. A significant portion of the City's plan to reduce future budget deficits in the HHC is contained in the Mayor's plan for Hospital closings and reorganization which must be implemented in the near future in order for the Plan to have the required positive budgetary impact in fiscal 1981 and 1982.

The Board of Education (BE) also continues to cause concern. The new Financial Plan projects expenditure increases for the BE of almost $300 million from fiscal 1980 through 1983. These expenditure increases result largely from State and Federal mandates with regard to the education and transportation of handicapped students. These growing costs are not projected to be offset entirely by intergovernmental aid.

In addition, the plan assumes increasing levels of State and Federal education grants from 1981 to 1983 which must be regarded with uncertainty in the current State Mayor's Plan to eliminate City-wide budget gaps is dependent on large expenditure reductions in the Board of Education ($111 million in 1981) which almost certainly must involve school closings and teacher layoffs. As a semiautonomous agency, the BE is not directly under the Mayor's control and the proposed cuts in the BE budget will, by their nature, be difficult to achieve.
Although the new Financial Plan begins a strategy which includes City-wide expenditure reductions, the City's Program to Eliminate the Gap in 1981 and 1982 includes the need for additional State and Federal actions of $170 million and $410 million respectively. It is becoming increasingly evident that both the State and Federal governments are moving into a period of budgetary retrenchment which may make the City's goals for additional intergovernmental budget balancing aid difficult to achieve. The current Financial Plan makes no provision for additional City actions should this aid fail to materialize.

In order to move to a GAAP balanced budget in 1981, the Mayor has proposed a series of tax increases including a small increase in the property tax, excise tax on beer and liquor, revision of the financial corporation tax, extension of taxes on gasoline and hotels and a rate increase for water and sewer services among others. Most of these proposals will require legislative action and therefore many of them must be regarded as uncertain at this time.

The City's Plan may also be negatively affected by national economic events. Although the City's Plan provides for the impact of a mild recession during 1980, it is possible that this recession may be deeper or more prolonged than anticipated. This situation could cause
a reduction in revenues which could occur in the face of continued inflationary pressure or expenditures.

Another area of concern to me is in the City's management of its capital program. While it is clearly evident that the City's physical plant is rapidly deteriorating, the City has failed to meet its spending targets in the capital program in 1979 and 1980. While the Mayor is correct in pointing out that recreating a viable capital program after three years (1976-1978) of forced inactivity takes time, management improvements in the capital program have lagged those in other areas. The City is not yet at a point where it is meeting its capital needs and there has been a lack of major progress with regard to directing and controlling the capital budgeting and planning process. The ultimate economic viability and habitability of New York City is dependent upon a capacity to plan, finance and execute restoration of its physical plant.

I will continue in my role in assisting the Municipal Assistance Corporation, to monitor these and other areas of the City's fiscal situation with the clear goal of helping to ensure that the Mayor succeeds in a strategy that is on the right road to fiscal health of New York City.
January 28, 1980

Mr. Felix Rohatyn, Chairman
Municipal Assistance Corporation
for the City of New York
2 World Trade Center
New York, N.Y. 10047

Dear Felix:

Enclosed is a statement that I submitted to the U.S. Senate Committee on Banking, Housing and Urban Affairs regarding the financial implications of New York State's proposal to change its budget, accounting and reporting systems.

Best regards.

Sincerely,

Comptroller

Encl.

EVR/goh
STATEMENT BY NEW YORK STATE COMPTROLLER EDWARD V. REGAN SUBMITTED TO THE U.S. SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS, JANUARY 29, 1980

Senator Proxmire and distinguished members of the Committee: this committee has indeed a most important responsibility to gather and assess information on the fiscal affairs of the City of New York and to inquire into the nature of the State's response to the needs of the City. My Special Deputy Comptroller for New York City, Sidney Schwartz, gave you his perspective on the City and as a part of his testimony he has discussed the program of the City to develop a balanced budget in accordance with Generally Accepted Accounting Principles (GAAP). I would like to give you an overview of New York State and our movement to provide for an integrated financial management system also based upon GAAP.

Last December 19, I presented to the Governor, the Legislature, the public and the media, a set of prototype financial statements for New York State prepared in accordance with generally accepted accounting principles for the fiscal year ended March 31, 1979. These statements included a comprehensive fund balance sheet showing the State's financial condition, similar in form to the type of report routinely prepared by a business corporation.

The balance sheet showed that New York State had an accumulated deficit of $2,001,834,000. Essentially, this deficit represents the net difference between the State's operating assets and its short-term operating liabilities at the statement date. Analysis shows that the major liability giving rise to the deficit is some $1.6 billion owed by the State to its school districts for education aid. This lag in payment is routinely paid in the first three months following the close of the State's fiscal year through the proceeds we receive from our annual spring borrowing. The background is that in the first three months of every fiscal year, the State's expenditures far exceed its revenues. In no small part this financial imbalance results from the past practices of "rolling over" payments from one fiscal year to the next. Although we meet our obligations routinely each year, the practice which we employ merely addresses the consequences of the problem without coming to grips with the problem itself.
What the State has been doing is well known to the financial community, members of this committee and others interested in our financial operations. There has been open discussion and adequate disclosure of the whole subject. My predecessor prepared prototype statements for the previous fiscal year and in our most recent Official Statement the $2 billion deficit was acknowledged. Discussion and disclosure is not enough. Therefore, I have called for the State to shift its system of budgeting, accounting and reporting from a cash to an accrual basis and to budget, account for and report the State's financial activity in accordance with Generally Accepted Accounting Principles. I am pleased to report that the Governor in both his State of the State and Budget messages earlier this month endorsed this program and recommended its adoption. The State Senate has previously gone on record in support of accrued accounting and the State Assembly is seriously considering this proposal. Given this support, I see the conversion to GAAP being accomplished within the next two to three years.

Significantly, the Governor in his Executive Budget for 1980-81 proposes important steps to eliminate the accumulated deficit. The budget calls for the expenditure of $47 million to fully accrue new increases in aid to education. A modest beginning, to be sure, but an essential first effort to dispose of the practice of rollovers. Additionally the Governor has asked for $100 million to be included in the 1981-82 budget to begin the gradual acceleration of education aid payments to place these payments on a current basis. The current financing of new payments and an acceleration of the schedule of existing payments will eliminate the $1.6 billion liability or the major component of the deficit in about 16 years.

Like most other states, New York has kept its books on a cash basis. The lack of discipline under the cash basis leads to flexible financial management and historically Governors and legislatures have manipulated the system at will. How one should consider financial requirements became subordinate to how one could meet these requirements. Expenditures and revenues were routinely moved across fiscal years; tax consequences of new spending programs were routinely deferred and fiscal accountability essentially obscured. New York State's past excessive spending program demands and the attendant tax consequences of these programs were rooted in the loose and undisciplined cash accounting system.
Generally Accepted Accounting Principles extended to our budget, accounting and reporting system will alter these ill-conceived spending opportunities. Financial judgements will have to be made in a disciplined environment. The implications of these decisions will have to be measured against reliable and consistent financial reports. Liabilities will be known and recorded, revenues will be measured and their availability assured. In a word fiscal accountability will work side by side with the financial management system.

We are taking this very progressive and far reaching step against a background of both misinformation and lack of information about our State finances. The State's economy and revenue base is now sound and stable, its spending has been running well below the rate of inflation and is now more in line with that of other States--yet a $2 billion accrued, accumulated deficit will now be formally discussed and dealt with. I am concerned that there is a potential for initial negative reaction by the financial community to the more accurate disclosure of this financial information. If this occurred it would be ironic. I have met with the leaders of New York State on this program and I am prepared to meet with the nation's financial communities to explain what we are doing, to answer their questions, and as necessary to correct misimpressions.

What I have discussed here represents a very important set of actions to provide the basis for disciplined fiscal affairs in New York State. Since these actions have the endorsement of State officials, the financial community, the press, and the public, I think it is safe for me to conclude on a note of optimism. The need for fiscal reform by adopting CAAP is evident; there is a clear expression of the will to meet that need. These new initiatives are critical. I am committed to see them through.

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ORAL TESTIMONY PRESENTED BEFORE
THE SENATE COMMITTEE
ON BANKING, HOUSING, AND URBAN AFFAIRS

MONDAY, JANUARY 28, 1980

BY

FREDA STERN ACKERMAN
SENIOR VICE PRESIDENT
MOODY'S INVESTORS SERVICE
My name is Freda Stern Ackerman. I am Senior Vice President and Director of the Municipal Bond Department of Moody's Investors Service, headquartered in New York City.

You have asked for our opinion as to "whether the requirements of the New York City Loan Guarantee Act are being met and to assess what progress New York City is making toward balancing its budget in accordance with generally accepted accounting principles and toward regaining access to the credit markets."

* * * * *
As credit analysts, we look to historical trend data in order to assist us in making evaluations as to future performance. This is an established procedure of credit analysis. Whether governmental administrations change or not, observation of trends in the basic areas of general obligation bond analysis provide the foundation for the credit analyst's judgment. Certainly, more than just trend data are looked to in formulating our assessments, but they constitute the core.

The term trend is commonly defined as the general movement in the course of time of a statistically detectable change. That is exactly the kind of measurement we make as credit analysts and is the kind of performance the City must demonstrate before their numbers become believable.

Ideally, a unit of government is able to demonstrate that it is in a sound condition before the incurrence of debt. Within its current financial structure and using current economic conditions as a guide, a unit should have no difficulty in making projections that show budgetary balance can be maintained, supplemented by positive margins available to deal with possible future adversities. As we all know, however, ideal conditions do not always exist, and we in fact have assigned investment grade ratings to many situations where less than optimum conditions prevail. To keep repeating that New York's case is made unique by many factors including the sheer magnitude of the numbers involved avoids addressing this point. There are numerous other large cities which are experiencing both financial and economic distress, and while New York is surely the largest, many parallels can be seen. Why then, do we and the financial community in general
express so much skepticism about New York while we are able to characterize those other cases as adequate? The basic reason relates to a unit of government's ability to demonstrate control within its limited resources. Indebtedness derives protection by virtue of the municipality's capability to deal with budget problems in a budgetary context. New York City has not yet been able to meet this test. It has not demonstrated an ability to manage its broad scope of operations with all their attendant problems within its resources. Until this is achieved, financial health will remain elusive.

* * * * *
We see the end of the 1981-82 fiscal year as the first real benchmark for a number of reasons. Failure to maximize savings and deficit reduction during the early years of the 1975-79 carry-over period now places the City in the position of having to achieve its required balanced operations by 1982 at the latest, a year when the City will no longer be able to rely on certain past safeguards.

MAC is expected to be near its presently constituted debt limit, debt issuance under the federal guarantee program will have expired, the commitments of the pension funds and Clearing House Banks will have been fully honored, wage settlements will no longer fall under the oversight of the FCB and the inclusion of expense items in the capital budget will no longer be permitted.

Certain remedial measures must be taken in order to provide for substantive and not merely technical reform. Revenues and expenditures must be brought into balance, something not yet realistically accomplished. The continuation of the use of stop-gap measures and one-shot revenues is not acceptable.

There must be demonstrated control over the operations of the covered and mayoral agencies: namely the Board of Education, Transit Authority and Health and Hospitals Corporation.

As yet unresolved are numerous pieces of outstanding litigation against the City which carry the threat of very costly solution. The very composition of the income base of the City is currently precariously tied to the whole question of mandated re-assessments which could
easily cause dramatic shifts in taxpayer components. As a lifetime resident of New York City, I unfortunately can attest to the well documented deterioration which has occurred in the physical plant. Capital needs are enormous and no long term plan of action exists to address this problem.

The relationship between the Municipal Assistance Corporation and the City needs further clarification. MAC has served a useful purpose and has served it well; however, numerous questions are raised as to MAC's scope and longevity. Indefinite perpetuation of the Corporation's powers and debt incurring ability could possibly have a deleterious effect on the formulation of the City's remedial plans. Over and above this, it is not considered a sound principle of public administration to segregate so important a function as capital financing from the body of the government; the loss of control to the unit can have serious ramifications.

Proposed amendments to the Federal Bankruptcy Law (Chapter IX) will, if allowed to remain in their present form, have the undesirable effect of hampering the City's efforts of regaining access to the public credit markets through the sale of general obligation bonds. Another disturbing point relating to Chapter IX remains New York State's willingness to give blanket consent (contained in Title 6-A of the Local Finance Law), without prior approval on a case by case basis, to all its municipalities to file petitions under Chapter IX.
Restoration of creditor confidence in New York City will be a burdensome task. The City's problems go far deeper than accounting practices. The City has disregarded the sound precepts of public administration; it has violated the most elementary rules for maintaining fiscal solvency. Although it has adhered rather well to date to the conditions prescribed by the various fiscal monitors, the long term perspective remains clouded. The magnitude of the problems yet to be addressed and the history of past poor performance must both be included in any calculation of future credibility. One very significant point not to be overlooked is the fact that the City, in the winter of 1975, permitted a default to occur, regardless of the euphemism created to characterize the action. Defaults in the municipal bond industry in the post-war period have been rare occurrences. There are various federal regulations prohibiting bank purchase of securities for a period of years after a default which will curtail potential buyers dramatically. More importantly, the negative psychological impact of a default on private as well as institutional purchasers almost defies quantification. The building and maintaining of confidence can be a tenuous act and one has great difficulty when trying to assess the future state of trust in overlooking or discounting past violations of that trust. For all the words and numbers coming out of the City and all its monitors, there have as yet been few concrete, positive actions taken toward resolving the problems; the one overriding action that was taken, the default on the $2,419,395,000 general obligation tax and revenue anticipation notes, carries a negative connotation that will be a long time in overcoming.
As credit analysts and raters of municipal securities we represent one viewpoint out of many in the marketplace. Our opinion, expressed in the form of ratings and the research we publish, is generally looked to by other market elements in making their judgments as whether to buy or sell a security and at what price. Certainly the Committee is aware that we have no fundamental control over these other judgments; a favorable opinion by a rating agency of an issuer's debt does not necessarily guarantee investor acceptance.

The City of New York has undeniably made progress toward restoring order to its finances. We recognized that progress by revising the rating on its general obligation bonds from Caa, a default level, to B in 1977 and by assigning ratings to the City's note issues. However, recognition of progress should not obscure the fact that the City started out from a position of extreme disorder which has yet to be fully remedied by the City itself. We have spent a large portion of this testimony discussing the importance of analyzing past performance trends in order to make future projections. We have yet to see a clearly definable positive trend for the City. The general rule in financial analysis is that three years of sound, realistically balanced operations can be defined as a trend. We expect the end of fiscal 1981 or 1982, whichever the City chooses, to mark the beginning of that trend which, in the case of an issuer so previously unmindful of the principles of sound administration, would require much longer than the generally accepted rules for it to be adequately characterized. As we stated in our municipal credit report of May 7, 1979, reviewing the City's bond rating:
Although the crisis atmosphere of earlier years has abated, the need for timely and comprehensive City action to cope with existing, fundamental weaknesses is paramount to restoration of credit worthiness. Near term plans now in place do not address structural defects and long range remedial measures have yet to be adopted. The overall credit outlook remains highly uncertain.
TESTIMONY PRESENTED BEFORE
THE SENATE COMMITTEE
ON BANKING, HOUSING, AND URBAN AFFAIRS

MONDAY, JANUARY 28, 1980

BY

FREDA STERN ACKERMAN
SENIOR VICE PRESIDENT
MOODY'S INVESTORS SERVICE
My name is Freda Stern Ackerman. I am Senior Vice President and Director of the Municipal Bond Department of Moody's Investors Service, headquartered in New York City.

You have asked for our opinion as to "whether the requirements of the New York City Loan Guarantee Act are being met and to assess what progress New York City is making toward balancing its budget in accordance with generally accepted accounting principles and toward regaining access to the credit markets."

* * * * *
I.

Before addressing myself to the Committee's inquiry, let me briefly describe to you the perspective from which we view New York City. We are one of the major nationally recognized independent municipal bond rating services. We express our judgments on the credit quality of a municipal bond or note issue with respect to an issuer's ability to meet its obligation. Our judgment is expressed in a credit rating assigned to a bond or note issue. Once a rating is assigned, we continually monitor the credit position and make rating adjustments as called for by changing conditions. The ratings are publicly released and are together with our analytical research disseminated to the subscribers to our various publications.

Our municipal ratings substantially cover the range of securities issued by the States, localities and their political subdivisions. These include revenue bonds and various types of limited obligations as well as general obligation full faith and credit bonds. Analysis of the security for any bond issue begins with the strength of the legal claims, protections and remedies available to the bondholder. General obligation bond analysis, whether for New York City or a small rural school district, additionally requires the fullest understanding of the economic, social, political and financial character of the debt issuer. The issuer's ability to support a given level of public debt and municipal service must be evaluated relative to its overall economic well being. Its fiscal operations are examined in order to evaluate how prudently management is using available resources and how efficiently it is allocating public monies to meet obligations and deliver requisite services. The margins available to meet unaddressed needs and unforeseen potentialities are also
considered. Past performance trends and assessments of current standing form the basis of our projections as to the ability of the issuer to meet its obligation over the life of a bond or note issue.

Moody's has two separate and distinct rating systems for municipal obligations; one for long term bond issues and one for short term note issues. Our bond ratings cover nine grades,\(^1\) ranging from those denoting the highest quality and most secure form of investment, Aaa and Aa, to those denoting highly speculative investments which may in fact be in default, the Caa, Ca and C ratings. The first four ratings, Aaa, Aa, A and Baa, are generally considered to be the investment grade rating categories, a distinction made, not by Moody's definitions, but by the Comptroller of the Currency and the marketplace.

The basic factors considered in assigning a bond rating will vary according to the security elements pledged for repayment of the obligation by the issuer. In general obligation analysis, there are four main areas which are looked at: debt factors, financial factors, governmental factors and economic factors. In revenue bond and limited liability obligations these factors are supplemented by analysis of the legal covenants made to the bondholders to maintain the enterprise or project being financed in good condition, as well as other considerations.\(^2\)

Our note rating system contains four grades\(^3\) and, unlike our bond rating system, considers each rating category to be of investment grade. The Moody's Investment Grade (MIG) ratings are separately defined from bond ratings and include analytical considerations not always found in the assessment of long-term debt. Investors and analysts alike
recognize that two forms of liquidity, that arising from cash flow and that arising from the ability to refinance, underlie the credit position of temporary loans. And, also unlike our bond ratings, each note issue is rated separately regardless of type or security, whereas parity bond issues carry a single rating. 4

As a consequence of our rating processes, we are able to respond to the Committee's questions regarding New York City. We have continued to make our judgments on various City obligations over the period of the fiscal crisis. 5 Moody's currently rates the long-term general obligation bonds of the City B. We have been rating the short-term notes of the City since the inception of our note rating system in 1973 6 and currently rate each short-term revenue anticipation note of the City MIG 3. We also rate the First and Second General Resolution bonds of the Municipal Assistance Corporation for the City of New York (MAC) Baa 1. 7 Additional information relating to the City is reviewed in conjunction with our rating of debt issues of the various State and City construction agencies that involve a pledge of City credit. 8

The information relied upon in our New York City rating and review process is drawn from a variety of City and non-City sources. Offering statements prepared in connection with the City's periodic note and guaranteed bond issuances provide updated disclosure on financial condition and relevant non-financial matters. The City's budgets, budget revisions and financial reports as well as other publications by the City and several of its departments including Finance and the Comptroller's Office are additional City sources of information. We also routinely receive copies of the City's monthly Financial Plan Statements and periodic special reports prepared for the Secretary of the Treasury and copies of the City's submissions to the Financial
Control Board (FCB). Reports commenting on the City's performance made to the City by the Control Board, the Special Deputy Comptroller for New York City and the Board of the Municipal Assistance Corporation are also received. The debt offering statements and annual reports prepared by other issuers associated with the City provide additional perspective. We historically maintain extensive files on the City and collect information from a broad spectrum of organizations reporting on the City. Finally, we have met regularly with City officials and their representatives and continue to maintain open lines of communications.

* * * * *
II.

Our last appearance before this Committee in December 1977 was shortly after the attempt by the City of New York to return to the public municipal note market for the first time since the 1975 fiscal crisis. The City had been a substantial and regular short-term market entrant prior to 1975 and its obligations were then deemed by Moody's to be of investment grade standing. After the beginning of 1975, Moody's did not have ratings assigned to any short-term obligations of the City.

In November 1977 the City offered publicly, $200,000,000 (approximate) Revenue Anticipation Notes, 1977 Series A, B, C and applied to Moody's for a Moody's Investment Grade (MIG) rating. At that time we looked for security almost solely to the amendments enacted by the State Legislature, effective October 26, 1977, to the Local Finance Law and the State Finance Law. Their provision for the payment of the notes from state education aid due the City and for the transfer of that aid directly from the State Comptroller to the paying agent of the noteholders gave us comfort in their structure and likely application and were cited as bridging the gap from a non-investment grade to a note rating. We found few other security elements. Not only were there some uncertainties concerning the State and the availability of the State education aid pledged, but many areas remained unclarified concerning the issuer, New York City, itself.

Uncertainty detracted from the quality of the obligation. Not only was Title 6-A of the Local Finance Law, under which the City had previously declared a moratorium on its debt, still in effect but also the City faced a number of immediate pressures. The following were drawing to a close: the three year emergency period; the Federal
Seasonal Loan Program; the municipal pension funds' commitment to purchase city bonds; and, the Emergency Financial Control Board. Additionally, union contract negotiations and settlements had not been budgeted for, there were uncertainties as to Municipal Assistance Corporation borrowing authorizations and its continued effectiveness in providing financing, and, most importantly, financial operations of the City continued unbalanced and were projected to deteriorate further. We assigned our lowest note rating, MIG 4, to the proposed offering. The notes were not sold.

The emergency period, which enabled the City to continue operations following the 1975 crisis, ended on June 30, 1978. Steps taken during 1978, to carry the City beyond the emergency period, were the foundation of the current four year recovery program. To regain fiscal stability and correct past deficiencies the City chose to pursue a strategy of gradual phase-in of sound operating practices and necessary austerity measures largely within the context of its existing administrative and budgetary structure. The goal was to restore a balanced operation and regain financing independence at the end of the four year period, June 30, 1982. To ensure that necessary steps were taken to achieve the goals, the City had to meet certain interim requirements including a specified phase-out of its inclusion of operating expenses in its capital budget. Monitoring functions and reporting requirements were put into place to review the City's compliance with specific requirements and to evaluate its ongoing performance relative to the June 30, 1982 goals.

The Financial Emergency Act was amended in June and September of 1978. Under the amendments the control period was extended from its original June 30, 1978 expiration to an indefinite period defined relative to the achievement of recovery goals and to the retirement
of debt issued under the Act's protections. Other provisions of the amendments expanded the review and oversight powers of the Control Board during as well as after the control period, provided for the establishment of a Debt Service Fund, authorized the City's inclusion of a covenant of the State on any loan agreements dated prior to July 1, 1983 and mandated balanced budgets in conformity with generally accepted accounting principles.

To permit the City to obtain short and long term financing needed during the recovery period, additional legislative and administrative measures were enacted in 1978. Those provisions of Title 6-A of the State's Local Finance Law under which the City had declared the 1975 moratorium were repealed. The Debt Service Fund mechanism was defined, to be financed from real property taxes, and providing for the payment of principal and interest on city debt through separately established accounts maintained and administered by the State Comptroller. The Municipal Assistance Corporation's debt issuing capacity was raised, in stages, to its current $8.8 billion authorization. Finally, the Federal Seasonal Financing Act which expired June 30, 1978 was replaced in August 1978 by the New York City Loan Guarantee Act providing for the issuance of up to $1.65 billion of guaranteed long term bonds through June 30, 1982. Within this framework the City has been able to adequately fulfill its financing requirements.

Seasonal cash flow needs have been met for the last two years from a combination of public note offerings and notes issued privately under loan agreements with local financial institutions. For the benefit of the Committee, I shall briefly describe the City's short-term financings during the last two years.

The City of New York successfully returned to the public credit market in January 1979 with the sale of $125,000,000 General Obligation
Revenue Anticipation Notes, 1979 Series C. Moody's assigned a MIG 3 rating to this issue based upon the quality of the legal mechanism to assure note repayment, the reliability of pledged revenues, and the more clearly defined and effectively managed cash flow combined with the presence of the financing agreement that assured a source for City's cash flow requirements. At that time, we also cited the chronic financial weakness of the issuer which still created an overall climate of uncertainty.

In accordance with its projected cash flow requirements, the City of New York returned to the public credit markets a month later in late February 1979. General Obligation Revenue Anticipation Notes 1979 Series D, were for a principal amount of $150,000,000 and were issued against the same categories of State aid and revenues due the City as were the Series C Notes sold publicly in January 1979 and the Series A and B Notes sold pursuant to the 1978-79 Loan Agreement with financial institutions. Moody's assigned a MIG 3 rating to the issue for the same reasons as cited above.

After the sale of the Series D Notes, the City did not issue any additional notes to the public during its 1978-79 fiscal year. Further issuance under the Loan Agreement was expected and required, resulting in aggregate seasonal borrowing for the 1978-79 fiscal year of $650,000,000, all of which was paid as due.

The first public note borrowing for the 1979-80 fiscal year was undertaken by the City in September 1979 when $200,000,000 General Obligation Revenue Anticipation Notes Fiscal 1980 Series A were offered. The essential legal mechanism for these notes was again the same. Moody's analysis and MIG 3 rating of the Series A Notes, as with previous separately secured offerings in the prior year, took account of the reliability of pledged revenues, quality of the
mechanism to assure payment of the notes, and overall credit condition of the issuer.

Most recently, in December 1979, the City, as expected, returned to the public credit market with the sale of $175,000,000 General Obligation Revenue Anticipation Notes Fiscal 1980 Series B. This sale was the second offering for the 1979-80 fiscal year. The security of the Series B Notes was identical to the $200,000,000 Series A Notes sold in September, 1979. These notes were also rated MIG 3.

Based upon the City's most recently submitted cash flow statements, additional seasonal borrowing is anticipated during the balance of 1979-80 to bring financings to a total of $600,000,000.

Long term financing needs during the City's recovery period have been provided for under the Four Year Debt Issuance Plan running through June 30, 1982. Components of the plan include non-public market financings through the sale of up to $1.8 billion Municipal Assistance Corporation bonds under purchase commitments by the various New York City financial institutions and four municipal pension funds and the sale of up to $750 million federally guaranteed city bonds under separate purchase commitments with city and certain state pension funds. The plan additionally calls for accessing the public credit markets through the sale of up to $1 billion Municipal Assistance Corporation bonds and in the final two years of the plan, the sale of up to $950 million non-guaranteed city bonds. The plan is completed by available debt authorization for the issuance of MAC bonds in the event that the City cannot sell its bonds and the back-up capability of issuing $900 million federally guaranteed bonds to the pension funds if the MAC bonds cannot be sold. To date, approximately $2.44 billion of the total $4.5 billion plan has been accomplished including MAC's public sales of $847 million bonds.
While the City of New York has since 1975 only been able to issue publicly its own short term debt, MAC has been able to sell publicly long term bonds and has become an accepted market entrant. MAC continues its role in helping to provide an orderly stream of revenues to assist the City in meeting its required expenses and also as another oversight vehicle monitoring the City's financial progress. The Corporation presently has outstanding, separately secured First General Resolution Bonds and Second General Resolution Bonds in the aggregate principal amount of roundly $6.7 billion.

Bonds issued under the First General Bond Resolution are general obligations of the Corporation payable out of any revenues and are entitled to a first lien created by the pledge under the Resolution of all monies and securities paid into the Debt Service Fund and Capital Reserve Fund held by the Trustee. Bonds issued under the Second General Bond Resolution are general obligations of the Corporation payable out of any available revenues of the Corporation not otherwise pledged. The bonds are entitled to a lien created by the pledge under the Second General Bond Resolution of all monies and securities paid into the Bond Service Fund and Capital Reserve Aid Fund held by the Trustee. First Resolution obligations have a claim prior to that of Second Resolution obligations on all amounts available to the Corporation from the 4% sales tax imposed in the City by the State and the stock transfer tax imposed upon sales and other security transactions made within the State. First Resolution obligations have no claim however, on per capita state aid, which is a principal source of payment for the Second Resolution Bonds.

The security afforded the First General Resolution Bonds and Second General Resolution Bonds of the Corporation rests primarily on the strength inherent in the stream of pledged revenues. Sufficiency
of revenues is currently adequate. Per capita aid has held constant at the state ceiling while sales and compensating use taxes and the stock transfer tax have grown. Requirements for additional bonds and the Corporation's overall debt limit will control the requirements placed upon the pledged revenues. Additionally, there appears to be little likelihood of an interruption or other impairment of the revenue stream to the Corporation. All bonds of the Corporation are currently rated Baa1.

Paralleling the immediate and long term objectives of the Four Year Debt Issuance Plan are the efforts to implement the provisions of the Four Year Financial Plan. The Financial Plan provides an orderly basis for ongoing operations during a period in which the City is required to take steps necessary to balance its annual operations in accordance with Generally Accepted Accounting Principles (GAAP) for the fiscal year ending June 30, 1982 and thereafter. For each year during the recovery period, the City must submit to the Control Board an annual operating budget balanced in accordance with the Financial Plan and a revised financial plan covering the ensuing three years. The Control Board also receives for its review and approval subsequent modifications to the current budget and a program to eliminate the budget gaps in the ensuing three years of the plan.

The City's most recently completed fiscal year closed on June 30, 1979. For the second consecutive year the financial statements for the City's General, Capital Projects and Debt Service Funds and its Statement of Long-term Obligations have been independently audited. The statements for the General Fund were again prepared both in accordance with GAAP and in accordance with the Financial Plan sanctioned by various state legislative acts which permit certain transactions
contrary to GAAP. The difference in these reporting approaches primarily reflects the Plan's sanction of capitalized operating expenses on a phased-out basis and the provision for pension costs on a cash basis and not on an accrual basis. Operating results for the year ending June 30, 1979 provided a General Fund excess of revenues over expenditures, encumbrances and transfers of $216.1 million on a Plan basis and a deficit of $422.3 million on GAAP basis. Comparable figures for 1978 were a $32.0 million Plan surplus and a $712.1 million GAAP deficit.
I.

As credit analysts, we look to historical trend data in order to assist us in making evaluations as to future performance. This is an established procedure of credit analysis. Whether governmental administrations change or not, observation of trends in the basic areas of general obligation bond analysis provide the foundation for the credit analyst's judgment. Certainly, more than just trend data are looked to in formulating our assessments, but they constitute the core. They are supplemented by other types of data: current economic statistics; projections of tax base growth; capital plans and, of course, budgets. But, especially in the financial area, projections, in the form of budgets, become more meaningful when past experience lends credibility.

One year of positive results does not constitute a trend; it may be the beginning of a trend. The term trend is commonly defined as the general movement in the course of time of a statistically detectable change. That is exactly the kind of measurement we make as credit analysts and is the kind of performance the City must demonstrate before their numbers become believeable.

Ideally, a unit of government is able to demonstrate that it is in a sound condition before the incurrence of debt. Within its current financial structure and using current economic conditions as a guide, a unit should have no difficulty in making projections that show budgetary balance can be maintained, supplemented by positive margins available to deal with possible future adversities. As we all know, however, ideal conditions do not always exist, and we in fact have assigned investment grade ratings to many situations where less than optimum conditions prevail. To keep repeating that New York's case is made unique by many factors including the sheer magnitude of the numbers
involved avoids addressing this point. There are numerous other large cities which are experiencing both financial and economic distress, and while New York is surely the largest, many parallels can be seen. Why then, do we and the financial community in general express so much skepticism about New York while we are able to characterize those other cases as adequate? The basic reason relates to a unit of government's ability to demonstrate control within its limited resources. Indebtedness derives protection by virtue of the municipality's capability to deal with budget problems in a budgetary context. New York City has not yet been able to meet this test. It has not demonstrated an ability to manage its broad scope of operations with all their attendant problems within its resources. Until this is achieved, financial health will remain elusive.

* * * * *
II.

A firm assessment of the City's ultimate fiscal health is not possible at this time. Progress to date has been more of a technical nature while substantive issues have not been fully addressed. The intermediate tests between now and 1982 are not as stringent as those beyond 1982.

Legislative measures and agreements with private and public institutions now in place have enabled the City to survive the turbulent period which began in 1975 when questionable financial and legislative maneuvers were commonplace. Although the City has been made aware of the invalidity of some of the former practices under which it sought recourse before and during the fiscal crisis, basic structural weaknesses in the overall credit outlook persist. Because of the lack of any meaningful long term remedial measures, there still exists the potential for a return to the conditions of high susceptibility prevailing in earlier years.

The prospect for establishing a recurring budgetary balance by June 30, 1982, or the June 30, 1981 target date Mayor Koch announced on January 17, 1980, is far from certain. Prior to the Mayor's most recent Financial Plan submission which is yet to be approved by the FCB, the 1980 budget is estimated to contain a $451 million GAAP deficit and the GAAP deficits projected for 1981 through 1983 are $742 million, $830 million and $854 million, respectively. The City's capital program has resumed but the City has neither geared up sufficiently to keep pace with the $2.3 billion proposed to be spent during the Four Year Plan nor has it detailed or updated the $12 billion 10-year capital plan that had been proposed in 1978. The most recent four-year plan submissions have an allowance for the Spring 1980 labor contract settlements of only roughly 4%. 
The City continues to look to declining school enrollments as a basis for education related budget cuts; however, in the current year, the Board of Education's spending pattern required mid-budget remedial actions to cover $75 million of projected over-spending. The subsidy levels to covered organizations are also viewed as possible targets for cutbacks. The 1980 Transit Authority subsidy was reduced by $60 million to $210 million but gaps in transit budgets are projected at $6.8 million, $103.6 million, $129.2 million and $151.2 million, respectively for 1980 through 1983. The Health and Hospitals Corporation's budget has proven even more difficult to control. Reduction of the net City general and Medicaid subsidy by $50 million to $369.8 million leaves a projected gap of $63 million for 1980 and gaps of $146.2 million, $153.2 million and $183.2 million for 1981 through 1983 respectively.

Recognized economic weaknesses include a high degree of cyclical vulnerability and continuing property and population base erosion. Continuing to rise are the fixed costs for pension and debt servicing including amortization of accumulated deficits funded by MAC. This constitutes a drain on current resources because revenues are derived from within the City's operating tax rate limit. To close the remaining budgetary gaps the City is relying upon the provision of substantial additional amounts of federal and state aid and upon its own ability to reduce the scope of City services. These plans are made in a climate of spending restraint for federal and state governments and continued demands by public employees and service recipients, but nevertheless must be carried out with a sense of urgency.
While the New York City Loan Guarantee Act specified certain conditions with which the City is to comply prior to June 30, 1982, and while it appears that the City has complied with these requirements to date, performance during the period beginning July 1, 1982 will hold the key to restoration of confidence.

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III.

We see the end of the 1981-82 fiscal year as the first real benchmark for a number of reasons. Failure to maximize savings and deficit reduction during the early years of the 1975-79 carryover period now places the City in the position of having to achieve its required balanced operations by 1982 at the latest, a year when the City will no longer be able to rely on certain past safeguards.

MAC is expected to be near its presently constituted debt limit, debt issuance under the federal guarantee program will have expired, the commitments of the pension funds and Clearing House Banks will have been fully honored, wage settlements will no longer fall under the oversight of the FCB and the inclusion of expense items in the capital budget will no longer be permitted.

Certain remedial measures must be taken in order to provide for substantive and not merely technical reform. Revenues and expenditures must be brought into balance, something not yet realistically accomplished. After having achieved this step, of having resources in the form of revenues at least equal to current expense items, hopefully with some margin of protection set aside for contingencies, the City must be able to show it can operate on a day-to-day and year-to-year basis in this manner. When and if balance is achieved, we would then look to see whether anticipated revenues appear to be of a recurring nature and as such are realistic and whether they are adequate to provide for mandated as well as potentially unanticipated expenditures. The continuation of the use of stop-gap measures and one-shot revenues is not acceptable.

Concerns abound about the likelihood of more severe recessionary conditions and increased inflation. Obviously, these two economic conditions have a profound effect on revenues, especially in a situation
were you are not starting out with a growth or even a stable economic
and employment base.

There must be demonstrated control over the operations of the
covered and mayoral agencies: an ability to contain the operations of
the Board of Education within its budget; more accurate and clearly
documented appraisals of target subsidy levels to the Transit Authority
and Health and Hospitals Corporation; demonstrated availability of
contingency reserves in the City's own budget to cover unexpected
additions to these subsidies; and, documented control measures and
revenue sources to enable the City to deal with unexpected additions
to these subsidies.

As yet unresolved are numerous pieces of outstanding litigation
against the City which carry the threat of very costly solution including
several challenges concerning inequality of property taxation. The
very composition of the income base of the City is currently precariously
tied to the whole question of mandated re-assessments which could easily
cause dramatic shifts in taxpayer components. As a lifetime resident
of New York City, I unfortunately can attest to the well documented
deterioration which has occurred in the physical plant. Capital needs
are enormous and no long term plan of action exists to address this
problem.

The relationship between the Municipal Assistance Corporation and
the City needs further clarification. Equally important to the evalua-
tion of each entity separately is a clear definition of their future
functions. MAC has served a useful purpose and has served it well.
The intent in the formation of MAC was that it perform the role of a monitor and also of a borrower on behalf of the City; the latter role to be transitional in nature, to provide financing for the City during the period in which the City could not borrow on its own. Because the prospect of the City's meeting the totality of its capital requirements on its own is uncertain at this time, numerous questions are raised as to MAC's scope and longevity. The steps to be taken by the City in restoring fiscal health can be greatly influenced by the existence of MAC. Indefinite perpetuation of the Corporation's powers and debt incurring ability could possibly have a deleterious effect on the formulation of the City's remedial plans. Over and above this, it is not considered a sound principle of public administration to segregate so important a function as capital financing from the body of the government; the loss of control to the unit can have serious ramifications.

Proposed amendments to the Federal Bankruptcy Law (Chapter IX) will, if allowed to remain in their present form, have the undesirable effect of hampering the City's efforts of regaining access to the public credit markets through the sale of general obligation bonds. They create a secured class of debtor for a revenue bond holder while placing the holders of faith and credit municipal debt in a weakened position in the event of a filing under Chapter IX by the issuer. The potential negative impact on New York City derives from the fact that in the State of New York, all municipal issuers are required by the State Constitution to pledge their faith and credit to their debt obligations. Another disturbing point relating to Chapter IX remains New York State's willingness to give blanket consent (contained in Title 6-A of the
Local Finance Law), without prior approval on a case by case basis, to all its municipalities to file petitions under Chapter IX. Either the FCB or the City administration may file for a City bankruptcy without specific approval by the State.
IV.

Restoration of creditor confidence in New York City will be a burdensome task. The City's problems go far deeper than accounting practices. The City has disregarded the sound precepts of public administration; it has violated the most elementary rules for maintaining fiscal solvency. Although it has adhered rather well to date to the conditions proscribed by the various fiscal monitors, the long term perspective remains clouded. The magnitude of the problems yet to be addressed and the history of past poor performance must both be included in any calculation of future credibility. One very significant point not to be overlooked is the fact that the City, in the winter of 1975, permitted a default to occur, regardless of the euphemism created to characterize the action. Defaults in the municipal bond industry in the post-war period have been rare occurrences. There are various federal regulations prohibiting bank purchase of securities for a period of years after a default which will curtail potential buyers dramatically. More importantly, the negative psychological impact of a default on private as well as institutional purchasers almost defies quantification. The building and maintaining of confidence can be a tenuous act and one has great difficulty when trying to assess the future state of trust in overlooking or discounting past violations of that trust. For all the words and numbers coming out of the City and all its monitors, there have as yet been few concrete, positive actions taken toward resolving the problems; the one over-riding action that was taken, the default on the $2,419,395,000 general obligation tax and revenue anticipation notes, carries a negative connotation that will be a long time in overcoming.

As credit analysts and raters of municipal securities we represent one viewpoint out of many in the marketplace. Our opinion, expressed
in the form of ratings and the research we publish are generally
looked to by other market elements in making their judgments as
whether to buy or sell a security and at what price. Certainly
the Committee is aware that we have no fundamental control over
these other judgments; a favorable opinion by a rating agency of
an issuer's debt does not necessarily guarantee investor acceptance.

The City of New York has undeniably made progress toward restoring
order to its finances. We recognized that progress by revising the rating
on its general obligation bonds from Caa, a default level, to B in
1977 and by assigning ratings to the City's note issues. However,
recognition of progress should not obscure the fact that the City
started out from a position of extreme disorder which has yet to
be fully remedied by the City itself. We have spent a large portion
of this testimony discussing the importance of analyzing past perform-
ance trends in order to make future projections. We have yet to see
a clearly definable positive trend for the city. The general rule in
financial analysis is that three years of sound, realistically balanced
operations can be defined as a trend. We expect the end of fiscal 1981
or 1982, whichever the City choses, to mark the beginning of that
trend which, in the case of an issuer so previously unmindful of the
principles of sound administration, would require much longer than the
generally accepted rules for it to be adequately characterized. As
we stated in our municipal credit report of May 7, 1979, reviewing the
City's bond rating:

Although the crisis atmosphere of earlier years has
abated, the need for timely and comprehensive City
action to cope with existing, fundamental weaknesses
is paramount to restoration of credit worthiness. Near term plans now in place do not address structural defects and long range remedial measures have yet to be adopted. The overall credit outlook remains highly uncertain.

* * * * *
1Bond rating definitions.

Aaa

Bonds which are rated Aaa are judged to be of the best quality. They carry the smallest degree of investment risk and are generally referred to as "gilt edge." Interest payments are protected by a large or by an exceptionally stable margin and principal is secure. While the various protective elements are likely to change, such changes as can be visualized are most unlikely to impair the fundamentally strong position of such issues.

Aa

Bonds which are rated Aa are judged to be of high quality by all standards. Together with the Aaa group they comprise what are generally known as high grade bonds. They are rated lower than the best bonds because margins of protection may be of greater amplitude or there may be other elements present which make the long-term risks appear somewhat larger than in Aaa securities.

A

Bonds which are rated A possess many favorable investment attributes and are to be considered as upper medium grade obligations. Factors giving security to principal and interest are considered adequate, but elements may be present which suggest a susceptibility to impairment sometime in the future.

Baa

Bonds which are rated Baa are considered as medium grade obligations, i.e., they are neither highly protected nor poorly secured. Interest payments and principal security appear adequate for the present but certain protective elements may be lacking or may be characteristically unreliable over any great length of time. Such bonds lack outstanding investment characteristics and in fact have speculative characteristics as well.

Ba

Bonds which are rated Ba are judged to have speculative elements; their future cannot be considered as well-assured. Often the protection of interest and principal payments may be very moderate, and thereby not well safeguarded during both good and bad times over the future. Uncertainty of position characterizes bonds in this class.

B

Bonds which are rated B generally lack characteristics of the desirable investment. Assurance of interest and principal payments or of maintenance of other terms of the contract over any long period of time may be small.
Caa

Bonds which are rated Caa are of poor standing. Such issues may be in default or there may be present elements of danger with respect to principal or interest.

Ca

Bonds which are rated Ca represent obligations which are speculative in a high degree. Such issues are often in default or have other marked shortcomings.

C

Bonds which are rated C are the lowest rated class of bonds, and issues so rated can be regarded as having extremely poor prospects of ever attaining any real investment standing.

Con. (...) 

Bonds for which the security depends upon the completion of some act or the fulfillment of some condition are rated conditionally. These are bonds secured by (a) earnings of projects under construction, (b) earnings of projects unseasoned in operating experience, (c) rentals which begin when facilities are completed, or (d) payments to which some other limiting condition attaches. Parenthetical rating denotes probable credit stature upon completion of construction or elimination of basis of condition.

Those bonds in the A and Baa groups which Moody's believes possess the strongest investment attributes are designated by the symbols A_l and Baa_l.
Bond Rating Criteria.

A municipal bond rating is a judgment of the investment quality of a long term obligation issued by a state or one of its subdivisions. It is based on an analysis that must ask, first, what has the debtor pledged to pay and, second, what is the likelihood that he will be able to keep his promises.

The rating is the essence of an analysis and is a shorthand statement of the judgment which is reached. It is a statement about the debtor's condition and the probability that he can and will do what he says regarding the debt. It is an evaluative assessment of the protections afforded the bondholder. The rating is a simple, easy-to-understand classification of the credit risks of a municipal bond. It is a judgment which the market finds to be useful in making comparisons and in maintaining liquidity of capital funds.

The first question asked in the analysis leading to the rating is what has the debtor pledged to pay. Because of the public nature of the issuer, true mortgages and the usual physical security associated with other long term debt instruments will be lacking. Aside from pledges concerning time, amount, and mechanics of payment, the central question is what will the debtor pay the obligation from. The answer determines the questions which will be asked to the analysis, and there are several broad categories of pledges. These are as follows:

(1) The general obligation pledge in which the borrower pledges his full faith and credit and unlimited taxing power. This is the broadest form of analysis. The most general. The traditional.

(2) The limited pledge involving a single tax or a specific governmental revenue. A variant of the special fund doctrine, the limited tax pledge involves use of a governmental power -- the power to tax.

(3) The enterprise or quasi-enterprise revenue pledge. Another variant of the special fund doctrine, this produces the true revenue bond, and the analysis leans heavily on long-standing corporate experience.

(4) The lease pledge whereby funds derive immediately from resources other than those of the issuer but in which the issuer does something to justify payments which include debt service.

(5) A pledge of resources of another government.

There are, of course, variations and combinations of these pledges. Aside from the general obligation pledge, the others, limited and indirect, have been inspired by the legal and constitutional limitations placed on debt usage over the last 130 years.

Having determined the pledge, the analyst examines the credit. Generally the credit aspect of bond security analysis seeks to appraise future performance in terms of debt service requirements. For these purposes, the debt commitment of a municipal issuer is compared with the pledged resources, and both factors are measured on a current
basis and projected into the future. Expressed as a ratio of debt to wealth, this measure may be compared as between situations and with empirical evidence from the past. The likelihood of converting pledged wealth into sustainable annual future income must be separately appraised to validate the equation, and protection that may be established against the uncertain future must be evaluated.

In General Obligation Bond Analysis

In general obligation bond analysis a great number of variables present themselves, but generally they may be subsumed under four heads: debt, financial, governmental, and economic.

Debt analysis:

1. Debt policy: the uses, purposes, and planning of debt issuance, as well as the type instruments used.

2. Debt structure: adequacy of plans for debt retirement - the relation between rate of retirement and purpose of debt, resources of the community, and existing and future debt needs.

3. Debt burden: gross and net debt related to resources and a comparison with other communities - overlapping debt and pyramiding.

4. Debt history and trend: the record as to defaults, refunding of maturing bonds and funding of operating deficits - rapidity of debt growth relative to purposes for which it has been incurred.

5. Prospective borrowing: authorized and unissued bonds - adequacy of capital programming - obsolescence or inadequacy of capital plant - existing debt structure.

Financial analysis

6. The current account: the year-end relation of current liabilities to available cash - promptness in disposing of casual deficits - devices to keep deficits from accumulating - if accounting is revenue accrual, the adequacy of reserves for uncollectible accounts - the liquidity of current account cash and uncollected taxes should equal demand liabilities outstanding.

7. Revenue system: adequacy of property tax base - trend of assessed value, equalization ratio, levy, and collections - other components of revenue system -- source, base, rates, yields - diversity, cyclical stability and adequacy of aid from other governments.


10. Financial administration: assessment practices - tax collection procedures - enforcement procedures - financial planning as evidenced by budgeting, reporting, services.

Government


13. Services: provision for essential services to perpetuate economic base.

14. Intergovernmental factors: the pyramid of governmental units, conflicts and duplications - complementarity - other units which drain off resources or impede planning.

15. Administrative performance: conscientious administrators who promote confidence through standing and experience - availability of audits, budgets, annual reports, capital planning documents, land use plans.

Economic

16. Identity and natural resources: geographic and locational advantages - natural catastrophe - natural resources - size and land use characteristics.

17. Population, wealth and labor factor: population characteristics - wealth level (family income and per capita full value) - housing characteristics - new construction values.

18. Economic structure and capital: types of employment, industry and occupation - major employers - relation to SMSA - evidences of industrial decline or population shifts - transportation and its relation to the economic structure.


The analysis of debt

The analyst is concerned with the total impact of all debt obligations on the reasonable ability of the taxpayers of the issuing unit to meet them. To this end, his central and first task is to derive a measure of the debt burden. In simplest terms, this is the relationship between the total debt burden on the tax base in the governmental unit and the wealth located there. Total debt includes not only the debt obligations issued by the subject government, which is the gross debt, but also the proportionate share of the debt obligations of overlapping governmental units on the taxpayers of the subject unit. Thus, the gross bonded debt of a city is adjusted to net by subtracting obligations accounted for by self-supporting (non-tax) utility operations, and to the net figure is added a proportionate share of any county, school district, or other local governmental debt payable from the same tax base. It is this burden which the taxpayers of the city are confronted with and which is generally designated as the overall net debt.
The overall net debt is related to the broadest and most generally available measure of the wealth of the community, which is the assessed valuation of all taxable property adjusted to reflect market value as nearly as possible. The adjustment is made through application of an equalization ratio, which generally reflects a state government's appraisal of local assessment practices and which is widely necessitated by grants-in-aid which require measures of local wealth. Empirical evidence indicates that there is good reason to expect difficulty in meeting debt obligations when the debt burden exceeds the 12% range and when an exogenous factor, such as an economic recession, comes into play.

The analyst also examines the structure of the debt, and how the issuer plans to pay it out. Unnecessary deferral of debt payment raises questions, and as a general rule the analyst prefers payment to be reasonably related to the life of the improvement the debt is used to finance. The payment of half the debt of a community over the ensuing ten years is generally recognized as prudent, accounting theoretically at least for some depreciation as well as maintaining capacity to borrow in the future. Another aspect of debt structure analysis seeks to determine irregularities and any special problems which might be incurred in meeting them.

Further checks in the analyst's appraisal of the debt of a community include examining its debt history for past mistakes and what has been done to prevent their recurrence; the uses the community makes of debt and how it plans debt incurrence related both to need and resources; and the necessity of future borrowing by the community. The latter factor is of utmost importance. It involves an assessment of a city's capital plant relative to its position in history. For a deteriorating, older city or for a rapidly growing, newer city, future borrowing policy dictates particular and careful planning. As he turns to other factors in the analysis, the analyst must bear in mind the possible future debt policies of the borrowing unit.

Financial analysis

An examination of the financial operations of the community for the latest period available serves to confirm its performance under existing conditions. To relate debt to economic resources only sets the problem. The translation of resources into revenues to pay expenses, including debt service, requires periodic and constant examination of the issuer's audited accounts. A singularly difficult aspect of municipal security analysis, as opposed to corporate analysis, is the general lack of standardization of accounting and reporting procedures, particularly among smaller units.

The analysis of the revenue system involves determination of the reliance on the property tax, the trend of assessed valuation and tax delinquencies, in addition to the diversification of the revenue structure. Expenditures should be analyzed to ascertain the relation of debt service payments to total current expenses as well as the vulnerability of the unit to mandated expenditures, which could create financial problems for it. Of particular importance is the sensitivity of the revenue and expenditure structures to cyclical fluctuation, and the record of tax delinquencies may be particularly useful as a tool in the determination of local cyclical sensitivity. The issuer's budgets require examination as a forecast, as well as the adequacy of the financial planning and management. Assessment practices, tax
collection procedures, and methods of enforcement may require examination, as the analyst attempts to determine the ability of the management of the unit to convert resources into tax receipts which are adequate for all its purposes.

The analyst will examine the audited accounts of the unit to determine the year-end relation of current liabilities to available cash. The unit's promptness is disposing of casual deficits, as well as devices to keep deficits from accumulating, should be determined, as should the liquidity of current account cash and uncollected taxes relative to demand liabilities outstanding. A prime concern of the analyst is that the current account be maintained soundly, because often in the past difficulty with debt service has been signalled first by current account difficulties, particularly when steps are not taken immediately to correct such troubles before they spread to longer term obligations.

Government analysis

In this endeavor, the analyst will seek to determine how well organized the governmental unit is to perform its functions and how well staffed and administered it is to carry out those functions. A major concern is that services are provided which will perpetuate a liveable community. Knowledge of the professionalism of government, as well as the traditions of the community in its governmental affairs, will help considerably, although the projection of these factors into the future may be tenuous and the element of subjectivity must be guarded against consciously. Intergovernmental relations constitute an important segment of this analysis in determining the cooperation and competition among and between this and other units, the relations with the state government—particularly in finance—and the actions of other units which may drain off resources of the subject unit. A major aspect of government analysis is the availability of adequate financial documents, annual reports, and meaningful capital planning devices and records.

Economic analysis

As the debt of the unit measures the problem the analyst is solving regarding any particular governmental unit, the economic background and analysis largely measures the dimensions of the solution to the problem. As in any form of security analysis, the future is of more importance that the past or present, so the analyst is concerned that he properly project what he can measure now against what will happen in the future. Briefly, the economic analysis of a borrowing unit should reveal the characteristics of any time series analysis; the secular, cyclical, seasonal, and random trends applicable to the unit involved.

The economic geography, the locational advantages, and the land use characteristics of the borrower need to be determined as a matter of identification. The degree to which a particular unit is subject to natural catastrophe may be enough to rule out some bonds as far as some investors are concerned. Earthquakes, for example, are not yet predictable occurrences, although they are more predictable in some areas than others; where they are, the analyst and the investor should at least recognize this factor before rather than after the event. The natural setting of the unit may provide clues as to its future development.
As a reinforcement of the knowledge gained through assessed valuation of taxable property, the analyst will seek out other measures of the wealth of the community. These include population characteristics, the level of income of families and individuals, and the market valuation per capita of the unit. Housing characteristics as measured by age of housing, value of owner-occupied homes, rental values, and new construction costs add further insight into the nature of the community. Additional surrogates are available through educational attainments of the adult population and occupational characteristics.

The economic structure of the community is among the most important factors to be examined. The types of employment in the community and the industry structure offer one of the best clues as to the economic future, as well as to the cyclical stability. Specifically, the firms which offer employment in the community, and the valuation of their investments there, lend verification which reinforces theoretical knowledge of employment structures. The relation of the community to the economic unit of which it is a part, the Standard Metropolitan Statistical Area or the agricultural area, is basic to an understanding of its economic future. Finally, the way the unit is related to the outside world by transportation facilities has been basic in the past to an understanding of its future development.

The rating

The question is how debt, financial, governmental and economic analyses are put together to determine a rating. Simply, it is a question of examining each area of information and their interrelations and making a judgment modified as necessary by evidence and experience. There is no way to cram them all into a single formula which invariably produces the right answer. The stumbling block is weighting.

Most analysts agree ability to pay is an important part of a good rating. The analyst is well down the road to reaching a judgment on this by an examination of Number 3 (burden) and Number 7 (wealth) in the preceding list. These relate the debt burden to the community wealth level. They are quantifiable rather precisely, and they lend themselves to comparisons.

Willingness to pay is another accepted principle. Again, Number 7 (revenues), Number 17 (wealth), and Number 3 (burden) may be related to provide a judgment, which may be modified by Number 4 (history) and other indicators. Probably, most disagreements on ratings spring from different weights attached to the factors in analysis by different analysts.

Revenue bond analysis

Revenue bond analysis is in many ways less elusive than general obligation bond analysis. Generally, it involves a closed system with a finite number of variables and greater possibilities for quantification. This pledge of security involves an enterprise where the debt is related to an earning asset. The principles of credit analysis are the same, but the analysis shifts from the use of sovereign power of government to extract a tax to the operation of a user enterprise involving benefit analysis. Generally, there is a measurable benefit for which people
either are or are not willing to pay. Thus, we have bonds secured by pledges of electric, water, toll bridge, college dormitory, parking facility, toll road, or airport revenue.

Chief among the factors that must be examined are those pertaining to the revenue producing enterprise, its demand-creating potential, and the legal protections which are safeguards against the unexpected.

The physical plant involves engineers' appraisals of the soundness of the system and its ability to produce a service that can be sold at a price consumers are willing to pay. This involves system capability and the ability of management to operate with financial success. Other factors include the secular, cyclical and operating characteristics of the industry and the particular system which is being analyzed.

Legal protections involve detailed examination of the covenants in the Trust Indenture or bond resolution. Of particular importance is the flow of funds which is established for the enterprise, the additional bond clause, and the rate covenant. There are many examples of difficulties caused by the establishment of an improper flow of funds or an additional bond clause that was too liberal in its permissiveness. And the rate covenant establishes a base by which to measure management and its performance.

Covenants inserted in Indentures as protections have a way of gaining currency with the passage of time. A traditional one has been that pertaining to how the Indenture itself is amended. Right now, there are prosperous revenue-bond financed enterprises being watched by the operators of less successful undertakings with a view to how their "surpluses" can be absorbed by the less financially adroit. The difficult process of amending the Indenture may be the chief obstacle in the way of some of the changes economic pressures dictate.

The lease-rental obligation

The lease-rental obligation has come increasingly into use in recent years, and its analysis adds an examination of the legal relationship between the lessor, the lessee, and any other party to the arrangement. In this case, of course, the economic base of the lessee and credit factors pertaining to his ability to meet debt service obligations assume central importance. Most of this type of analysis is covered in the general obligation bond discussion previously noted.

Generally, the credit of the lessee does not impact on the credit of the lessor, where there is clear denial of any liability by the lessor. But any obscurity could result in future damage to the lessor's standing, particularly in psychological terms and in market reaction.

Other resources

Another type of bond security has been the "moral obligation" bond. Most frequently in this case, the issuer pledges as security the revenues associated with the undertaking. Then, to strengthen the bond,
funds from another source, usually the State, are pledged in one way or another. A common way is to establish a reserve fund for the bond which the State may contribute to and presumably keep filled if necessary, thereby establishing in the beholder's mind a flow of funds from the state treasury to the bondholder. The term "moral obligation" has set down roots in these discussions and has proved to be unfortunate. In this regard, dictionary phraseology runs "sanctioned by, or, operative upon one's conscience or ethical judgment; as, to feel a moral obligation."

A different matter is the guaranteed bond. In this case, another government will guarantee that principal and interest will be met. In such instances, the analyst examines the credit of the guarantor. But the analyst also looks for the payment mechanism. Prompt payment is what is required, and any time lapse between due date and payment date--while the guarantor learns of and responds to the situation--severely vitiates the usefulness of the guarantee.

The question the bond analyst must ask ultimately is: Under what set of circumstances, political or economic, would meeting these commitments become a burden? The State legally may or may not elect to appropriate moneys to fill the reserve once it has been drawn upon, in the case of the moral obligation bond.

Because of the open-ended nature of these commitments, they are insufficient per se to warrant a high investment standing. There are too many unresolved questions. There is no control on the magnitude of debt that can be brought under this umbrella. There is a lamentable postponement of unpleasant decisions regarding tax increases to fill a deficiency, and probably such decisions would have to be made in a financially-troubled atmosphere.
Note Rating Definitions.

MIG 1

Loans bearing this designation are of the best quality enjoying strong protection from established cash flows of funds for their servicing or from established and broad-based access to the market for refinancing, or both.

MIG 2

Loans bearing this designation are of high quality, with margins of protection ample although not so large as in the preceding group.

MIG 3

Loans bearing this designation are of favorable quality, with all security elements accounted for but lacking the undeniable strength of the preceding grades. Market access for refinancing, in particular, is likely to be less well established.

MIG 4

Loans bearing this designation are of adequate quality, carrying specific risk but having protection commonly regarded as required of an investment security and not distinctly or predominantly speculative.
Note Statement of Policy/Liquidity

Moody's, the nation's largest and oldest municipal bond rating agency, has an established rating policy that includes the rating and reporting on short-term state and municipal borrowing as well as long-term debt instruments. The rating and reporting system for short-term loans was established in recognition of the increasing importance of annual volume of short-term loans and the need of the market for credit analysis and appraisal of these loans. The following statement elaborates on some of the questions which arise in connection with our policy.

Nature of Short-Term Borrowing

The great bulk of state and local short-term borrowing falls into one of two categories.

One is short-term operating loans, normally tax anticipation or revenue anticipation notes issued to provide cash during a dry cash-flow period. These are issued in anticipation of the collection of property taxes or other major revenues and are rapid when the cash comes in.

The other is bond anticipation notes issued to provide construction money in advance of the sale of bonds. These are repaid when the proceeds of the bond sale are realized.

If expected cash flow do not materialize, or bonds are not sold prior to the time the notes mature, the holder of notes faces either delay in payment or the necessity of a renewal or extension of the maturing paper. Delay to the holder of notes may be costly in terms of ability to adhere to investment plans. A forced extension may require the holder to borrow to meet cash demands intended to be met with funds to be recieved at maturity of the note.

Eligibility for Rating

Short-term loans backed by the full faith and credit of the issuer will be eligible for a rating, as will loans backed by established revenues or cash flows specifically pledged to the loans, or by demonstrated ability to refinance either temporarily or with long-term debt securities. Ratings will be placed only on securities the credit quality of which is deemed by Moody's to be of an order qualifying such security for so-called unrestricted investment by commercial banks pursuant to present regulations and examination procedures of federal and state regulatory authorities, as interpreted by Moody's.

Application for rating may be made by the borrower, the underwriter, or an investor interested in the securities. The applicant will be required to provide or to assist in providing financial and other information on the borrower to insure the currency of relevant information and the dependability of the rating. Ratings will not be assigned or will be withdrawn when current information is not made available.
Moody's ratings will be assigned only on application and a fee will be charged separate from that charged for bond ratings. The rating will apply solely to each specific loan as identified by description including date of issuance and date of maturity, and will expire at maturity of the note. The rating of any issue will carry no implications as to the rating of a similar issue.

The distinction between notes and bonds being, in municipal financial practice, sometimes indistinct, the purpose and internal financial function of the loan will be a factor in determining whether a short-term loan rating or a bond rating is applicable. Certain short-maturity loans maturing serially and representing definitive financing for capital improvements continue to be rated as bonds. In general, short-term loan ratings will not be placed on securities maturing in more than five years.
5 Rating History - Rating Changes
New York City, New York (Bonds)

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(Series 1977 A & B)

*11/11/77 WITHDRAWN
(Sale Cancelled)

2/18/75 MIG 2*

*3/3/75 WITHDRAWN
(Sale Cancelled)

URBAN RENEWAL NOTES

<table>
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<td>2/16/79 MIG 3 1979 Series D</td>
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<td>MIG 2</td>
<td>9/21/79 MIG 3 Fiscal 1980 Series A</td>
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<td>12/7/79 MIG 3 Fiscal 1980 Series B</td>
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Rating History of the Municipal Assistance Corporation for the City of New York Bonds.

Series A, First General Resolution: A on 6/25/75 (New); A to B on 5/26/76; B to Baa on 5/24/77; Baa to Baa 1 on 11/13/78.

Series B, First General Resolution: A on 8/11/75 (New); A to B on 5/26/76; B to Baa on 5/24/77; Baa to Aaa on 1/12/78. (Refunded).

Series EE, 1977 First General Resolution: Baa on 6/10/77 (New); Baa to Baa 1 on 11/13/78.

Series GG, 1977 First General Resolution: Baa on 8/7/78 (New); Baa to Baa 1 on 11/13/78.

Series JJ, 1978 First General Resolution: Baa on 12/21/77 (New); Baa to Baa 1 on 11/13/78.

Series 8, 1977 Second General Resolution: Baa on 8/22/77 (New); Baa to Baa 1 on 11/13/78.

Series 9, 1977 Second General Resolution: Baa on 12/21/77 (New); Baa to Baa 1 on 11/13/78.


Series 14, 1979 Second General Resolution:

Baa 1 on 3/6/79 (New).

Series 15, 1979 Second General Resolution:

Baa 1 on 5/16/79 (New).

Series 16, 1979 Second General Resolution:

Baa 1 on 7/25/79 (New).

Series G, 1975 First General Resolution:

Con. (Aaa) on 7/25/79 (New).

Series M, 1975 First General Resolution:

Con. (Aaa) on 7/25/79 (New).

Series FF, 1977 First General Resolution:

Baa 1 on 8/7/79 (New).

Series 17, 1979 Second General Resolution:

Baa 1 on 8/28/79 (New).

Series 18, 1979 Second General Resolution:

Baa 1 on 8/28/79 (New).

Series 19, 1979 Second General Resolution:

Baa 1 on 10/26/79 (New).

Series 21, 1979 Second General Resolution:

Baa 1 on 12/13/79 (New).

Series 22, 1979 Second General Resolution:

Baa 1 on 12/31/79 (New).

Series 23, 1980 Second General Resolution:

Baa 1 on 1/10/80 (New).
Ratings of Related Entities Involving Pledge of New York City Credit

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<td>New York State Dormitory Authority Community College Bonds</td>
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<tr>
<td>New York State Housing Finance Agency Health Facilities Bonds</td>
<td>Baa</td>
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<tr>
<td>New York City Educational Construction Fund Bonds</td>
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<tr>
<td>New York City Housing Authority New York City Guaranteed Bonds</td>
<td>B</td>
</tr>
<tr>
<td>New York City Housing Development Corporation, General Housing Bonds</td>
<td>Ba</td>
</tr>
<tr>
<td>New York City Transit Authority Gross Revenue Bonds</td>
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</tbody>
</table>
Appendix

I  City of New York General Obligation Bond Review Report dated May 7, 1979

II  City of New York General Obligation Revenue Anticipation Note Reports:

   Fiscal 1980 Series B dated December 12, 1979
   Fiscal 1980 Series A dated September 21, 1979
   1979 Series D dated February 16, 1979
   1979 Series C Addendum dated January 30, 1979
   1979 Series C dated January 16, 1979
   1977 Series A,B,C, Addendum dated November 11, 1977

III  Municipal Assistance Corporation for the City of New York Reports:


   Series 15, 1979 Second General Resolution Bonds dated May 18, 1979
Mr. Chairman, as you know, I am here on behalf of Mr. Brenton W. Harries, President of Standard & Poor's Corporation, whose prior business travel commitments made his personal appearance here impossible. Your invitation to appear today indicated that the purpose of the hearing was to assess what progress New York City is making towards balancing its budget in accordance with generally accepted accounting principles and toward regaining access to the credit markets.

Perhaps a good point of departure would be to recall some of the points made by Mr. Harries a little over two years ago before this same committee. Mr. Harries indicated then that "... the City will be unable to borrow in the public debt market in a meaningful way until it can demonstrate fiscal stability through dependably balanced budgets with an outside
monitoring system." The same thing can pretty much be repeated today; and showing only one year would probably not be enough. That is why the Mayor's January 15 modification of the Financial Plan, bringing the City within the guidelines of generally accepted accounting principles in fiscal 1981, a year ahead of the 1982 requirement by law, assumes great potential significance. More about that a bit later.

My message to you today is that the City has made progress in moving to generally accepted accounting principles, but full access to the free public marketplace for other than limited note sales remains elusive -- and even the recent note sales are no real test of the City's credit, as their security is based upon state aids received late in the year after the State itself does its own spring borrowing. I had frankly thought that a relatively small City bond sale, even without an investment-grade rating, could have reached the market at a reasonable cost last August or September. What I had in mind was a 15-year bond issue of some $50 to $75 million. However, with the escalated yield trend since early October of last year, that chance has disappeared; and I do not see a current marketing of City bonds at what one could consider a reasonable rate. New York City bonds would have to carry a yield in fifteen years well in excess of the current scale of 9.50 percent for Detroit or 9 percent for Philadelphia, compared with the 8.25 percent for the Municipal Assistance Corporation. About the only municipal entity now close to the
New York City problem is the Chicago Board of Education, whose bonds in the secondary market (such as are available) are in the 10 percent range for fifteen years.

Much has been said in the past about New York City's unique attributes -- its size, its strengths and its weaknesses. Indeed, New York City over the years bit off more than it could chew. Spending patterns developed that could not be reversed and when ongoing solid revenues were not there to pay for it, the shortfall was borrowed and rolled over year after year until the snowball, if you will, just got too heavy; and the collapse resulted. New York City is now showing the symptoms of withdrawal. The City is slowly and painfully moving off the crutch of easy short-term borrowing for deficit financing and on to meeting expenses with a more reliable stream of revenues. The large scale governmental service sector in the City, built over many years with comparatively easy money, makes retrenchment very difficult indeed.

Progress has been made, however; and the January 15 modification is an accelerated step in the same direction. Beginning with the year ending June 30, 1976, the unaudited year-end deficit under generally accepted accounting principles was $1.87 billion, followed by $1.04 billion in 1977. The City's first outside audit report covered the 1978 year which reported a deficit of $722 million, followed by a deficit of $422 million at June 30, 1979. This is good progress, and the outside audit process and fiscal monitoring in place is also
something that must be maintained to enhance credibility and keep the City's feet to the fire. The estimated deficit for 1980 is placed at about $400 million.

This brings us to the January 15 modification in the Financial Plan, which calls for elimination of the deficit beginning in Fiscal 1981 -- that is, in the next budget. The estimated gaps to be closed are $677 million in 1981 and $1.1 billion in 1982. Although the City portion of the program to eliminate the gap rightly represents the largest portion of the program -- $507 million in 1981 and $729 million in 1982 -- dependence upon prospective federal and state legislative actions also remain an important ingredient and are of some concern in examining the total picture. Most of the City reductions will be in the area of education; a most difficult part of the City's operations and labor negotiations loom on the horizon. The new modification also shows the impact of inflation -- especially fuel costs upon City operations, which compound the problem of closing the gap.

Although progress can be said to have been made in the City's movement to GAAP, it has been and continues to be a difficult process. It is also important to note that continued federal and state aids remain an important part of the fiscal picture.

In the area of borrowing, progress has been made here, too, as the City's short-term needs have been reduced to the $600 to $800 million annual range, down from over $2.1 billion
four years ago. We have for more than ten years suggested that the City and the State of New York work together to even out the cash flow calendar so that anticipatory borrowing could be reduced for all units. The State has only recently indicated a movement in that direction, and it is possible that New York State's movement to GAAP will also prove to be a painful experience -- the dimensions of which have, as yet, not been at least publicly explored.

We have suggested that the City consider moving its water and sewer systems to a fully self-supporting enterprise basis and the subsequent issue of enterprise revenue bonds. Since a good deal of long-range capital borrowing will have to be done in this area over the years, it would seem logical to pull this substantial financing package away from the general purpose type of capital borrowing. With the Municipal Assistance Corporation providing some backstop borrowing power and the City's economy (which is so important to long-term viability) showing some signs of at least blotting the seepage of the last twenty years, the City could by late 1982 make a serious attempt to test the market on its own.

To the extent we can be of additional assistance, we will be glad to answer questions at this time.

HG:dmh
Statement

of

Amos T. Beason
Senior Vice President
Morgan Guaranty Trust Company

before the
Committee on Banking, Housing, and Urban Affairs
of the
Senate of the United States

January 28, 1980
Washington, D.C.
Senator Proxmire, Members of the Committee.

My name is Amos T. Beason. I am a Senior Vice President of Morgan Guaranty Trust Company, responsible for the bank's activities in the underwriting and trading of municipal securities and in providing public finance advisory services.

I appreciate the opportunity to share with you my thoughts about the City of New York's fiscal recovery process and where it is in that process. Naturally, I can speak only for my own bank, but I believe the views I express are shared rather widely by other financial-market observers of New York City's affairs.

I am sure I speak for the financial community generally in commending the Committee, its Chairman, and its staff for the constructively critical interest they have shown in New York City.

New York City needs access to short-term credit for its legitimate seasonal financing requirements and access to long-term credit to finance the maintenance of its infrastructure and the addition of capital improvements needed to serve its citizens.

New York City will have completed its fiscal recovery when it once more can meet those financing needs - short term and long term - on its own, when it no longer must resort to the props that were devised to keep it going after its loss of access to the public markets.

When the recovery process was started in 1975 no one thought that it would be easy. In magnitude the City's financial problems were unprecedented. During the last five years the Federal government, the State of New York, the City's elected officials, its labor unions, and New York financial institutions have all had to stretch in order to keep New York City financed. Today, the human, financial, and political resources applied to the process of fiscal recovery have
begun to show substantial, measurable results.

These results include:

1. Operating under more stringent budgeting and accounting procedures, including an annual independent audit, and under the review of the Financial Control Board,
2. Reducing annual budget deficits, and
3. Achieving a degree of public-market acceptance as evidenced by four successful public note sales totaling $650 million in the past two fiscal years.

Mayor Koch recently stated his intention that the City would operate under a balanced budget - balanced in accordance with generally accepted accounting principles - one year earlier than had been scheduled.

Such progress is crucial because some of the financial support that has carried the City for the last five years will not be available after fiscal 1982. Even if municipal pension funds were to consider adding to the substantial amounts of MAC bonds and unguaranteed city bonds they hold, Congressional approval would be required before they could act. The financial institutions that have come to the City's aid are limited in how much further credit they can extend by their duties to depositors, policy holders, and shareholders.

Nor can the Municipal Assistance Corporation be regarded as a long-term financing vehicle for the City. MAC has a debt ceiling, which cannot be changed without legislative and bond-holder approvals. It also has restrictive covenants which could limit its long-term financing flexibility, and the issuance of additional MAC bonds would increase the contingent debt of the State of New York. Further, I believe that investors regard MAC as a secure device meant to serve until the City regains access to the marketplace and
that if they came to feel that the City were not making every effort to return to the bond market under its own name, market acceptance of MAC bonds would be negatively affected.

In the minds of most professionals, a prerequisite to the City's full return to the debt market is that its bonds carry investment grade ratings. Because of the complexity of the City's finances and its recent history, sufficient time must be devoted to obtaining even minimum investment grade ratings. For that reason, continuing efforts leading to improved ratings must remain a high priority of key City officials. This will require a strong commitment despite the demands of labor negotiations, budget reviews, independent audits, and election campaigns. In view of the difficulty of understanding and rating a complex credit, the City's approach to the rating agencies must be on-going, with the objective of seeing that the City is accorded the highest rating consistent with its financial condition at a given time. I should think that credit analysts may want to gain first-hand impressions over time of how City officials cope with such critical matters as labor negotiations, revenue shortfalls, expenditure over-runs, and capital planning. After all, a rating and its improvement over time will be based not only on analysis of financial data, but equally important, on the confidence of the analysts in the willingness of City officials to retain financial practices which they embraced in adversity and their ability to produce predictable financial results in the future.

I believe the City has a significant message to convey to the rating agencies today. The last time the rating agencies gave the City an "A" rating was in the spring of 1975. New York is a stronger city today than it was then. Its financial results are measurable and its revenue base has grown. The public sector as a percentage of City gross product has declined. Elected
officials, recognizing that affordable government can be equated with good politics, have taken meaningful actions to improve the way the City's financial affairs are handled.

Further improvement clearly is still required of New York City, but I think the worst is behind it and its goal of regaining entry to the public debt markets is in sight.
TESTIMONY OF VICTOR GOTBAUM, EXECUTIVE DIRECTOR
OF DISTRICT COUNCIL 37, AMERICAN
FEDERATION OF STATE, COUNTY AND
MUNICIPAL EMPLOYEES

Before the U.S. Senate Committee
on Banking, Housing and Urban Affairs

January 28, 1980
I am pleased to be here today to speak on the contributions of New York City's workers to the present solvency of the City.

I am a labor leader and I expect that when I am asked to speak it is the point of view of labor that is desired. I shall leave the fiscal analyses to the fiscal experts and the issue of market entry to those who make their livings trying to read the market.

I will address myself to what I know best, the workers of the City of New York. I can tell you that they are hurting badly from their share of the fiscal belt tightening and sacrifices imposed by all levels of government.

In addition to the fiscal austerity there has been the onslaught of inflation, continually eroding their paychecks and preventing the small wage increases won in collective bargaining from being worth much at all. Since June, 1975, the New York City area CPI has increased about 35%. A conservative projection would be that by June 1980 it will have gone up almost 40%. During this same period, New York City's workers' net pay has gone up considerably less. (See Table I) For lower-paid workers, such as the Nurses Aide or Senior Clerk, inflation rose faster than pay by 11-12%; for Librarians and Social Workers, the gap is about 15%; for Accountants, 18½%; and for Engineers the difference approaches 25%. The dollar losses in monthly purchasing power range from approximately $60/month for the lower paid workers to approximately $125/month for the Librarians and Social Workers to almost $250/month for the Engineer. And, these workers cannot look forward at the moment to any likely slowdown of inflation.
over the period relatively more than other лиқas which did not receive an equivalent increase.

3. Social workers had an education differential built into their rate during 1975 under the terms
recalculated to the title office which put employees on the list and to.

2. Correspondent salaries were recalculated during this period; the former senior clerk was automatically
included in calculations.

1. The New York area CPI and real net wages for 6/80 are estimates based on a 91 change in the

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<td>$ 113.84</td>
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ENGINEER
SOCIAL WORKER
ACCOUNTANT
MOTOR VEHICLE OPERATOR
LIBRARIAN
CUSTOMS ASSISTANT
SENIOR CLERK/OFFICE AIDE
NURSE'S AIDE

(6/80 DOLLARS)

CHANGE IN REAL 

DOLLARS 

MONTHLY NET PAY

6/75 - 6/80

6/80 - 6/80

FOR DETERMINATION OF NET PAY

LOST IN REAL

MONTHLY NET PAY

6/75 - 6/80

FOR DETERMINATION OF

MONTHLY NET PAY
Economic hardship is very real for our members. The inadequacy of their salaries to provide life's necessities cannot be ignored. A study by our Research Department, examining our members' family circumstances and their family income in the summer of 1978 revealed that 20-30% of our members were then earning less than the Bureau of Labor Statistics' (BLS) low budget amount appropriate to their family size, and 45% more were earning less than the appropriate intermediate family budget. In total, then, about 75,000 District Council 37 members are likely to be in families where the earnings fall below the appropriate BLS intermediate family budget for New York City. Counting dependents, there may be as many as a quarter of a million people experiencing this hardship.

Many of our members are women who are not currently married and have dependent children. Our Research Department estimates that 40% of them earn less than the appropriate BLS low budget, with another 52% falling between the low and intermediate budget levels. Thus, more than 90% of our members who are not currently married and have dependents earn less than the BLS New York City intermediate family budget for their appropriate sized family. And, we all know that segment of our workforce is growing very rapidly.

Now, it is true that we do not take workers' family considerations into account directly when determining their pay. But, we must take account of their economic hardship. Their sacrifices have been real and their economic hardship is tangible. That is borne out by the data I have presented.

But their sacrifices and their hardship go beyond the ravages of inflation on their paychecks. In the immediate days
of the fiscal crisis of 1975 it was take-backs and layoffs:

WAGE AND FRINGE BENEFIT CUTS AND DEFERRALS SUFFERED BY THE GENERAL WORKERS OF NEW YORK CITY

11/74 - 1/75 Waiving of past due welfare fund contributions, changes in work rules, reductions in scheduled overtime, elimination of summer hours, etc.

6/75 Deferral of all or part of a scheduled 6% wage increase due on July 1, 1975

4/76 Reduction of Increased-Take-Home-Pay benefit (Increased 2% pension contribution)

6/76 - 6/78 Deferred/reduced fringe benefits, fiscal years 1977-1978

6/76 - 6/78 Deferral of difference between a .4 COLA and a .3 COLA, fiscal years 1977 and 1978

The value of the losses in pay and fringe benefits exceed $400 million.

Layoffs of our members numbered about 30,000. Layoffs and a strict attrition policy have resulted in a drop of almost a quarter of New York City's filled full-time positions since the end of FY75. The elimination of more than 60,000 full-time positions and thousands more part-time positions has been no small accomplishment. It has meant a considerable increase in the workloads for those who remain.

At the same time the fiscal crisis austerity has meant that this increased workload is often performed with out-moded and unmended equipment and in deteriorated and dangerous conditions. For too many of the City's workers, there are offices with broken windows, no heat, and peeling paint; welfare centers with rats and roaches; work-sites without functioning toilets and with exposed asbestos. Such demeaning conditions are clearly counter-productive; yet the City makes minimal effort to improve them.
Then, too, there is the danger. The sad fact is that too many City employees are being maimed on the job. Highway laborers on improperly marked work-sites are struck and seriously injured or even killed by passing vehicles. Drivers of City owned trucks are forced to drive improperly inspected vehicles which often lack brakes, proper lighting, or good tires. Such trucks are rolling death-traps for their drivers and other motorists. Tree sprayers use pesticides without proper protective equipment and training and are thus subjected to skin rashes, burns, anemia, stomach disorders, and even brain damage. Workers in hospital laundry rooms breathe cotton fibers and are subject to lung cancer and cancer of the digestive track.

New York City employees have an accident and injury rate which is astounding. As the table below indicates, in 1977, the accident rate for City employees was almost four times greater than for all private sector employees, and it exceeded that for coal miners, the most hazardous private sector occupation.

<table>
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<th>ACCIDENT RATES FOR SELECTED GROUPS OF EMPLOYEES - 1977</th>
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<tbody>
<tr>
<td>Accidents per one Million hours of Work</td>
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<tr>
<td>All U.S. Private Business</td>
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<tr>
<td>Coal Miners</td>
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<tr>
<td>New York City Employees</td>
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These facts and the working conditions they describe should tell you much about the demoralization of the workforce. Lack of productivity - anywhere - stems from bad workplaces,
not bad workers. With the best will in the world, three workers cannot be expected to do the work of five when equipment is deteriorated and dangerous and the workplace itself is decrepit and depressing.

And, still, efforts have been made toward increasing productivity in these circumstances. They have been made because they must. Because there are dedicated public employees who want to serve the public; because there are dedicated managers who want to see that the best services are provided; and because the public demands it.

This Union has co-operated with management in the broad-banding of civil service titles, to allow for greater management flexibility in staffing and to open up promotions and new responsibilities for workers. We also support a more flexible system of internal transfers of personnel within the City.

We also pushed the Mayor to set up the City-wide Productivity Council mandated by the Federal Loan Guarantee Act. It is not our fault that the Mayor placed responsibility with two Deputy Mayors who left in mid-year. I have strong hopes that a reconstituted Productivity Council, which will begin meeting in February, will address some of the pressing issues of the management of public services. New York City labor and management have a long tradition of co-operation on this issue. We want it to continue and will work in that direction.

However, national efforts are really needed on the question of improved service productivity -- public and private. New York City's productivity is certainly no worse than that in
other local governments and in non-governmental service industries. But so far the lead of Washington has not materialized. The Federal civil service has not led the way; nor have suggestions from the National Productivity Council. We hope there will be a serious and creative examination of this issue, because it is common to all local governments and to the wider, growing service sector.

One needs only to look at the fiscal problems in Chicago to know that, really, all the problems that this Committee has investigated with respect to New York City are pervasive urban problems. "The city that works" doesn't anymore. It never really did for many of its residents and its workers. One can add Detroit and Wayne County, Cleveland, San Francisco, St. Louis, New Orleans, Newark and others to the growing list of cities in trouble. New York City was not a special case; it was not unique. It simply got there first. And now that it has been followed, the need for an American Urban Policy becomes pressing.

We who have been to the brink and have painfully worked ourselves back from it know the stumbling blocks which were in the way. The nation's cities, particularly the old ones, carry the burden of the country's poor on their backs. New York City's share of Medicaid and welfare approach $1 billion. But, beyond that, the burden expresses itself in the higher unemployment rates, the abandonment of property, the tremendous burdens on the school systems for special classes, the post-ponement of capital improvements and repairs and its accompanying general aura of disrepair.
We in New York appreciate the loan guarantees. We feel we are demonstrating that they were the right thing for Congress to have done. But, ultimately they have not cost the Congress or the U.S. government anything. They have cost the workers of the City of New York plenty. But, too, they have cost the other cities of this country something. Treating New York City as if it were a special case has simply put off dealing with the fundamental inequalities of today's cities. Lost opportunities are real costs. I hope they can be eliminated.
Presentation By Jack Bigel
on Behalf of the New York City
Municipal Labor Committee
To The United States Senate,
Committee on Banking, Housing and
Urban Affairs,
Senator William Proxmire, Chairman

January 28, 1980

1980 Program Planners, Inc.
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- New York City Financial Progress 6-23
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Senator Proxmire, the distinguished Chairman of this Committee, in his letter of January 8, clearly set forth the purposes of this hearing:

"[It] is to determine whether the requirements of the Act are being met and to assess what progress New York City is making toward balancing its budget in accordance with generally accepted accounting principles and toward regaining access to the credit markets."

In accordance with that mandate our statement will describe the achievement of amazing progress, using 1975 as the benchmark year. In fiscal year 1975 the City:

- issued $3.4 billion in short-term debt (see Table 1);
- its short-term financing was equal to 69.9% of the operating budget (see Table 1);
- it had an operating deficit (in accordance with generally accepted accounting principles) that exceeded $1.8 billion;
- the public financing markets were closing to the city;
- financial record keeping was at a minimal level;
- was on the verge of bankruptcy.

This should be compared with the current state of affairs:

- the City will issue less than $600 million of short-term debt in FY 1980;
Table 1

Comparison of NYC's Operating Expenses and Short-Term Debt Issue For Fiscal Years 1940-1979

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Total Operating Expenses</th>
<th>Short Term Debt Issue</th>
<th>Year's Issue of Short Term Debt As a Percent of Operating Expenses</th>
</tr>
</thead>
<tbody>
<tr>
<td>1979</td>
<td>$12,755,776,000</td>
<td>$650,000,000</td>
<td>5.1%</td>
</tr>
<tr>
<td>1978</td>
<td>13,580,291,647</td>
<td>2,073,000,000</td>
<td>15.3%</td>
</tr>
<tr>
<td>1977</td>
<td>13,583,309,000</td>
<td>2,306,000,000</td>
<td>16.9%</td>
</tr>
<tr>
<td>1976</td>
<td>12,249,071,000</td>
<td>6,038,902,987</td>
<td>48.9%</td>
</tr>
<tr>
<td>1975</td>
<td>12,017,684,521</td>
<td>8,395,745,000</td>
<td>69.9%</td>
</tr>
<tr>
<td>1974</td>
<td>10,247,642,736</td>
<td>7,305,915,000</td>
<td>71.3%</td>
</tr>
<tr>
<td>1973</td>
<td>9,560,927,970</td>
<td>4,003,285,000</td>
<td>41.9%</td>
</tr>
<tr>
<td>1972</td>
<td>8,497,773,904</td>
<td>5,248,960,000</td>
<td>61.8%</td>
</tr>
<tr>
<td>1971</td>
<td>7,822,342,445</td>
<td>6,513,240,000</td>
<td>83.3%</td>
</tr>
<tr>
<td>1970</td>
<td>6,700,803,800</td>
<td>4,400,925,000</td>
<td>65.7%</td>
</tr>
<tr>
<td>1969</td>
<td>6,058,823,974</td>
<td>3,270,995,000</td>
<td>54.0%</td>
</tr>
<tr>
<td>1968</td>
<td>5,290,788,316</td>
<td>2,427,717,000</td>
<td>45.9%</td>
</tr>
<tr>
<td>1967</td>
<td>4,492,797,211</td>
<td>2,076,036,800</td>
<td>46.2%</td>
</tr>
<tr>
<td>1966</td>
<td>3,774,733,084</td>
<td>1,645,597,560</td>
<td>43.6%</td>
</tr>
<tr>
<td>1965</td>
<td>3,341,783,221</td>
<td>1,469,989,860</td>
<td>44.0%</td>
</tr>
<tr>
<td>1964</td>
<td>3,098,265,632</td>
<td>1,166,728,800</td>
<td>37.7%</td>
</tr>
<tr>
<td>1963</td>
<td>2,789,112,984</td>
<td>807,651,800</td>
<td>29.0%</td>
</tr>
<tr>
<td>1962</td>
<td>2,601,408,634</td>
<td>842,238,000</td>
<td>32.4%</td>
</tr>
<tr>
<td>1961</td>
<td>2,428,223,378</td>
<td>697,700,000</td>
<td>28.7%</td>
</tr>
<tr>
<td>1960</td>
<td>2,244,808,814</td>
<td>703,743,000</td>
<td>31.3%</td>
</tr>
<tr>
<td>1959</td>
<td>2,081,308,139</td>
<td>665,643,000</td>
<td>32.0%</td>
</tr>
<tr>
<td>1958</td>
<td>2,002,500,191</td>
<td>534,190,000</td>
<td>26.7%</td>
</tr>
<tr>
<td>1957</td>
<td>1,912,607,869</td>
<td>563,300,000</td>
<td>29.5%</td>
</tr>
<tr>
<td>1956</td>
<td>1,782,260,575</td>
<td>479,230,000</td>
<td>26.9%</td>
</tr>
<tr>
<td>1955</td>
<td>1,630,706,797</td>
<td>499,501,450</td>
<td>30.6%</td>
</tr>
<tr>
<td>1954</td>
<td>1,517,417,222</td>
<td>499,100,000</td>
<td>32.5%</td>
</tr>
<tr>
<td>1953</td>
<td>1,476,319,752</td>
<td>422,000,000</td>
<td>28.6%</td>
</tr>
<tr>
<td>1952</td>
<td>1,341,289,847</td>
<td>379,401,510</td>
<td>28.3%</td>
</tr>
<tr>
<td>1951</td>
<td>1,240,373,348</td>
<td>348,900,000</td>
<td>28.1%</td>
</tr>
<tr>
<td>1950</td>
<td>1,169,703,655</td>
<td>446,920,000</td>
<td>38.2%</td>
</tr>
<tr>
<td>1949</td>
<td>1,104,751,647</td>
<td>408,500,000</td>
<td>37.0%</td>
</tr>
<tr>
<td>1948</td>
<td>1,026,859,998</td>
<td>305,200,000</td>
<td>29.7%</td>
</tr>
<tr>
<td>1947</td>
<td>918,071,045</td>
<td>243,900,000</td>
<td>26.6%</td>
</tr>
<tr>
<td>1946</td>
<td>768,689,270</td>
<td>244,800,000</td>
<td>31.8%</td>
</tr>
<tr>
<td>1945</td>
<td>726,266,387</td>
<td>219,100,000</td>
<td>30.2%</td>
</tr>
<tr>
<td>1944</td>
<td>732,419,726</td>
<td>261,100,000</td>
<td>35.6%</td>
</tr>
<tr>
<td>1943</td>
<td>752,380,457</td>
<td>290,300,000</td>
<td>38.6%</td>
</tr>
<tr>
<td>1942</td>
<td>791,290,935</td>
<td>275,900,000</td>
<td>34.9%</td>
</tr>
<tr>
<td>1941</td>
<td>811,417,679</td>
<td>274,000,000</td>
<td>33.8%</td>
</tr>
<tr>
<td>1940</td>
<td>$751,411,617</td>
<td>$304,300,000</td>
<td>40.4%</td>
</tr>
</tbody>
</table>
a. Because of accounting and definitional changes in the NYC budget, over the last few years, it is very difficult to make clear consistent comparisons between pre and post fiscal 1975 expenses.

Source:

Annual Report of the Comptroller of the City of New York
1940: General Summary I
1941-1942: Part I, Consolidated Statement, Summary I
1943-1975: Part 6-C, Statement 1 & 2
1978: Part 2, Statement 5
For operating expenses only,
1941-1958: Part I, Consolidated Statements, Summary I
1959-1975: Part I, Consolidated Statements, Chart 7
1978: Part 2 - General Fund-Statement I
1979: Part 2 - General Fund-Statement I
the City will have a balanced budget under generally accepted accounting principles in FY 1981, and had budgetary surpluses (as defined by State law) in FY 1978 of $32 million, and in FY 1979 of $213 million;

- the City sold $275 million of short-term notes in the public market in FY 1979 and will accomplish all of its seasonal financing in FY 1980 in the public market;

- the City now has one of the leading municipal accounting and budgetary systems in the United States.

Of critical importance has been the elimination of any real threat of bankruptcy to the City. In 1975 this could have occurred because a significant part of the financing was required to fund daily operations. This is no longer the case. The City will have eliminated the financing of current operations from the proceeds of capital bond sales by FY 1981. Should the City be unable to obtain financing for its capital needs in FY 1983 the daily operations of the City would continue. This is a 100% reversal from the circumstances in FY 1975.

The City has for the most part resolved the major problems that existed in FY 1975. The current problems are
in three areas: transit, health care, and education. These financing problems are not peculiar to New York City; every major urban area in the United States faces similar problems. The size of New York City magnifies the problem. The common thread that binds these problems is that the national government has failed to adequately provide funds or provide comprehensive solutions and direction in these areas. Until adequate national financing and solutions are made available, these problems will continue to plague America's urban centers, as well as New York.

The sections which follow reviews the fiscal health of the City, its progress, market access, and the actions of the City's Retirement Systems and workforce during the fiscal crisis.
GAAP Deficit Reduction

The City has been able since FY 1976 to reduce its GAAP deficit by over $1.4 billion and prevent a possible $1.6 billion increase in expenses due to inflation.

On July 1, 1976, the City reported that it ended FY 1976 with a GAAP-basis deficit of over $1.8 billion. Three years later that deficit was $422 million, or $1.4 billion less than FY 1976. In three years, 78% of the deficit was eliminated.

Table 2

New York City
FY 1976 - FY 1979
GAAP-Basis Revenues and Expenses
($ in millions)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenues</td>
<td>$7,131.0</td>
<td>$7,809.4</td>
<td>$8,021.3</td>
<td>$8,144.3</td>
<td>$1,013.3</td>
</tr>
<tr>
<td>Expenses</td>
<td>8,953.0</td>
<td>8,848.2</td>
<td>8,733.4</td>
<td>8,566.6</td>
<td>(386.4)</td>
</tr>
<tr>
<td>Deficit</td>
<td>$1,822.0</td>
<td>$1,038.8</td>
<td>$712.1</td>
<td>$422.3</td>
<td>($1,399.7)</td>
</tr>
</tbody>
</table>

Source: New York City Comptroller Reports FY 1976 - FY 1979
adjusted to exclude Federal and State Categorical Aid.

NOTE:
a. This does not include the expenses assumed by the State
during this period (e.g., CUNY and court expenses)
Table 2 indicates the City had increased revenues of $1 billion and reduced expenses of $386 million. The $1 billion increase was due to the City's tax income increasing $754 million, unrestricted Federal/State aid increasing $220 million, and the reserve for disallowances of intergovernmental aid decreasing (and therefore increasing revenue) $40 million. The $754 million represents a 12% increase over the amount collected in FY 1976.

The argument could be made that the reduction in expenses was not substantial. However, if the City's FY 1976 expenses had increased by the rate of inflation in New York City during the three year period (FY 1977 - FY 1979), then the expenses would have increased over 18% or $1,619 million. Table 3 indicates that possibility with the deficit growing by $606 million.

Table 3

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenues</td>
<td>$7,131.1</td>
<td>$7,809.4</td>
<td>$8,021.3</td>
<td>$8,144.3</td>
<td>$1,013.2</td>
</tr>
<tr>
<td>Expenses</td>
<td>8,953.0</td>
<td>9,427.5</td>
<td>9,898.9</td>
<td>10,572.0</td>
<td>1,619.0</td>
</tr>
<tr>
<td>Deficit</td>
<td>$1,821.9</td>
<td>$1,618.1</td>
<td>$1,877.6</td>
<td>$2,427.7</td>
<td>$605.8</td>
</tr>
</tbody>
</table>

Source: Revenue from New York City Comptroller Reports, expenses adjusted for New York City increase in CPI: FY 1977 5.3%; FY 1978 5.0%; FY 1979 6.8%.
The reduction of expenses (on a GAAP-basis) by $386 million, then, should be seen in the context that the City was able during that time period to prevent expenses from escalating $1.6 billion.

It is significant that while New York City expenditures decreased in FY 1976-FY 1979, the expenditures of other cities with a population of more than one million have increased:

<table>
<thead>
<tr>
<th>Rank</th>
<th>City</th>
<th>Expenditures</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>1976</td>
<td>1979</td>
</tr>
<tr>
<td>1</td>
<td>Detroit</td>
<td>$465.5</td>
<td>$623.9</td>
</tr>
<tr>
<td>2</td>
<td>Chicago</td>
<td>$629.8</td>
<td>$825.9</td>
</tr>
<tr>
<td>3</td>
<td>Houston</td>
<td>$271.5</td>
<td>$398.4</td>
</tr>
<tr>
<td>4</td>
<td>Philadelphia</td>
<td>$786.1</td>
<td>$989.1</td>
</tr>
<tr>
<td>5</td>
<td>NEW YORK CITY</td>
<td>$8,953.0</td>
<td>$8,567.0</td>
</tr>
</tbody>
</table>

NOTES:

a. Those cities with estimated July 1, 1976 population of 1,000,000 or more; Los Angeles data are not available.

b. Not including categorical Federal and State aid.

c. Corporate Purposes Funds.

Source: Official Statements of Respective Cities.
Personnel

From July 1, 1975, to June 30, 1980 (projected) the City's workforce (Mayoral agencies only) will have decreased by 23%. In agencies such as Social Services the decline was 29%. In agencies which are predominantly City financed (Police, Fire, Sanitation), the decline ranges from 10% to 21% of the workforce. Table 5 contains the details of the workforce reduction.

Table 6 indicates the change from June 30, 1975 to June 30, 1982 as the workforce is projected at that date. This indicates that the City has reduced its workforce by over 25% in seven years.

This reduction must be compared with that which occurred in other jurisdictions. Table 7 compares the change in workforce for New York City and eight other counties and cities in New York State for FY 1975-FY 1979 period. New York City's reduction was far greater than any other jurisdiction.

Looking at government employment throughout the United States (Tables 8 to 10):

- in the period FY 1975-FY 1979 New York City was the only government to lose employees

---

1Employment and payroll data for N.Y.C. in Tables ... to the Department of Commerce and includes non-mayoral agencies, and personnel from agencies not otherwise paid by the City (e.g. Transit and HHC).
- for cities with population of more than one million,
New York City lost 19.5% of its employees (including non-mayoral agencies), while the other cities showed small increases in the aggregate.

In addition, Tables 11 and 12 indicate that payroll costs for the City have decreased while that of other cities has increased significantly.
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Education</td>
<td>81,970</td>
<td>67,785</td>
<td>63,582</td>
<td>71,734</td>
<td>72,262</td>
<td>70,729</td>
<td>(11,241)</td>
<td>(14%)</td>
</tr>
<tr>
<td>Police</td>
<td>35,447</td>
<td>30,202</td>
<td>29,258</td>
<td>29,378</td>
<td>28,350</td>
<td>27,928</td>
<td>(7,519)</td>
<td>(21%)</td>
</tr>
<tr>
<td>Social Services</td>
<td>28,331</td>
<td>23,992</td>
<td>22,569</td>
<td>23,021</td>
<td>22,379</td>
<td>20,171</td>
<td>(8,160)</td>
<td>(29%)</td>
</tr>
<tr>
<td>Fire</td>
<td>13,885</td>
<td>12,180</td>
<td>11,528</td>
<td>11,918</td>
<td>12,344</td>
<td>12,431</td>
<td>(1,454)</td>
<td>(10%)</td>
</tr>
<tr>
<td>Sanitation and EPA</td>
<td>18,846</td>
<td>16,117</td>
<td>15,729</td>
<td>16,165</td>
<td>16,106</td>
<td>16,117</td>
<td>(2,729)</td>
<td>(14%)</td>
</tr>
<tr>
<td>All Other</td>
<td>75,198</td>
<td>61,911</td>
<td>52,510</td>
<td>49,669</td>
<td>46,177</td>
<td>47,290</td>
<td>(27,911)</td>
<td>(37%)</td>
</tr>
<tr>
<td></td>
<td>253,677</td>
<td>212,187</td>
<td>195,176</td>
<td>201,885</td>
<td>197,618</td>
<td>194,666</td>
<td>(59,001)</td>
<td>(23%)</td>
</tr>
</tbody>
</table>

NOTES:

b. Excludes HKC, Transit Authority, Housing Authority Personnel
c. Projected as of 1/17/80
d. Includes CETA, CD, and other non-City funded personnel
Table 6

New York City Personnel
1975 vs. Projected 1982

<table>
<thead>
<tr>
<th></th>
<th>6/30/75</th>
<th>6/30/82</th>
<th>Change</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Education</td>
<td>81,970</td>
<td>67,302</td>
<td>(14,668)</td>
<td>(17.9%)</td>
</tr>
<tr>
<td>Police</td>
<td>35,447</td>
<td>27,426</td>
<td>(8,021)</td>
<td>(22.6%)</td>
</tr>
<tr>
<td>Social Services</td>
<td>28,331</td>
<td>20,294</td>
<td>(8,037)</td>
<td>(28.4%)</td>
</tr>
<tr>
<td>Fire</td>
<td>13,885</td>
<td>11,893</td>
<td>(1,992)</td>
<td>(14.3%)</td>
</tr>
<tr>
<td>Sanitation and EPA</td>
<td>18,846</td>
<td>14,838</td>
<td>(4,008)</td>
<td>(21.3%)</td>
</tr>
<tr>
<td>All Other</td>
<td>75,198</td>
<td>44,603</td>
<td>(30,595)</td>
<td>(40.7%)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>253,677</td>
<td>186,361</td>
<td>(67,316)</td>
<td>(26.6%)</td>
</tr>
</tbody>
</table>

**NOTES:**

a. New York City official statement and Financial Plan 1/15/80
b. Excluded HHC, Transit Authority, Housing Authority Personnel
c. Includes CETA, CD, and other non-city funded personnel
<table>
<thead>
<tr>
<th></th>
<th>FY 1975</th>
<th>FY 1979</th>
<th>Absolute</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Onondaga County</td>
<td>4,328</td>
<td>5,382</td>
<td>1,054</td>
<td>24.4%</td>
</tr>
<tr>
<td>Rochester</td>
<td>8,718</td>
<td>9,732</td>
<td>1,014</td>
<td>10.4%</td>
</tr>
<tr>
<td>Nassau County</td>
<td>19,271</td>
<td>20,602</td>
<td>1,331</td>
<td>6.9%</td>
</tr>
<tr>
<td>Westchester County</td>
<td>7,045</td>
<td>7,392</td>
<td>347</td>
<td>4.9%</td>
</tr>
<tr>
<td>Monroe County</td>
<td>5,425</td>
<td>5,331</td>
<td>(94)</td>
<td>(1.7%)</td>
</tr>
<tr>
<td>Buffalo</td>
<td>13,218</td>
<td>12,543</td>
<td>(675)</td>
<td>(5.1%)</td>
</tr>
<tr>
<td>Suffolk County</td>
<td>11,195</td>
<td>10,266</td>
<td>(927)</td>
<td>(8.3%)</td>
</tr>
<tr>
<td>Yonkers</td>
<td>5,428</td>
<td>4,552</td>
<td>(876)</td>
<td>(16.1%)</td>
</tr>
<tr>
<td>New York City</td>
<td>253,677</td>
<td>197,618</td>
<td>(56,059)</td>
<td>(22.1%)</td>
</tr>
</tbody>
</table>

### Table 3

**Changes in Government Employment in the United States**

**FY 1975 - FY 1979**

<table>
<thead>
<tr>
<th>Government Level</th>
<th>Employment (^a) FY 1975</th>
<th>Employment (^a) FY 1979</th>
<th>Absolute Change</th>
<th>Percent Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Federal</td>
<td>2,742,654</td>
<td>2,746,628</td>
<td>3,974</td>
<td>1.4%</td>
</tr>
<tr>
<td>State &amp; Local (^b) Education</td>
<td>9,485,442</td>
<td>10,406,102</td>
<td>920,660</td>
<td>9.7%</td>
</tr>
<tr>
<td></td>
<td>4,795,494</td>
<td>5,102,550</td>
<td>307,056</td>
<td>6.4%</td>
</tr>
<tr>
<td></td>
<td>4,689,948</td>
<td>5,303,552</td>
<td>613,604</td>
<td>13.1%</td>
</tr>
<tr>
<td>States</td>
<td>2,653,259</td>
<td>2,965,961</td>
<td>312,702</td>
<td>11.8%</td>
</tr>
<tr>
<td>Local (^b)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>County</td>
<td>6,832,183</td>
<td>7,440,141</td>
<td>607,958</td>
<td>8.9%</td>
</tr>
<tr>
<td>Municipal</td>
<td>1,343,219</td>
<td>1,606,283</td>
<td>263,064</td>
<td>19.6%</td>
</tr>
<tr>
<td>Township</td>
<td>1,731,644</td>
<td>1,844,563</td>
<td>112,919</td>
<td>6.5%</td>
</tr>
<tr>
<td>School District</td>
<td>232,798</td>
<td>245,114</td>
<td>12,316</td>
<td>5.3%</td>
</tr>
<tr>
<td>Special District</td>
<td>3,212,175</td>
<td>3,393,035</td>
<td>180,860</td>
<td>5.6%</td>
</tr>
<tr>
<td>New York City</td>
<td>395,430</td>
<td>318,376</td>
<td>-77,054</td>
<td>-19.5%</td>
</tr>
<tr>
<td>Education</td>
<td>135,152</td>
<td>99,750</td>
<td>-35,402</td>
<td>-26.2%</td>
</tr>
<tr>
<td>Other</td>
<td>260,278</td>
<td>218,626</td>
<td>-41,652</td>
<td>-16.0%</td>
</tr>
</tbody>
</table>

**NOTES**

b. Excluding New York City.

**Source:**

Table 3

Ranking of United States Cities
With Populations of One Million or More People
By Changes in the Number of Municipal Workers,
FY 1975 to FY 1979

<table>
<thead>
<tr>
<th>Rank</th>
<th>City</th>
<th>Number of Employees</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>1975</td>
<td>1979</td>
</tr>
<tr>
<td>1</td>
<td>Houston</td>
<td>11,937</td>
<td>13,726</td>
</tr>
<tr>
<td>2</td>
<td>Chicago</td>
<td>44,416</td>
<td>47,535</td>
</tr>
<tr>
<td>3</td>
<td>Los Angeles</td>
<td>44,560</td>
<td>44,027</td>
</tr>
<tr>
<td>4</td>
<td>Philadelphia</td>
<td>37,124</td>
<td>36,428</td>
</tr>
<tr>
<td>5</td>
<td>Detroit</td>
<td>27,017</td>
<td>23,955</td>
</tr>
<tr>
<td>6</td>
<td>New York City</td>
<td>395,430</td>
<td>318,376</td>
</tr>
</tbody>
</table>

Five City Total: 165,054 165,671 617 0.4%
All US Cities: 1,731,644 1,846,435 114,791 6.6%

NOTES:

a. Full-Time equivalents as of October, 1974 and October, 1978 unless otherwise noted.
c. Not including New York City.

<table>
<thead>
<tr>
<th>Rank</th>
<th>City Grouping by Population</th>
<th>Percent Change in Employees</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>0 - 49,999</td>
<td>8.3%</td>
</tr>
<tr>
<td>2</td>
<td>50,000 - 249,999</td>
<td>8.2</td>
</tr>
<tr>
<td>3</td>
<td>250,000 - 499,999</td>
<td>7.7</td>
</tr>
<tr>
<td>4</td>
<td>All US Cities&lt;sup&gt;b&lt;/sup&gt;</td>
<td>6.6</td>
</tr>
<tr>
<td>5</td>
<td>500,000 - 999,999</td>
<td>3.2</td>
</tr>
<tr>
<td>6</td>
<td>1,000,000 or more&lt;sup&gt;b&lt;/sup&gt;</td>
<td>0.4</td>
</tr>
<tr>
<td>7</td>
<td>NEW YORK CITY</td>
<td>-19.5%</td>
</tr>
</tbody>
</table>

**NOTES:**

a. Except for a few cities noted elsewhere, full-time equivalents as of October, 1974 and October, 1978.

b. Not including New York City.


Table 11

Ranking of Groupings of
United States Cities by Changes in
The Monthly Payroll Costs,
FY 1975 to FY 1979

<table>
<thead>
<tr>
<th>Rank</th>
<th>City Grouping by Population</th>
<th>Percent Change in Monthly Payroll Costs(^a)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>0 - 49,999</td>
<td>43.2%</td>
</tr>
<tr>
<td>2</td>
<td>50,000 - 249,999</td>
<td>40.5</td>
</tr>
<tr>
<td>3</td>
<td>All US Cities(^b)</td>
<td>37.5</td>
</tr>
<tr>
<td>4</td>
<td>500,000 - 999,999</td>
<td>32.8</td>
</tr>
<tr>
<td>5</td>
<td>250,000 - 499,999</td>
<td>31.5</td>
</tr>
<tr>
<td>6</td>
<td>1,000,000 or more(^c)</td>
<td>29.3</td>
</tr>
<tr>
<td>7</td>
<td>NEW YORK CITY(^d)</td>
<td>- 0.1%</td>
</tr>
</tbody>
</table>

NOTES:

a. Except for a few cities noted elsewhere, based on reported
total monthly payroll costs (including overtime, shift
differential, part-timers, etc.) in October of 1974 and 1978.
b. Not including New York City or Baltimore.
c. Not including New York City.
d. Does not reflect the October 1, 1978 4% wage increase which
was not paid out in that month. An overall 4% increase
would bring the 1975-1979 change to 3.9%.

Source: City Employment in 1978, GE78-No.2, US Department of Commerce,

City Employment in 1974, GE74-No.2, US Department of Commerce,
DC: June, 1975.


<table>
<thead>
<tr>
<th>Rank</th>
<th>City</th>
<th>Monthly Payroll (in thousands)</th>
<th>Change</th>
<th>Absolute (in thousands)</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Houston</td>
<td>$9,755</td>
<td>$16,756</td>
<td>$7,001</td>
<td>71.8%</td>
</tr>
<tr>
<td>2</td>
<td>Chicago</td>
<td>49,238</td>
<td>66,637</td>
<td>17,399</td>
<td>35.3</td>
</tr>
<tr>
<td>3</td>
<td>Detroit</td>
<td>31,127</td>
<td>40,414</td>
<td>9,287</td>
<td>29.8</td>
</tr>
<tr>
<td>4</td>
<td>Philadelphia</td>
<td>39,551</td>
<td>49,334</td>
<td>9,783</td>
<td>24.7</td>
</tr>
<tr>
<td>5</td>
<td>Los Angeles</td>
<td>56,109</td>
<td>67,043</td>
<td>10,934</td>
<td>19.5</td>
</tr>
<tr>
<td>6</td>
<td>NEW YORK CITY</td>
<td>$453,361</td>
<td>$453,088</td>
<td>--$ 273</td>
<td>-- 0.1%</td>
</tr>
<tr>
<td></td>
<td>Five City Total</td>
<td>$135,780</td>
<td>$240,184</td>
<td>$54,404</td>
<td>29.3%</td>
</tr>
<tr>
<td></td>
<td>All US Cities</td>
<td>$1,499,654</td>
<td>$2,062,519</td>
<td>$562,865</td>
<td>37.5%</td>
</tr>
</tbody>
</table>

NOTES:

a. Reported total monthly payroll costs (including overtime shift differential, part-timers, etc.) in October of 1974 and 1978, unless otherwise noted.

b. Higher education payroll as of October, 1977. Does not reflect the October 1, 1978 4% wage increase due to its delayed implementation. An overall 4% increase would amount to $18,124 bringing the 1979 monthly payroll figure to $471,212; and the 1975-1979 change to $17,851 or 3.9%.

c. Not including New York City or Baltimore.


Financing

In the financing of the City substantial progress has also occurred. While it has not regained access in the public credit markets for its long-term debt, it has accomplished the following:

- obtained seasonal financing from the public credit markets in FY 1979 and FY 1980;
- reduced its seasonal needs from $8.4 billion in FY 1975 to under $600 million in FY 1980;
- eliminated an $800 million advance of State aid;
- ended FY 1978 and FY 1979 with the highest working capital in the last 10 years.

Table 1 (pg. 2) examines the amount of short-term debt issued by the City as a percentage of its operating expenses over the last 40 years. The amount issued in FY 1979 was the lowest in aggregate dollars since FY 1958. It represents the lowest percentage to operating expenses in the past 40 years. It emphasizes an increasing municipal ability to match more evenly revenues and expenses.

As a result, the City has been able to reduce its interest costs on a permanent basis, i.e., had the City issued the same amount of short-term debt in FY 1979 as it did in FY 1978 it would have had an additional operating expense of almost $50 million.

-19-
Reduced seasonal borrowing needs will mean easier access to the public markets. The less overall debt to be issued in one year, the lower the interest cost and the easier it is to sell the securities due to the desirability of a triple-tax exempt security.

The ratio of short-term debt to operating expense stresses the following factors:

1. The City no longer has deficit financing.
2. The City is issuing debt only against revenues which will be collected later in the year and not against revenue of Federal/State programs not yet enacted.
3. The City is funding current expenses with current revenues.

New York's seasonal borrowings as a percentage of operating budget is significantly less than that of other major governments in the State.

Table 13
Seasonal Financing as % of Operating Budget
by 1979
($ in millions)

<table>
<thead>
<tr>
<th></th>
<th>Amount Borrowed</th>
<th>Operating Budget</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>New York State</td>
<td>$2,990</td>
<td>$14,165</td>
<td>21%</td>
</tr>
<tr>
<td>Nassau County</td>
<td>$56</td>
<td>$186</td>
<td>30%</td>
</tr>
<tr>
<td>Buffalo</td>
<td>$227 (est.)</td>
<td>$594</td>
<td>38%</td>
</tr>
<tr>
<td>NEW YORK CITY</td>
<td>$650</td>
<td>$13,580</td>
<td>5%</td>
</tr>
</tbody>
</table>

Source: Official Statement for each government unit.
The City's beginning cash balance has improved substantially in the last two years. The following table shows the amount of cash the City had on July 1, and the seasonal financing or pre-paid taxes which were included in that opening balance. If the City's cash balance at the beginning of the year is the result of borrowing funds or the pre-payment of revenues (pre-paid real estate taxes or outstanding seasonal financing), then the City's cash position for that year is weaker, its operating costs higher, and its seasonal financing requirements greater.
Table 14

New York City
Cash July 1
($ in millions)

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Cash 7/1</th>
<th>Funds Borrowed or Pre-Paid Taxes Contributing to 7/1 Balance</th>
<th>Cash Less Contributions to Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>1971</td>
<td>$101</td>
<td>$1,288</td>
<td>($1,187)</td>
</tr>
<tr>
<td>1972</td>
<td>304</td>
<td>2,319</td>
<td>(2,015)</td>
</tr>
<tr>
<td>1973</td>
<td>580</td>
<td>2,650</td>
<td>(2,070)</td>
</tr>
<tr>
<td>1974</td>
<td>214</td>
<td>2,517</td>
<td>(2,303)</td>
</tr>
<tr>
<td>1975</td>
<td>55</td>
<td>3,415</td>
<td>(3,360)</td>
</tr>
<tr>
<td>1976</td>
<td>512</td>
<td>4,540</td>
<td>(4,028)</td>
</tr>
<tr>
<td>1977</td>
<td>158</td>
<td>- a</td>
<td>158</td>
</tr>
<tr>
<td>1978</td>
<td>478</td>
<td>- a</td>
<td>478</td>
</tr>
<tr>
<td>1979</td>
<td>1,082</td>
<td>321</td>
<td>761</td>
</tr>
<tr>
<td>1980</td>
<td>807</td>
<td>87</td>
<td>720</td>
</tr>
</tbody>
</table>

NOTES: a. Notes in moratorium were $2,071 million in FY1977 and $1,027 million in FY1978.

SOURCE: N.Y.C. Comptroller Reports

A major accomplishment in the financing area was the elimination of the short-term debt outstanding on July 1, 1975, -- $4.54 billion. Table 15 shows how this debt was paid off in the course of three years. This occurred in the FY1976-FY1978 period while the City also was eliminating a GAAP budget deficit of over $1 billion.
<table>
<thead>
<tr>
<th>Redemption of Short-Term Notes Outstanding as of 7/1/75 ($ in millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Outstanding 7/1/75</td>
</tr>
<tr>
<td>Paid by New York City¹</td>
</tr>
<tr>
<td>FY 1976</td>
</tr>
<tr>
<td>FY 1977</td>
</tr>
<tr>
<td>FY 1978</td>
</tr>
<tr>
<td>Public Exchange for MAC bonds</td>
</tr>
<tr>
<td>FY 1976</td>
</tr>
<tr>
<td>FY 1977</td>
</tr>
<tr>
<td>Retirement System Exchange</td>
</tr>
<tr>
<td>City bonds</td>
</tr>
<tr>
<td>MAC bonds</td>
</tr>
<tr>
<td>City Clearinghouse Bank Exchange for MAC bonds</td>
</tr>
<tr>
<td>Summary</td>
</tr>
<tr>
<td>Outstanding 7/1/75</td>
</tr>
<tr>
<td>Redeemed</td>
</tr>
<tr>
<td>Cash¹</td>
</tr>
<tr>
<td>City Bonds</td>
</tr>
<tr>
<td>MAC bonds</td>
</tr>
<tr>
<td>Outstanding 6/30/78</td>
</tr>
</tbody>
</table>

Source: New York City Comptroller Reports, MAC Annual Statements, City Financial Plans

Note

1. Part of the payment was provided by the sale of MAC bonds.
FEDERAL AID

In FY 1976 the City had a deficit (under GAAP) of $1,822 million. Unrestricted Federal aid (Federal revenue sharing) was $263 million. In FY 1979 the City had reduced its deficit to $422 million, and unrestricted Federal aid was $302 million. In FY 1980 the City will receive $292 million of unrestricted Federal aid. This represents a growth of $29 million, or 11%, in four years. Had this assistance grown with inflation it would have been $352 million.

A similar result occurred with Federal grants. As indicated in the following table, should the City's current projections be realized, by FY 1983 the Federal aid received by the City would have decreased in real dollar terms by 9%.

Table 16

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Federal Aid</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Grants</td>
<td>$2,327</td>
<td>$2,421</td>
<td>$2,534</td>
<td>$2,208</td>
<td>$2,214</td>
<td>$2,301</td>
<td>$2,357</td>
<td>$2,416</td>
</tr>
<tr>
<td>Less: Medicaid</td>
<td>628</td>
<td>628</td>
<td>693</td>
<td>290</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Adj. Grants</td>
<td>$1,699</td>
<td>$1,793</td>
<td>$1,931</td>
<td>$1,918</td>
<td>$2,214</td>
<td>$2,301</td>
<td>$2,357</td>
<td>$2,416</td>
</tr>
<tr>
<td>Revenue Sharing</td>
<td>263</td>
<td>291</td>
<td>305</td>
<td>302</td>
<td>292</td>
<td>296</td>
<td>296</td>
<td>295</td>
</tr>
<tr>
<td>Countercyclical</td>
<td>-</td>
<td>89</td>
<td>142</td>
<td>15</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Total</td>
<td>$1,962</td>
<td>$2,173</td>
<td>$2,378</td>
<td>$2,235</td>
<td>$2,506</td>
<td>$2,597</td>
<td>$2,653</td>
<td>$2,711</td>
</tr>
</tbody>
</table>
| Constant Dollars | FY 1976 = 100 | $1,962 | $2,062 | $2,149 | $1,893 | $1,984 | $1,921 | $1,835 | $1,776 - 9%
a. Medicaid funds received from the Federal government were originally included in the City's budget. In FY 1976 this was approximately $628 million. This amount was the FY 1975 amount reported in the City Comptroller's Annual Report for FY 1975. Data for FY 1976 and FY 1977 was not available. Beginning with FY 1978 the City began to eliminate the budgeting for this, and eliminated $313 million in that year ($603-$313 = $290). This was entirely eliminated in FY 1980 and thereafter. The Federal Grants have been adjusted to eliminate the Medicaid amounts contained in the budget each year from FY 1976-FY 1979.
While Federal aid to New York City has decreased in real terms Federal policy has continued to have a negative impact on the City. In FY 1979 the City spent $967 million of its tax-levy funds for medicaid and public assistance. In FY 1980 this will be $952 million. This represents the combined tax-levy funds the City will spend on providing police and fire services in the City in FY 1980.

As indicated in the following tables (17 and 18) the public and medical assistance burden mandated upon the City far exceeds that of other cities in the United States. The failure of the national government to reform the financing of these two programs is borne by the localities that must continue to meet its social obligations.

Special education represents a classic example of Federal policy that may be socially correct but puts the burden of funding the program on the level of government least able to afford it. Federal law (P.L. 94-142) required cities to provide adequate education to handicapped children. In FY 1980 the program will cost $427 million. It is projected that by FY 1983 the cost will increase to $533 million, an increase of 37%. The City's share of the cost will increase by 71% in that time period ($221 million to $377 million).
<table>
<thead>
<tr>
<th>State</th>
<th>Federal Government Contribution</th>
<th>State Government Contribution</th>
<th>Local Government Contribution</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alabama</td>
<td>65.00%</td>
<td>35.00%</td>
<td>-</td>
</tr>
<tr>
<td>Alaska</td>
<td>50.00</td>
<td>50.00</td>
<td>-</td>
</tr>
<tr>
<td>Arizona</td>
<td>56.46</td>
<td>43.54</td>
<td>-</td>
</tr>
<tr>
<td>Arkansas</td>
<td>65.00</td>
<td>35.00</td>
<td>-</td>
</tr>
<tr>
<td>California</td>
<td>50.00</td>
<td>50.00 b</td>
<td>-</td>
</tr>
<tr>
<td>Colorado</td>
<td>53.71</td>
<td>26.29</td>
<td>20.00</td>
</tr>
<tr>
<td>Connecticut</td>
<td>50.00</td>
<td>50.00</td>
<td>-</td>
</tr>
<tr>
<td>Delaware</td>
<td>50.00</td>
<td>50.00</td>
<td>-</td>
</tr>
<tr>
<td>D. of Columbia</td>
<td>50.00</td>
<td>50.00</td>
<td>-</td>
</tr>
<tr>
<td>Florida</td>
<td>51.72</td>
<td>48.28</td>
<td>-</td>
</tr>
<tr>
<td>Georgia</td>
<td>62.02</td>
<td>37.98</td>
<td>-</td>
</tr>
<tr>
<td>Guam</td>
<td>50.00</td>
<td>50.00</td>
<td>-</td>
</tr>
<tr>
<td>Hawaii</td>
<td>50.00</td>
<td>50.00</td>
<td>-</td>
</tr>
<tr>
<td>Idaho</td>
<td>50.53</td>
<td>40.47</td>
<td>-</td>
</tr>
<tr>
<td>Illinois</td>
<td>50.00</td>
<td>50.00</td>
<td>-</td>
</tr>
<tr>
<td>Indiana</td>
<td>53.18</td>
<td>23.09</td>
<td>18.72</td>
</tr>
<tr>
<td>Iowa</td>
<td>50.00</td>
<td>50.00</td>
<td>-</td>
</tr>
<tr>
<td>Kansas</td>
<td>52.35</td>
<td>47.65</td>
<td>-</td>
</tr>
<tr>
<td>Kentucky</td>
<td>65.00</td>
<td>35.00</td>
<td>-</td>
</tr>
<tr>
<td>Louisiana</td>
<td>65.00</td>
<td>35.00</td>
<td>-</td>
</tr>
<tr>
<td>Maine</td>
<td>65.00</td>
<td>35.00</td>
<td>-</td>
</tr>
<tr>
<td>Maryland</td>
<td>50.00</td>
<td>50.00</td>
<td>-</td>
</tr>
<tr>
<td>Massachusetts</td>
<td>50.00</td>
<td>50.00</td>
<td>-</td>
</tr>
<tr>
<td>Michigan</td>
<td>50.00</td>
<td>50.00</td>
<td>-</td>
</tr>
<tr>
<td>Minnesota</td>
<td>50.29</td>
<td>29.82</td>
<td>19.88</td>
</tr>
<tr>
<td>Mississippi</td>
<td>65.00</td>
<td>35.00 c</td>
<td>-</td>
</tr>
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**NOTES:**


b. Prior to 1979, there was a mandated local government share of 16.25%. Since the passage of the "Proposition 13 Emergency Bailout Legislation," the State of California has assumed all local ADC costs. Pending legislation if passed would formalize this new financial arrangement.

c. Counties contribute to administrative costs according to ability to pay.

d. State contributes 6.5% to county administrative costs, 50.0% to state.

e. Counties contribute 43.5% to county administrative costs.

f. State contributes 30% and local governments 20% to administrative costs.

g. Minimum State contribution.

h. Maximum county contribution.


Telephone conversation between Program Planners, Inc., and Mrs. Katherine Miller of the State Plans and Program Characteristics Branch, Office of Management Services, Family Assistance Office, Social Security Administration, 3/14/79.
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<th>State</th>
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<td>Local Government Contribution</td>
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<td>46.56%</td>
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</table>
NOTE:


b. Arizona has no Medicaid program.

c. Prior to 1979, there was a mandated local government share of 12.5%. Since the passage of the "Proposition 13 Emergency Bailout Legislation," the State of California has assumed all local Medicaid costs. Pending legislation if passed would formalize this new financing arrangement.

d. Prior to 1975, there was a mandated local government share.

e. Local counties cover 35% of the nonfederal costs of inpatient hospital care in excess of 12 days up to 45 days; and 35% of the cost of nursing home care in excess of $170.00/month, not to exceed $55.00/month.

f. Prior to 1969, there was a mandated local government share.

g. Prior to 1975, there was a mandated local government share.

h. Local governments contribute towards administrative expenses. This share is estimated at 1.78% for the period 10/1/77 to 9/30/79.

i. Local governments contribute towards 10% of total administrative costs.

j. Local governments contribute only towards the nonfederal share of nursing home care.


In addition, correspondence between specific state medical assistance directors and Program Planners, Inc.
Federal law provided that contributions by the Federal government for the program is to be based upon the per pupil expenditure for non-handicapped children in school. The percentage would range between 5% in 1977 to 40% in 1982. Despite the authorization permitting an increase in Federal funds, Congress has appropriated only 12% for 1980 and 1981. Had Congress appropriated the full amount for a program which is mandated on the City, then it would have meant an additional $25 million to the City in FY 1982.

Transit financing is another illustration of how New York City must bear the burden of Federal discrimination against urban areas. A rational approach in this area would not only assist urban areas but the entire nation because it would promote energy efficiency and conservation. To do this would require the formula which is used allocate Federal transit operating assistance (P.L. 93-503) be based upon mass transit dependence within an area. At this time in the history of the United States a policy of incentives for energy conservation and efficiency must be promoted. The current transit allocation formula, based upon population and population density, is outmoded and counterproductive to a required and rational national policy.
Table 19 indicates how New York City is penalized for having a transit system that is in the nation's best interests. New York receives 6.4¢ per rider in Federal assistance, while Omaha, Nebraska, servicing a population which is approximately 0.5% of New York's, receives almost 381% more per rider in Federal assistance.

New York's reliance on Federal assistance for operating purposes is far less than other major cities (see Table 20).

Table 21 indicates total Federal operating assistance allocations for FY 1979 and the amount received by the NYCTA. Also included in Table 21 is calendar 1978 national ridership. As can be seen, the NYCTA is the recipient of 11% of available appropriated Federal operating assistance while it generates 23.0% of all public transportation ridership. If the NYCTA had received 23.0% of appropriated Section 5 monies, then an additional $129 million would have been realized.
<table>
<thead>
<tr>
<th>Rank</th>
<th>City/System</th>
<th>Section 5 Operating Assistance</th>
<th>Annual Ridership</th>
<th>Operating Assistance Per Rider</th>
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<td>Phoenix</td>
<td>1,941,754</td>
<td>7,562,624</td>
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<td>Detroit/DRT</td>
<td>16,837,094</td>
<td>66,616,000</td>
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<tr>
<td>4</td>
<td>Columbus/COTA</td>
<td>3,584,100</td>
<td>14,929,889</td>
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<tr>
<td>5</td>
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<td>5,964,616</td>
<td>29,800,000</td>
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<tr>
<td>6</td>
<td>Indianapolis/ITC</td>
<td>2,549,143</td>
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<tr>
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<td>8</td>
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<td>9</td>
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<td>32,700,000</td>
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<td>Boston/MBTA</td>
<td>26,628,396</td>
<td>159,240,000</td>
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<td>14</td>
<td>Miami-Dade/Miami-Dade</td>
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<td>15</td>
<td>Washington/ATA</td>
<td>17,800,000</td>
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<td>16</td>
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<td>17</td>
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<td>19</td>
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<td>20</td>
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<td>21</td>
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**NOTE:**
1. 1976 unless otherwise noted.

**Source:** Annual reports of cooperative systems; newsclippings.
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<th>Rank</th>
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<th>FTA as Percent of Total Revenue</th>
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<td>Los Angeles/SCCRA</td>
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<td>3</td>
<td>Omaha/MAK</td>
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<td>4</td>
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<td>5</td>
<td>Detroit/DOT</td>
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<td>6</td>
<td>Indianapolis/PAC</td>
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</tr>
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<td>7</td>
<td>Cincinnati/SOCTA</td>
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**Note:**

1. 19/9

Source: Respective annual reports; news clippings.
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<td>Total</td>
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Calendar 1978 Ridership

<table>
<thead>
<tr>
<th></th>
<th>National</th>
<th>NYCTA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rapid Transit</td>
<td>1,506.0</td>
<td>1,047.9</td>
</tr>
<tr>
<td>Bus</td>
<td>4,457.0</td>
<td>333.9</td>
</tr>
<tr>
<td>Total</td>
<td>5,963.0</td>
<td>1,371.8</td>
</tr>
</tbody>
</table>

**Note:**

a. Of this amount, $14.0 million is being carried into fiscal 1980.

**Source:** NYCTA Operating Budget FY 1979, American Public Transit Association, District Mass Transportation Administration.
New York City Retirement Systems

In 1975 the representatives of the City's five retirement systems sought Federal legislation that permitted the Retirement Systems to purchase City securities in fiscal years 1976-1978. Federal legislation was required so that the purchases would not violate the prohibited transactions (Section 503b) and exclusive benefits rule (Section 401a) of the Internal Revenue Code. At that time it was stated that the investment was being undertaken because the bankruptcy of New York City would result in the eventual bankruptcy of the Retirement Systems. Purchases of City securities would lead to a stronger system and would delay eventual bankruptcy even if the City followed that course.

With the expiration of the Federal legislation in 1978, and the City still lacking the means to finance itself, a renewal of Federal legislation was sought. In addition, the trustees of the Retirement System sought additional security for the City bonds - a Federal guarantee of repayment in the event of default by the City. In one of the most complex financing arrangements in governmental history, the Retirement Systems entered into agreements to purchase $1 billion of City and Municipal Assistance Corporation securities over a four year period.
Without the investments of the City Retirement Systems in the last five years the City would have been bankrupt. From FY 1975 - FY 1978 the Retirement Systems were the sole financiers for the City. Without participation by the Retirement Systems in the FY 1979-FY 1982 Agreement, the other parties (State Retirement Systems and City financial institutions) stated that they would not participate in any financing agreement.

In retrospect the decisions made by the Trustees were correct. The City is now approaching the point where the financial investment of the Retirement Systems will no longer be required. Bankruptcy has not occurred and during the last five years the Retirement Systems have been significantly strengthened.

The City and MAC securities actions taken by the Retirement Systems are set forth in detail in Tables 23 to 24. During the last five years the Retirement Systems have purchased over $4 billion of City and MAC securities, exchanged $301.5 million of City notes for City/MAC bonds, and re-invested $360.0 million of maturing City obligations.

While providing this major financing role for the City, the Systems have also made financial progress. The
Table 22
New York City Retirement Systems
FY 1976 - FY 1980
Transactions in New York City/MAC Securities
($ in millions)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purchase MAC Bonds</td>
<td>$ 949.4</td>
</tr>
<tr>
<td>Purchase City Bonds</td>
<td>2,575.0</td>
</tr>
<tr>
<td>Total Purchases</td>
<td>$3,524.4</td>
</tr>
<tr>
<td>Re-investment in City Bonds</td>
<td>$ 360.8</td>
</tr>
<tr>
<td>Exchange of City Note for City Bond</td>
<td>30.0</td>
</tr>
<tr>
<td>Exchange of City Note for MAC Bonds</td>
<td>271.5</td>
</tr>
<tr>
<td>Purchase Short-Term MAC Notes</td>
<td>335.5</td>
</tr>
<tr>
<td>Purchase Short-Term City Notes</td>
<td>192.5</td>
</tr>
<tr>
<td>Total</td>
<td>$4,714.7</td>
</tr>
</tbody>
</table>

Purchases of Securities                    | $4,952.4 |
Exchange of Notes                           | 301.5    |
Re-investment                               | 360.8    |
                                                | $4,714.7 |
### Table 23

New York City Retirement Systems  
FY 1976 -- FY 1980  
Transactions in New York City/MAC Securities  
($ in millions)

#### Short-Term

<table>
<thead>
<tr>
<th>Date</th>
<th>Security</th>
<th>Amount</th>
<th>Interest Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>6/20/78</td>
<td>MAC Note</td>
<td>$335.5</td>
<td>7.5%</td>
</tr>
<tr>
<td>12/28/78</td>
<td>City Note</td>
<td>125.0</td>
<td>9.5%</td>
</tr>
<tr>
<td>3/21/79</td>
<td>City Note</td>
<td>67.5</td>
<td>9.5%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td><strong>$528.0</strong></td>
<td></td>
</tr>
<tr>
<td>Date</td>
<td>Security</td>
<td>Amount</td>
<td>Interest Rate</td>
</tr>
<tr>
<td>----------</td>
<td>------------</td>
<td>--------</td>
<td>---------------</td>
</tr>
<tr>
<td>8/21/75</td>
<td>MAC Bond</td>
<td>$165.0</td>
<td>11%</td>
</tr>
<tr>
<td>9/5/75</td>
<td>MAC Bond</td>
<td>100.0</td>
<td>9% - 11%</td>
</tr>
<tr>
<td>9/15/75</td>
<td>MAC Bond</td>
<td>41.5</td>
<td>9% - 11%</td>
</tr>
<tr>
<td>9/25/75</td>
<td>MAC Bond</td>
<td>63.0</td>
<td>9 1/2% - 11%</td>
</tr>
<tr>
<td>10/9/75</td>
<td>MAC Bond</td>
<td>22.0</td>
<td>9%</td>
</tr>
<tr>
<td>10/17/75</td>
<td>MAC Bond</td>
<td>177.0</td>
<td>11%</td>
</tr>
<tr>
<td>11/10/75</td>
<td>MAC Bond</td>
<td>31.0</td>
<td>11%</td>
</tr>
<tr>
<td>11/20/75</td>
<td>MAC Bond</td>
<td>14.5</td>
<td>11%</td>
</tr>
<tr>
<td>12/1/75</td>
<td>City Bond</td>
<td>130.0</td>
<td>9%</td>
</tr>
<tr>
<td>12/15/75</td>
<td>City Bond (1)</td>
<td>30.0</td>
<td>6%</td>
</tr>
<tr>
<td>12/15/75</td>
<td>City Bond</td>
<td>185.0</td>
<td>9%</td>
</tr>
<tr>
<td>3/15/76</td>
<td>City Bond</td>
<td>185.0</td>
<td>9%</td>
</tr>
</tbody>
</table>

**TOTAL PURCHASES** **FY 1976**

<table>
<thead>
<tr>
<th>Date</th>
<th>Security</th>
<th>Amount</th>
<th>Interest Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>7/1/76</td>
<td>City Bond</td>
<td>$125.0</td>
<td>9%</td>
</tr>
<tr>
<td>9/1/76</td>
<td>City Bond</td>
<td>250.0</td>
<td>9%</td>
</tr>
<tr>
<td>11/15/76</td>
<td>City Bond</td>
<td>180.0</td>
<td>9%</td>
</tr>
<tr>
<td>5/20/77</td>
<td>City Bond</td>
<td>255.0</td>
<td>9%</td>
</tr>
<tr>
<td>5/20/77</td>
<td>City Bond</td>
<td>245.0</td>
<td>9%</td>
</tr>
<tr>
<td>6/6/77</td>
<td>City Bond (2)</td>
<td>381.8</td>
<td>9%</td>
</tr>
</tbody>
</table>

**TOTAL PURCHASES** **FY 1977** $1,386.0
<table>
<thead>
<tr>
<th>Date</th>
<th>Security</th>
<th>Amount</th>
<th>Interest Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>11/28/77</td>
<td>City Bond (3)</td>
<td>$ 53.4</td>
<td>9%</td>
</tr>
<tr>
<td>6/29/78</td>
<td>City Bond (4)</td>
<td>564.6</td>
<td>9%</td>
</tr>
<tr>
<td><strong>TOTAL PURCHASES FY 1978 (6)</strong></td>
<td></td>
<td>$ 617.0</td>
<td></td>
</tr>
<tr>
<td>8/25/79</td>
<td>City Bonds (5)</td>
<td>$106.0</td>
<td>9%</td>
</tr>
<tr>
<td>11/17/79</td>
<td>MAC Bonds</td>
<td>60.4</td>
<td>8.3/8%</td>
</tr>
<tr>
<td>11/17/79</td>
<td>City Bonds</td>
<td>50.0</td>
<td>8.9%</td>
</tr>
<tr>
<td>2/15/79</td>
<td>City Bonds</td>
<td>100.0</td>
<td>9.5%</td>
</tr>
<tr>
<td><strong>TOTAL PURCHASES FY 1979</strong></td>
<td></td>
<td>$ 316.4</td>
<td></td>
</tr>
<tr>
<td>8/15/79</td>
<td>MAC Bonds</td>
<td>$ 74.0</td>
<td>7.88%</td>
</tr>
<tr>
<td>8/15/79</td>
<td>City Bonds</td>
<td>100.0</td>
<td>9.25%</td>
</tr>
<tr>
<td>12/15/79</td>
<td>MAC Bonds</td>
<td>150.0</td>
<td>8.75%</td>
</tr>
<tr>
<td>1/2/80</td>
<td>City Bonds</td>
<td>75.0</td>
<td>10.75%</td>
</tr>
<tr>
<td><strong>TOTAL PURCHASES (as of 1/3/80) FY 1980</strong></td>
<td></td>
<td>$ 399.0</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>TOTAL LONG-TERM PURCHASES FY 1976 - FY 1980</strong></td>
<td></td>
<td>$3,913.4</td>
</tr>
</tbody>
</table>

**NOTES:**
1. Exchange of City note
2. Re-investment of maturing City Bonds $136.8 million
3. Re-investment of maturing City Bonds $53.4 million
4. Re-investment of maturing City Bonds $64.6 million
5. Re-investment of maturing City Bonds $106.0 million
6. Not reflected is the exchange of City notes ($271.5 million) for MAC bonds and the refinancing of the $886 million MAC bonds held in the Retirement Systems on August, 1975.
average yield of securities held by the Systems has increased from 5.3% in 1975 to 7.4% in 1979. The assets of the Systems have grown from $8.250 million in 1975 to $11.750 million in 1980, a 42% growth. In the course of the last 4 years, with the absence of City bankruptcy, the City and its employees have contributed $5.5 billion, investment income has been $2.3 billion, and the benefits paid to members have been $4.1 billion. None of this would have been possible if the Trustees of the Retirement Systems had not taken necessary actions from 1975-1980.

In the last five years the City's Retirement Systems have become the leading public systems in terms of adequacy of funding, fiscal prudence, and fiscal responsibility. As a result of a commission appointed by Mayor Beame in 1976 major reforms were undertaken to make the systems actuarially sound. The Commission recommended, and the City implemented, a plan which updated the actuarial assumptions used by the systems and changed the actuarial funding method to insure proper amortization.

The only system which has not been strengthened is the Fire Pension Fund. A dispute between the City and the
labor unions which dates back to 1952 prevents the system from being in the same financially secure position as the other systems. Without a change in the current situation the Fire Pension Fund will be bankrupt in 1990. A solution would not only be less costly for the City in the long-run, but will eliminate a problem often cited by investors.

What of the future?

We expect that the Retirement Systems will have 23% of their assets in City and City related paper at the end of FY 1982. At that time the City should return to the public credit markets for its financing, even if such financing is less than is currently contemplated. It is not expected that the Retirement Systems will return to Congress to seek an extension of Federal legislation.
MARKET ACCESS

The last public sale of general obligation bonds that the City accomplished took place on February 15, 1975. Since that time the City has painstakingly had to rebuild its credibility in the public financing markets. This meant:

- the creation of an outside vehicle (M.A.C.) to assist the City;
- purchases of securities by negotiated commitments (City and State Retirement Systems, New York City Financial institutions);
- absorption and financing of an $800 million state advance;
- the reduction of seasonal financing needs from $2.1 billion to less than $600 million;
- the provision of seasonal needs by the Federal government, and then by the City's retirement systems and financial institutions;
- obtaining a loan facility with over 40 banks that would provide seasonal financing assistance if public financing were not available;
- public sales of short-term notes, secured by expected revenue from the State.

All of these steps indicate substantial progress, but the goal of public sales of long-term securities
appears to be difficult to attain. There are three reasons, among others, for this: the rating agencies, the City's oversight bodies, and the size of the financing that the City requires.

Rating Agencies
The market experts indicate that unless the City is able to receive an investment grade rating from the two municipal securities rating agencies then the City will be unable to regain access to the public credit markets.

Is it proper public policy for the financial fate of the largest City in the United States to be dependent upon an analysts viewpoint? Should the 7 million people who receive services in this City be at the mercy of unknown, anonymous, credit analysts? Who are the rating agencies accountable to?

It is not being suggested that the Federal government regulate the industry, but rather that if such substantial power is being concentrated in an institution then that institution must be responsive to public needs.

In May, 1979, the City's credit rating was reviewed by Moody's Investor's Service, Inc. The securities were rated B, a rating below the investment grade. In reviewing the Report it was found to be inaccurate, failed
to take into consideration the progress the City had made, and was inconsistent with prior statements made by Moody's.

The Report states that the City's debt (combined with MAC debt) is $15.8 billion. As the City Comptroller has indicated, this overstates the true net debt by $3.2 billion. The following table, utilizing the data supplied by the Comptroller, details the errors made.

NYC Debt as of March, 1979

<table>
<thead>
<tr>
<th></th>
<th>Moody</th>
<th>Actual Debt Position 3/31/79</th>
<th>Adjustment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Funded debt</td>
<td>$ 7,378.5</td>
<td>$ 6,641.5</td>
<td>a) 737.0</td>
</tr>
<tr>
<td>Debt issued since 6/30/78</td>
<td>456.0</td>
<td>( 280.4)</td>
<td>b) 736.4</td>
</tr>
<tr>
<td>Unfunded Debt</td>
<td>1,013.8</td>
<td>-</td>
<td>c) 1,013.8</td>
</tr>
<tr>
<td>Public Benefit Corporation Debt</td>
<td>1,104.0</td>
<td>951.7</td>
<td>d) 152.3</td>
</tr>
<tr>
<td>MAC Debt</td>
<td>5,882.4</td>
<td>5,349.2</td>
<td>e) 533.2</td>
</tr>
<tr>
<td></td>
<td>$15,834.7</td>
<td>$12,662.0</td>
<td></td>
</tr>
</tbody>
</table>

NOTES:

a. Sinking funds assets at 3/31/79
b. City bonds redeemed in FY 1979
c. RWU's held by MAC
d. MAC assets available for debt service
e. MAC assets available for redemption of Bonds.

Source: NYC Office of the Comptroller.
In June, 1977 Moody's issued a credit report which gave the New York City General Obligation Bonds a B rating. Reviewing past history and further prospects of the City, Moody's indicated certain long-term problems facing the City and certain structural problems which had to be overcome.

Reviewing the issues raised then, and the steps already taken by May, 1979:

1 - Temporary expedients were made in the past to generate a sufficient cash flow (e.g. advance of State aid, deferral of wage contracts, Federal Credit Agreement)

PROGRESS: The City ended June 30, 1978 with over a $1 billion cash balance. On June 30, 1979 it had a cash balance of $823 million. The City has eliminated the advance of State aid and has successfully sold notes in the short-term public credit market in FY 1979 and in FY 1980.

2 - Since the City used bonds to pay for current expenses in FY 1975 of $695 million and will issue bonds of $713 million in FY 1978, no progress was being made to eliminate this practice.
PROGRESS: The City in FY 1980 will bond $185 million of operating expenses. By FY 1981 all operating expenses not permitted to be bonded will be eliminated from the capital budget. This is required by Federal and State legislation.

3 - The City required adjustments to its revenue structure in order to lighten the tax burden for various classes of taxpayers.

PROGRESS: The City has capped (until FY 1980) the real estate tax rate at $8.75/$100 of assessed value. It also:

1 - reduced the commercial rent tax by 10%;

2 - reduced the general corporation tax from 10.05% to 9%; and,

3 - will be eliminating the stock transfer tax over a 4 year period.

4 - City must restructure its current and capital liabilities.

PROGRESS: The City has eliminated $800 million of liabilities in the form of the State advance, and the RAN's held by MAC have been the subject of an agreement between
the City and MAC by which the City
issued bonds to MAC.

5 - The average maturity of the City bonds is short be-
cause of the State legislative limit which requires
the City to make a downpayment of 5% (from operating
expenses) for a capital project in the year it is
started, or to issue bonds for only one-half the
amortization period it otherwise would be able to.

PROGRESS: The State legislature suspended the
major downpayment limit in 1978 for a
period of 4 years. This will permit the
City to issue bonds for the full amor-
tization period without making any down-
payment.

6 - The City lacks a sufficient procedure for financing
expenditures for unforeseen emergencies and for casual
overexpenditures of appropriations.

PROGRESS: The City is required by State law to
have a $100 million reserve each year
for unforeseen expenditure increases
or revenue losses. In addition, re-
serves for disallowances of Federal/
State aid and real estate taxes are
established. Further Sec. 9b(5) of
the FAA requires all budget notes
(which can be used to finance emergency or unforeseen expenditures) to be redeemed within 10 months of the fiscal year after which they were issued. This changes the 1971 law which permitted the City more than 3 years to redeem such notes.

The May, 1979 Report failed to note that these problems, cited two years earlier, have been resolved. It seems that Moody's escalates its criteria for re-entry as the City moves forward.

Oversight Agencies

New York City is subject to the scrutiny of numerous public and private oversight organizations:

- the office of the Special Deputy State Comptroller
- the Municipal Assistance Corporation
- the Financial Control Board
- the United States Treasury Department
- the United States Senate and House Banking Committees
- the accountants, auditors, and consultants affiliated with all of the above.

The reports and prognostications made by all of them has had, and will continue to have, an impact on the City's access to the public credit markets. The considerable weight given to these agencies requires that
the degree of accuracy of their statements and positions be measured. Their past forecasts should be reviewed with actual events and developments so that the investing public can determine the degree of reliance to be placed on their utterances.

The City is held accountable in the public's mind for the accuracy of its forecasts and its ability to plan ahead. The oversight agencies must be held to some standard because their judgements are not always accurate. Currently their judgments are afforded as much, if not more, weight than the City's. This should occur only if they exhibit better judgment.

As an example of what has occurred, we reviewed the FY 1979 projections made by the Office of the Special Deputy Comptroller. Its 50 plus member staff provides detailed analyses to the State Comptroller, the Financial Control Board, the Municipal Assistance Corporation, various Congressional committees, and the media.

Beginning March 27, 1978, OSDC projected the following results for the City's FY 1979:
<table>
<thead>
<tr>
<th>Date of Projection (Document #)</th>
<th>Estimate ($ in millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2/28/78 (FCB 77-78)</td>
<td>$345 deficit</td>
</tr>
<tr>
<td>6/06/78 (FCB 23-79)</td>
<td>$98 deficit</td>
</tr>
<tr>
<td>8/14/78 (FCB 44-79)</td>
<td>$289 deficit</td>
</tr>
<tr>
<td>11/08/79 (FCB 75-79)</td>
<td>$255 deficit</td>
</tr>
<tr>
<td>1/08/79 (FCB 102-79)</td>
<td>$211 deficit</td>
</tr>
<tr>
<td>2/13/79 (FCB 117-79)</td>
<td>$154 deficit</td>
</tr>
<tr>
<td>6/01/79 (FCB 24-80)</td>
<td>$67 surplus</td>
</tr>
<tr>
<td>Actual</td>
<td>$216 surplus</td>
</tr>
</tbody>
</table>

Difference 2/28/78 projected deficit to actual surplus: $561

Comparing the estimate made after the adopted FY 1979 PP (contained in FCB 44-79, 8/14/78) in terms of the dollar amount of error:
Table 25

New York City

FY1979

Actual vs. Estimate

($ in millions)

<table>
<thead>
<tr>
<th>Revenues:</th>
<th>Actual</th>
<th>OSDC Estimate</th>
<th>Dollar Amount of Error</th>
</tr>
</thead>
<tbody>
<tr>
<td>Taxes</td>
<td>$7,243</td>
<td>$7,206</td>
<td>$37</td>
</tr>
<tr>
<td>Misc. Federal/State Aid(^a)</td>
<td>54</td>
<td>(18)</td>
<td>72</td>
</tr>
<tr>
<td>Unrestricted State Aid</td>
<td>530</td>
<td>519</td>
<td>11</td>
</tr>
<tr>
<td>Unrestricted Federal Aid</td>
<td>318</td>
<td>423</td>
<td>105</td>
</tr>
<tr>
<td>Proceeds from Capital Budget</td>
<td>502</td>
<td>524</td>
<td>22</td>
</tr>
<tr>
<td><strong>Error</strong></td>
<td></td>
<td></td>
<td><strong>$247</strong></td>
</tr>
</tbody>
</table>

| Expenses:                     |        |               |                       |
| Debt Service                  | $1,844 | $1,966        | $122                  |
| Personal Service OPEX         | 6,587  | 6,977         | 390                   |
| **Error**                     |        |               | **$512**              |

\(^a\) Includes reserve for disallowances

Had the City been required to change its FY1979 FP by the $289 million deficit projected on August 14, 1978\(^1\) by OSDC, it might
have had to (for example):

1. eliminate 21,911 people, or 13% of the municipal workforce,
or

2. increase its sales tax by 1.5%.
Financing Needs

The City faces a dilemma concerning its financing requirements in FY 1981-FY 1983. The credit market experts say that it is easier to attain public access if fewer bonds are to be sold. Were the City to follow this line of reasoning it would try in 1982 to 1983 to do relatively small amounts of public financing for its general obligation bonds.

However, the City has massive capital needs, requiring large amounts of capital financing. The City Comptroller in his report Rebuilding During The 1980's, estimated that the City requires as much as $4 billion of capital construction per year for 10 years to simply up-grade and maintain existing public facilities.

The balancing of need against financing capability is difficult. It is further complicated by the understandable reluctance of the City to revise its FY 1978 estimate of $2.3 billion of financing required over four years. The estimate was the premise of the 4 year financing agreement.

However, the inability of the City to spend funds as rapidly as expected makes the attainment of reaching
$2.3 billion over the four years seem implausible. The City initially expected to spend $964 million or 42% in the first two years of the plan. It will have spent (if the FY 1980 Plan is fully realized) $557 million or 24% of the planned amount.

The spending and commitments made in FY 1980, FY 1981 and FY 1982 will for the most part determine the amount of financing required in FY 1982 and FY 1983. The City plans would result in a required $1 billion public financing in FY 1983.

Given the City's inability to meet the planned targets, and the large financing requirement it will have at a time when it is first entering the public markets, it may by prudent for the City to modestly revise its capital financing plan for FY 1981 and FY 1982. The City should not be in a position where it pushes ahead with a program in FY 1981 and FY 1982 that will require public financing in FY 1983 that cannot be met.
The New York City Workforce

The FY 1981 contract negotiations will shortly begin for the more than 250,000 New York City employees. The negotiations will take place in a context that recognizes:

- the impact of the economy on the New York City worker;
- the wage and benefit history of the City worker during the period of the fiscal crisis;
- conditions in the public sector throughout the United States.

The most vivid example of what has occurred to New York City worker is demonstrated in Table 26. It demonstrates the position of the worker vis-a-vis inflation and comparable public sector employees.

Table 27 indicates the increase in the Consumer Price Index from June 1975 to June, 1980 (projected). As indicated in Tables 28 to 30, this has meant that the New York City worker has had an increase in his/her annual gross wage and spendable wage, but had a decrease in real annual spendable wages.
Table 26

Changes in Annual Rate of $11,500 Worker by Changes in Salaries of NYC Municipal Workers, in the Consumer Price Index, in Average Federal Civilian Salaries, by Annual Increase in Federal GS

July 1975 to July 1980

<table>
<thead>
<tr>
<th>Date</th>
<th>New York City Municipal Employee</th>
<th>By Increase in NY Area CPI</th>
<th>By Change in Salary of Federal Civilian Employees</th>
<th>By Increase in GS</th>
</tr>
</thead>
<tbody>
<tr>
<td>/30 1975</td>
<td>$12,736</td>
<td>$12,736</td>
<td>$12,736</td>
<td>$12,736</td>
</tr>
<tr>
<td>/30 1976</td>
<td>13,432</td>
<td>13,569</td>
<td>13,602</td>
<td>13,373</td>
</tr>
<tr>
<td>/30 1977</td>
<td>14,361</td>
<td>14,355</td>
<td>14,649</td>
<td>14,019</td>
</tr>
<tr>
<td>/39 1978</td>
<td>14,823</td>
<td>15,079</td>
<td>15,880</td>
<td>15,008</td>
</tr>
<tr>
<td>/30 1979</td>
<td>15,231</td>
<td>16,359</td>
<td>16,754</td>
<td>15,833</td>
</tr>
<tr>
<td>/30 1980</td>
<td>15,840</td>
<td>18,111</td>
<td>17,926</td>
<td>16,941</td>
</tr>
<tr>
<td>Change</td>
<td>+24.4%</td>
<td>+42.2%</td>
<td>$40.8%</td>
<td>+33.0%</td>
</tr>
</tbody>
</table>

NOTES:

a. Calculated as follows: 6% effect 7/1/75; wage deferral effective 7/1/75-6/30/76; $441 "old COLA" on 4/1/75; $189 COLA II on 10/1/76; $420 COLA II on 4/1/77; $693 COLA III on 10/1/77; $882 COLA II on 4/1/78; COLA II is replaced by MOCMP $750 on 7/1/78; 4.0% increase on 10/1/78 based on 6/30/76 base wage; 4.0% increase on 10/1/79 on 10/1/78 base plus $441 old COLA

b. Consumer Price Index for Urban Wage Earners and Clerical Workers, NY-Northeast N.J. June 1980 CPI is projected at a 10.7% annual rate; based on the increase for the period December 1978 to December 1979. This increase is then applied to the June 1979 CPI of 212.2 to give a projected June 1980 CPI of 234.9. Assumes wage adjustments on July 1 of each year based on previous year July to July change.

c. Represents the change in wages and salaries for full-time equivalent employee for federal civilian workers for 1975 through 1978. For 1979 and 1980, annual increases in General Schedule are applied. Data from Bureau of Economic Analysis. This includes all federal non-military employees: blue collar, GS Schedule, and appointed employees.
d. Utilizes the annual adjustment in the Federal General Schedule as follows:

October 1975 - 5.0%
October 1976 - 4.33%
October 1977 - 7.05%
October 1978 - 5.5%
October 1979 - 7.0%

General Schedule employees are primarily clerical and professional employees.

Source: Respective New York City Collective Bargaining Agreements
US Dept. of Labor, Bureau of Labor Statistics
US Dept. of Commerce Bureau of Economic Analysis
Bureau of National Affairs
<table>
<thead>
<tr>
<th>Date</th>
<th>NY Metro CPI(^a)</th>
<th>Increase</th>
</tr>
</thead>
<tbody>
<tr>
<td>June 1980</td>
<td>734.9(^b)</td>
<td>10.7%</td>
</tr>
<tr>
<td>June 1979</td>
<td>212.2</td>
<td>8.5%</td>
</tr>
<tr>
<td>June 1978</td>
<td>195.6</td>
<td>5.0%</td>
</tr>
<tr>
<td>June 1977</td>
<td>186.2</td>
<td>6.4%</td>
</tr>
<tr>
<td>June 1976</td>
<td>175.6</td>
<td>5.9%</td>
</tr>
<tr>
<td>June 1975</td>
<td>165.2</td>
<td>---</td>
</tr>
<tr>
<td>June 1978 to June 1980(^c)</td>
<td></td>
<td>20.1%</td>
</tr>
<tr>
<td>June 1975 to June 1980</td>
<td></td>
<td>42.2%</td>
</tr>
</tbody>
</table>

**NOTES:**

a. Urban Wage Earner & Clerical Worker Index
b. June 1980 CPI, projected at 10.7% annual rate, based on the increase for the period December 1978 to December 1979. This increase is then applied to the June 1979 CPI of 212.2 to give a projected June 1980 CPI of 234.9
c. Represents term of current contract for most New York City municipal employees.

<table>
<thead>
<tr>
<th>Employee Title</th>
<th>Gross Annual Wage 6/30/75</th>
<th>Gross Annual Wage 6/30/80&lt;sup&gt;a&lt;/sup&gt;</th>
<th>Real Annual Gross Wage 6/30/80&lt;sup&gt;b&lt;/sup&gt;</th>
<th>% Change Real Wage 6/30/75 to 6/30/80</th>
</tr>
</thead>
<tbody>
<tr>
<td>Typist</td>
<td>$8,875</td>
<td>$11,349</td>
<td>$7,981</td>
<td>-10.1%</td>
</tr>
<tr>
<td>NYCTA Bus Operator&lt;sup&gt;c&lt;/sup&gt;</td>
<td>13,389</td>
<td>16,878</td>
<td>12,082</td>
<td>-9.8%</td>
</tr>
<tr>
<td>Supervising Clerk</td>
<td>12,310</td>
<td>15,324</td>
<td>10,776</td>
<td>-12.5%</td>
</tr>
<tr>
<td>Computer Operator</td>
<td>12,015</td>
<td>14,745</td>
<td>10,369</td>
<td>-13.7%</td>
</tr>
<tr>
<td>Nurses Aide</td>
<td>10,240</td>
<td>12,836</td>
<td>9,027</td>
<td>-11.8%</td>
</tr>
<tr>
<td>Housing Caretaker&lt;sup&gt;d&lt;/sup&gt;</td>
<td>10,200</td>
<td>12,890</td>
<td>9,027</td>
<td>-11.5%</td>
</tr>
<tr>
<td>Sanitationman</td>
<td>14,840</td>
<td>18,223</td>
<td>12,815</td>
<td>-13.6%</td>
</tr>
<tr>
<td>Teacher MA</td>
<td>18,500</td>
<td>22,841</td>
<td>16,063</td>
<td>-13.2%</td>
</tr>
<tr>
<td>5 yrs Experience</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Firefighter</td>
<td>16,470</td>
<td>20,091</td>
<td>14,129</td>
<td>-14.2%</td>
</tr>
</tbody>
</table>

**NOTES:**

a. Includes two 4% wage increases, $441 COLA roll-in, and $750 NPCP as mandated by Coalition Economic Agreement.

b. June 1980 CPI is projected at a 10.7% annual rate based on the increase for the period December 1978 to December 1979. This increase is then applied to the June 1979 CPI of 212.2 to give a projected June 1980 CPI of 234.0. Gross annual 6/30/80 wages are then deflated by the June 1975-June 1980 change in the NYNE-NJ Clerical Worker CPI.

c. Comparison period is from March 1975 to March 1980.


**Source:** Respective Collective Bargaining Agreements.
Table 29
Change in Real Annual Spendable Wage Rate for Selected New York City Municipal Employees, 1975 to 1980

<table>
<thead>
<tr>
<th>Employee Title</th>
<th>Annual Spendable Wage 6/30/75⁴</th>
<th>Annual Spendable Wage 6/30/80⁶</th>
<th>Real Annual Spendable Wage 6/30/80⁷</th>
<th>% Change Real Wage 6/30/75 to 6/30/80⁸</th>
</tr>
</thead>
<tbody>
<tr>
<td>Typist</td>
<td>$ 7,115</td>
<td>$ 9,046</td>
<td>$ 6,361</td>
<td>-10.6%</td>
</tr>
<tr>
<td>NYCTA Bus Operator ³</td>
<td>10,450</td>
<td>13,124</td>
<td>9,394</td>
<td>-10.1%</td>
</tr>
<tr>
<td>Nurses Aide</td>
<td>8,081</td>
<td>9,985</td>
<td>7,022</td>
<td>-13.1%</td>
</tr>
<tr>
<td>NYCHA Caretaker ⁰</td>
<td>8,198</td>
<td>10,082</td>
<td>7,060</td>
<td>-13.9%</td>
</tr>
<tr>
<td>Computer Operator</td>
<td>9,125</td>
<td>11,156</td>
<td>7,736</td>
<td>-15.2%</td>
</tr>
<tr>
<td>Supervising Clerk</td>
<td>9,510</td>
<td>11,398</td>
<td>7,904</td>
<td>-16.9%</td>
</tr>
<tr>
<td>Sanitationman</td>
<td>11,088</td>
<td>12,926</td>
<td>8,964</td>
<td>-20.7%</td>
</tr>
<tr>
<td>Firefighter</td>
<td>12,636</td>
<td>14,192</td>
<td>9,841</td>
<td>-22.1%</td>
</tr>
<tr>
<td>Teacher, MA 15yrs+</td>
<td>13,368</td>
<td>15,355</td>
<td>10,648</td>
<td>-20.4%</td>
</tr>
</tbody>
</table>

NOTES:

a. Does not reflect deferral program.
b. Includes two 4% wage increases, $641 COLA roll-in and $750 bonus as mandated by Coalition Economic Agreement, except NYCTA bus operator, which includes 6% wage increase and 29% productivity COLA payment. Includes changes in employee pension contributions due to change on 4/1/76.
c. June 1980 CPI is projected at a 10.7% annual rate based on the increase for the period December 1978 to December 1979. This increase is then applied to the June 1979 CPI of 212.2 to give a projected June 1980 CPI of 234.9. For NYCTA bus operator, 10.7% is assumed from March 1979 to March 1980, and NYCHA caretaker, which assumes 10.7% from December 1979 to December 1980.
d. Comparison period is for March 1975 to March 1980.
e. Comparison period is for December 1975 to December 1980.

Source: Respective Collective Bargaining Agreements.

-63-
### Table 30

Change in Annual Gross, Spendable, and Real Spendable Wages for Selected New York City Municipal Employees, 1975 to 1980a

<table>
<thead>
<tr>
<th>Employee Title</th>
<th>Annual Gross Wage 6/30/75 to 6/30/80</th>
<th>Annual Spendable Wage 6/30/75 to 6/30/80</th>
<th>Real Annual Spendable Wage 6/30/75 to 6/30/80b</th>
</tr>
</thead>
<tbody>
<tr>
<td>Typist</td>
<td>+27.9%</td>
<td>+27.1%</td>
<td>-10.6%</td>
</tr>
<tr>
<td>YCTA Bus Operatorc</td>
<td>+26.0%</td>
<td>+25.6%</td>
<td>-10.1%</td>
</tr>
<tr>
<td>Nurses Aide</td>
<td>+25.4%</td>
<td>+23.6%</td>
<td>-13.1%</td>
</tr>
<tr>
<td>NYCHA Caretakerd</td>
<td>+26.4%</td>
<td>+23.0%</td>
<td>-13.9%</td>
</tr>
<tr>
<td>Computer Operator</td>
<td>+22.7%</td>
<td>+22.5%</td>
<td>-15.2%</td>
</tr>
<tr>
<td>Supervising Clerk</td>
<td>+24.5%</td>
<td>+19.9%</td>
<td>-16.9%</td>
</tr>
<tr>
<td>Sanitationman</td>
<td>+22.8%</td>
<td>+14.3%</td>
<td>-20.7%</td>
</tr>
<tr>
<td>Firefighter</td>
<td>+22.0%</td>
<td>+12.3%</td>
<td>-22.1%</td>
</tr>
<tr>
<td>Teacher, MA 15 yrs+</td>
<td>+23.5%</td>
<td>+14.9%</td>
<td>-20.4%</td>
</tr>
</tbody>
</table>

**NOTES:**

a. Does not reflect deferral program. Does include two 4% wage increases, $441 COLA roll-in and $750 NPCP as mandated by Coalition Economic Agreement, except NYCTA bus operator, which includes 6% wage increase and 29¢ productivity COLA payment.

b. June 1980 CPI projected at a 10.7% annual rate based on the increase for the period December 1978 to December 1979. This increase is then applied to the June 1979 CPI of 212.2 to give a projected June 1980 CPI of 234.9. For NYCTA bus operator, 10.7% is assumed from March 1979 to March 1980, and NYCHA caretaker, 10.7% is assumed from December 1979 to December 1980.

c. Comparison period is for March 1975 to March 1980

d. Comparison period is for December 1975 to December 1980

Source: Respective Collective Bargaining Agreements.
FY 1975 - FY 1980

The period of the fiscal crisis has been one of sacrifice for the New York City worker. Wages have not kept pace with inflation, and wages and benefits have been deferred and reduced. The specific history of settlements are:

- July 1, 1974: 8% increase as of 7/1/74
  6% increase as of 7/1/75
  COLA as of 4/1/76 ($441)
- July 1, 1976-July 1, 1978: Productivity COLA
- July 1, 1978: 4% increase effective 10/1/78
  4% increase effective 10/1/79
  $750 non-pensionable cash bonus

This must be contrasted with the wage and fringe benefits deferrals and reductions taken since January, 1974. This is indicated in Table 31.

It must also be noted that after the FY 1979-FY 1980 contract was concluded the statement by many was that the City workforce had just taken every available dollar from the City. The Honorable Senator William Proxmire said, "You (referring to the municipal unions) have pushed for a contract settlement which would take more than every penny that can be found in this budget in
<table>
<thead>
<tr>
<th>Date</th>
<th>Item</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>11/74 - 1/75</td>
<td>Waiving of past due welfare fund contributions, changes in work rules, reductions in scheduled overtime, elimination of summer hours, etc.</td>
<td>$33.0m</td>
</tr>
<tr>
<td>6/75</td>
<td>Deferral of all or part of a scheduled 6% wage increase due on July 1, 1975</td>
<td>180.0m</td>
</tr>
<tr>
<td>4/76</td>
<td>Reduction of Increased-Take-Home-Pay benefit</td>
<td>106.0m</td>
</tr>
<tr>
<td>6/76-6/78</td>
<td>Deferred/reduced fringe benefits, fiscal years 1977-78</td>
<td>48.0m</td>
</tr>
<tr>
<td>6/76-6/78</td>
<td>Deferral of difference between a .4 COLA and a .3 COLA, fiscal years 1977 and 1978</td>
<td>54.2m</td>
</tr>
<tr>
<td>7/1/78 to 6/30/80</td>
<td>Value of annual COLA II reduction from $882 to the NYC $750</td>
<td>52.80m</td>
</tr>
</tbody>
</table>

Subtotal for Mayoral Agencies, HHC, and nonteaching employees of the Boards of Education and Higher Education: $474.00m

9/75-9/78 | Deferrals of COLA, increments, longevity payments and annuity contributions | $105.24m |

9/75-9/78 | Schedule changes, elimination of sabbaticals, etc. | 109.90m |

Subtotal for teaching employees of the Boards of Education and Higher Education: $215.14m

Grand total value of NYC municipal employee give-ups and deferrals: $689.14m
the next two years...." (June 12, 1978). In FY 1979 the City actually had a $213 million budget surplus (as defined by State law).

Public Sector In The United States

One of the most significant contributions made by the City workforce in the past several years has been the lack of labor strife. At a time when conditions were often chaotic, when layoffs were occurring, and their jobs threatened, this workforce reacted responsibly.

This must be compared with turmoil that has existed elsewhere, as indicated in Tables 32 and 33.

While the country experienced 1,837 work stoppages, under far less onerous conditions than existed in New York City, only 3 labor actions in the public sector took place in New York City.

At the time that this condition occurred, settlements in the public sector have exceeded those in New York. The average wage increase in 1979 has been 7% (see Tables 34 and 35).
<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Work Stoppages</th>
<th>Number of Employees Involved</th>
<th>Number of Days Lost</th>
</tr>
</thead>
<tbody>
<tr>
<td>1975</td>
<td>478</td>
<td>318,500</td>
<td>2,204,400</td>
</tr>
<tr>
<td>1976</td>
<td>378</td>
<td>180,000</td>
<td>1,690,700</td>
</tr>
<tr>
<td>1977</td>
<td>413</td>
<td>170,200</td>
<td>1,765,700</td>
</tr>
<tr>
<td>1978&lt;sup&gt;a&lt;/sup&gt;</td>
<td>481</td>
<td>195,500</td>
<td>1,681,400</td>
</tr>
<tr>
<td>1979 1qtr&lt;sup&gt;b&lt;/sup&gt;</td>
<td>87</td>
<td>38,800</td>
<td>321,200</td>
</tr>
</tbody>
</table>

**NOTES:**

a. Final estimate, revision still possible.

b. Preliminary

Table 33
Summary of Reported Municipal Strikes, 1978 and 1979a

<table>
<thead>
<tr>
<th>Employee Category</th>
<th>1978</th>
<th></th>
<th></th>
<th>1979a</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Number</td>
<td>Percent</td>
<td>Number</td>
<td>Percent</td>
<td></td>
</tr>
<tr>
<td>Police</td>
<td>7</td>
<td>4.1%</td>
<td>8</td>
<td>7.5%</td>
<td></td>
</tr>
<tr>
<td>Fire</td>
<td>19</td>
<td>11.1%</td>
<td>4</td>
<td>3.7%</td>
<td></td>
</tr>
<tr>
<td>Sanitation</td>
<td>14</td>
<td>8.2%</td>
<td>11</td>
<td>10.3%</td>
<td></td>
</tr>
<tr>
<td>Transit</td>
<td>14</td>
<td>8.2%</td>
<td>7</td>
<td>6.5%</td>
<td></td>
</tr>
<tr>
<td>Teacher</td>
<td>111</td>
<td>64.9%</td>
<td>66</td>
<td>61.7%</td>
<td></td>
</tr>
<tr>
<td>Nonuniform, General</td>
<td>6</td>
<td>3.5%</td>
<td>14</td>
<td>10.3%</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>171</td>
<td>100.0%</td>
<td>107</td>
<td>100.0%</td>
<td></td>
</tr>
</tbody>
</table>

Primary Cause

<table>
<thead>
<tr>
<th></th>
<th>Number</th>
<th>Percent</th>
<th>Number</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pay</td>
<td>143</td>
<td>83.6%</td>
<td>27</td>
<td>84.3%</td>
</tr>
<tr>
<td>Work Conditions</td>
<td>15</td>
<td>8.8%</td>
<td>6</td>
<td>5.6%</td>
</tr>
<tr>
<td>Union Recognition</td>
<td>0</td>
<td>0.0%</td>
<td>5</td>
<td>4.73%</td>
</tr>
<tr>
<td>Firings, layoffs</td>
<td>6</td>
<td>3.5%</td>
<td>3</td>
<td>2.83%</td>
</tr>
<tr>
<td>Fringe Benefits</td>
<td>1</td>
<td>0.6%</td>
<td>6</td>
<td>5.6%</td>
</tr>
<tr>
<td>Other, not reported</td>
<td>0</td>
<td>3.5%</td>
<td>0</td>
<td>0.0%</td>
</tr>
</tbody>
</table>

Average Duration

<table>
<thead>
<tr>
<th></th>
<th>Days</th>
<th>Days</th>
</tr>
</thead>
<tbody>
<tr>
<td>Police</td>
<td>4.6</td>
<td>7.9</td>
</tr>
<tr>
<td>Fire</td>
<td>11.6</td>
<td>6.0</td>
</tr>
<tr>
<td>Sanitation</td>
<td>7.9</td>
<td>10.0</td>
</tr>
<tr>
<td>Transit</td>
<td>11.0</td>
<td>12.4</td>
</tr>
<tr>
<td>Teacher</td>
<td>10.0</td>
<td>12.1</td>
</tr>
<tr>
<td>Non Uniformed, General</td>
<td>5.5</td>
<td>10.5</td>
</tr>
<tr>
<td><strong>All</strong></td>
<td>10.2</td>
<td>11.2</td>
</tr>
</tbody>
</table>

* Up to September 21
* Includes one strike still in progress
* Includes 21 strikes either still in progress or settlements not yet reported.

Source: Developed by Program Planners, Inc. from data reported by the Bureau of National Affairs and local newspaper articles.
### Table 34

<table>
<thead>
<tr>
<th>Group</th>
<th>Weighted Average First Year Increase</th>
<th>Weighted Annual Contract Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>Firefighters</td>
<td>8.4%</td>
<td>7.5%</td>
</tr>
<tr>
<td>Police Officers</td>
<td>8.9%</td>
<td>8.8%</td>
</tr>
<tr>
<td>Sanitation</td>
<td>6.6%</td>
<td>6.5%</td>
</tr>
<tr>
<td>Transit</td>
<td>6.7%</td>
<td>6.1%</td>
</tr>
<tr>
<td>Teachers</td>
<td>6.5%</td>
<td>6.6%</td>
</tr>
<tr>
<td>General</td>
<td>7.8%</td>
<td>7.3%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>7.4%</strong></td>
<td><strong>7.0%</strong></td>
</tr>
</tbody>
</table>

**NOTE:**
- a. Based on a total of 112 agreements covering 152,800 employees.
- b. January 1 to August 31

<table>
<thead>
<tr>
<th>Location</th>
<th>Group</th>
<th>Length of Contract</th>
<th>Wage Settlement</th>
<th>Other Provisions</th>
</tr>
</thead>
<tbody>
<tr>
<td>San Francisco</td>
<td>Police, Fire</td>
<td>2 years</td>
<td>15.1%</td>
<td>-</td>
</tr>
<tr>
<td>Philadelphia</td>
<td>All Employees</td>
<td>1 year</td>
<td>10.3%</td>
<td>Wage adjustment is last year of two year agreement that provided full COLA</td>
</tr>
<tr>
<td>Washington, D.C.</td>
<td>All Employees</td>
<td>1 year</td>
<td>7.0%</td>
<td>To be negotiated separately (wage adjustment same as Federal employees).</td>
</tr>
<tr>
<td>Detroit</td>
<td>Police &amp; Fire</td>
<td>3 years</td>
<td>24.4%</td>
<td>If ( t = 0.3 ) point ( 1967 = 100 ) COLA continues</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1st yr - 5.5%</td>
<td>2nd yr - 4.0%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>3rd yr - 4.0%</td>
<td>+ COLA</td>
</tr>
<tr>
<td>Los Angeles</td>
<td>Police &amp; Fire</td>
<td>1 year</td>
<td>8.4%</td>
<td>-</td>
</tr>
<tr>
<td>Seattle</td>
<td>All Employees</td>
<td>2 years</td>
<td>1st yr - 7.6%</td>
<td>COLA is 90% of Seattle</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>2nd yr - COLA</td>
<td>area CPI for 1980</td>
</tr>
</tbody>
</table>

FOR RELEASE ON DELIVERY
EXPECTED AT 10:00 A.M.
January 28, 1980

STATEMENT OF THE HONORABLE ROGER C. ALTMAN
ASSISTANT SECRETARY OF THE TREASURY (DOMESTIC FINANCE)
BEFORE THE SENATE COMMITTEE ON BANKING,
HOUSING AND URBAN AFFAIRS

Mr. Chairman and Members of this distinguished Committee:

I appear before you today to discuss the Treasury Department's activities under the New York City Loan Guarantee Act of 1978. My testimony will cover the following major areas:

-- a recent history of the City's budget and financing developments including the Federal guarantees of City debt and the conditions under which these guarantees were issued;

-- the status of the City's fiscal year (FY) 1980 budget, and the Program to Eliminate the Gap (PEG) for FY 1981 and FY 1982; and

-- a discussion of several key problems affecting New York's financial future, including prospects for the City's regaining access to the public bond market.

RECENT DEVELOPMENTS

Let me put this issue into some perspective by briefly reviewing the history of the New York City fiscal crisis.
It erupted in 1975 when the City lost access to conventional lending sources and teetered on the edge of bankruptcy. The City lost its ability to borrow because it was incurring enormous budget deficits and had already borrowed huge amounts to finance them. Lenders had lost confidence in the City's ability to repay.

The State of New York then undertook massive efforts to solve the City's fiscal problems. Among other things, it established the Municipal Assistance Corporation (MAC), the Emergency Financial Control Board (EFCB), and advanced $800 million to the City. It was not until Congress passed the New York City Seasonal Financing Act of 1975, however, that the City was actually saved from apparent bankruptcy.

In the intervening four years, New York has met each of its budget goals since Federal credit assistance was first provided in late 1975. It intends to achieve real budget balance -- balance in accordance with Generally Accepted Accounting Principles (GAAP) -- in its fiscal 1981, a full year ahead of schedule.

Several important recent financial strides deserve mention:

-- the City's 1980 budget will reduce its GAAP deficit to approximately one-fifth of the 1976 level and the City's budget has been balanced for the last two fiscal years in accordance with State law.

-- the City's proposed 1981 budget entirely eliminates its GAAP deficit. This compares to a $1.8 billion GAAP deficit in FY 1976.

-- the City was independently audited for the first time in fiscal year 1978 and this was repeated last year.

-- the overhang of short-term debt has been funded. Indeed, its short-term borrowing needs have been cut from as high as $8.4 billion in 1975 to $600 million in fiscal year 1980.

-- the City re-entered the public credit markets in 1979 for the first time since 1975. Two City sales of short-term notes totalling $275 million were oversubscribed by investors and only $375 million of the $750 million pension fund/bank standby credit line was used in fiscal 1979. In fiscal 1980, the City has already sold $375 million
of its notes to the public and now expects to sell up to $225 million more in the public markets, thereby avoiding any use of its standby credit facility, which now consists solely of financial institutions.

Federal Guarantees Issued to Date

Mr. Chairman, since I last testified before you in February 1979, Treasury has issued further Federal guarantees of City bonds as follows:

<table>
<thead>
<tr>
<th>Date</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>February 15, 1979</td>
<td>$150 million</td>
</tr>
<tr>
<td>June 28, 1979</td>
<td>50 million</td>
</tr>
<tr>
<td>August 30, 1979</td>
<td>100 million</td>
</tr>
<tr>
<td>January 3, 1980</td>
<td>150 million</td>
</tr>
<tr>
<td>TOTAL</td>
<td>$450 million</td>
</tr>
</tbody>
</table>

To date, the aggregate amount of City bonds guaranteed is $650 million. An additional $100 million of guarantees are scheduled to be issued next month. This would complete the $750 million in Federal guarantees which are included in the $4.5 billion long-term financing plan as "up-front" guarantees. The $900 million of remaining guarantee authority will only be used in the unlikely event that both the City and MAC are unable to finance the City's long term needs in the next two years.

The United States has received prompt quarterly payments from the City of the one-half percent guarantee fee provided under the Guarantee Act. At the end of December, these payments totalled $2,070,053.47.

The Guarantees

On each issuance of Federal guarantees, Treasury must determine that the City is in compliance with the conditions
of eligibility set forth in the Guarantee Act. Your Committee
staff has been provided with copies of the formal determinations
made before each issuance. I will devote a significant
portion of my testimony reviewing the most important aspects
of the City's compliance with the Guarantee Act -- budget
balance and credit market progress. I think it important,
however, to mention briefly the City's compliance with certain
other areas of the Guarantee Act.

Reasonable Prospect of Repayment

Federal guarantees of City debt cannot be issued unless
there is a "reasonable prospect" that the principal and
interest on the outstanding guaranteed indebtedness will be
repaid. Since these Federally-guaranteed obligations have
maturities of up to fourteen years, Treasury evaluates this
"reasonable prospect" in terms of the City's long-term fiscal
and economic health. We have found that both the strength
of the City's economy and the demonstrated local commitments
to continued budgetary and financial reform enhance the
security of the guaranteed debt.

One recent change in the financing program will be of
interest to you, Mr. Chairman. According to the City's latest
financial plan, in FY 1983 the City anticipates refunding $180
million of its Federally-guaranteed bonds. This represents
24% of the principal amount of guaranteed bonds projected to be
outstanding by the end of FY 1980, exceeding the 15% refunding
requirement under the Guarantee Act.

Financing Commitments

The local financial institutions and City pension funds
have maintained their commitments to purchase unguaranteed
Municipal Assistance Corporation securities. Also, MAC has
sold its bonds to the public on schedule. We expect these
parties to continue to meet their financing commitments
in FY 1981 and FY 1982 in accordance with the City's
financing plan.

Independent Fiscal Monitor

Section 103(6) of the Guarantee Act requires that "an
independent fiscal monitor" -- the Financial Control Board -- "has
the authority to control the financial affairs of the City...."
The Control Board has exhibited broad financial control, review
and supervisory powers over the City on its course toward fiscal recovery.

Financial Reporting and Accountability

Another aspect of the City's creditworthiness relates to the City's financial reporting and control systems. Since 1975 the City improved significantly in this area through the implementation of its Integrated Financial Management System (IFMS).

To comply with Section 103(7)(a) of the Guarantee Act, the City has been audited in two consecutive years by a consortium of independent certified public accountants. There are few large municipalities that can claim a like accomplishment.

Beyond this major improvement, and as a result of the Guarantee Act, the City has established an actively functioning Audit Committee in order to address and review major accounting issues affecting New York City. The improvement of the City's record-keeping system, the implementation of annual independent audits, and the establishment of an Audit Committee are all positive developments.

THE NEW YORK CITY BUDGET

The key to restoring New York's ability to finance itself is for it to attain true balance in the City budget and to maintain that balance. On this basis, institutional lenders and the credit rating agencies will regain confidence in the City's debt. The Guarantee Act recognized this by requiring the Treasury Department to determine, prior to each issuance of a Federal guarantee, that the City's budget is in balance under New York State law and that the City is making substantial progress toward balance according to GAAP in FY 1982.

FY 1979 Results

The City incurred a $422 million deficit on a GAAP basis in fiscal 1979. This represented an improvement of $290 million over the 1978 deficit level. Indeed, this improvement occurred even though $116 million of revenues, originally projected for 1979, will be realized in later years. The principal reason that New York remains in GAAP deficit at all is its continued practice of funding certain operating expenses from its capital budget.
The Guarantee Act requires the City to phase out this practice by budgeting no more than $450 million of these so-called capitalized expenses in fiscal 1979, $300 million in fiscal 1980, $150 million in fiscal 1981 and zero in fiscal 1982. In fiscal 1979, the City voluntarily began to accelerate this phase-out schedule.

In contrast to the $422 million GAAP deficit, under accounting principles prescribed by New York State law the City realized a $216 million surplus in 1979. Thus, fiscal 1979 was a year of financial progress for the City.

**FY 1980**

Fiscal 1980 has also been another year of budget improvement. In January 1979, the City announced its preliminary 1980 budget, that included a set of actions to eliminate a potential deficit under State law of $433 million. These measures included up to $250 million of City actions and at least an additional $183 million in State and/or Federal assistance.

The actual 1980 budget, adopted in June 1979, was balanced on a State law basis. A substantial increase in City's revenue, in addition to a proportional mix of City, State and Federal actions eliminated the potential deficit. Due to various uncertainties, the Financial Control Board (FCB) requested that the City detail a contingency program of more than $100 million of City actions if FY 1980 balance could not be maintained as the year progressed.

As fiscal 1980 unfolded, serious budget problems developed in the Board of Education and the Health & Hospitals Corporation (HHC). In December, the City was required to establish an additional reserve of $50 million to cover potential budget gaps in HHC and allocate an additional $19 million of support for the Board of Education.

Yet, stronger than expected revenue growth and further expenditure reductions enabled the City to tackle these mid-year problems and still remain in balance under State law without implementing the contingency program required by the FCB. Indeed, even though $135 million of forecasted FY 1980 revenues are now targeted for FY 1981, the City's net revenues are projected at $38 million above the adopted budget.

This reserve strength enabled New York to avoid in 1980 the type of sharp spending cuts which would have resulted if the
City had to implement its contingency program. It might have been wise to voluntarily reduce City expenditures further, in light of the large potential 1981 and 1982 budget gaps, but the City chose a milder course.

The Fiscal 1981 and Fiscal 1982 Budgets

On January 16, Mayor Koch released his preliminary 1981 budget. The Treasury Department has had only 11 days to evaluate this plan and our conclusions, therefore, are highly preliminary. We are not required by the Loan Guarantee Act to make findings concerning the success of this plan until the next issuance of guarantees, currently scheduled for February 21.

The PEG plan would attain the long sought goal of true budget balance according to GAAP next year. This would be one year earlier than required by Federal and State law and is a courageous step.

The City estimates that attaining this FY 1981 goal will require eliminating a potential deficit of $677 million. Moreover, if this 1981 gap is not closed, it will grow to approximately $1.1 billion in 1982. Certain fiscal monitors, using various "worst-case" assumptions, have estimated considerably larger potential gaps in each of these years -- in excess of $1 billion in FY 1981 and growing to $2 billion in FY 1982.

These estimated gaps are large, but it is important to put them into perspective.

Background

Table 1 below compares the City's performance against its budget goals for FY 1976-FY 1979. As you will note, the City has met or exceeded each of its budget goals over this period.
TABLE I

Actual Budget Results Compared to Original Budget Goals
($ millions)

<table>
<thead>
<tr>
<th></th>
<th>City's Goal Under State Law</th>
<th>Year-End Budget Results Under State Law</th>
<th>Year-End Budget Results Under GAAP</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY 1976</td>
<td>$1,051 deficit</td>
<td>$968 deficit</td>
<td>$1,822 deficit</td>
</tr>
<tr>
<td>FY 1977</td>
<td>$ 686 deficit</td>
<td>$329 deficit</td>
<td>$1,039 deficit</td>
</tr>
<tr>
<td>FY 1978</td>
<td>Balance</td>
<td>$ 32 surplus</td>
<td>$ 712 deficit</td>
</tr>
<tr>
<td>FY 1979</td>
<td>Balance</td>
<td>$216 surplus</td>
<td>$ 422 deficit</td>
</tr>
</tbody>
</table>

The large differences between the original projections and the actual results reflect the inherent conservatism in revenue and expenditure assumptions in the City's budget methodology. In effect, the process itself requires that potential budget gaps be overstated.

Specifically, the City did not include non-recurring revenues in its forecasts, even though varying amounts of such revenue occur each year. Furthermore, the City did not reduce its expenditure forecasts to reflect likely spending shortfalls ("underspending") even when such shortfalls appeared certain.

Finally, the City has generally used conservative assumptions to forecast its economically-sensitive revenues. Actual revenues have frequently exceeded plan, as they did in FY 1980.

In short, the real budget gaps have invariably been smaller than the originally estimated gaps. This could again be the case in the future.

Fiscal 1981

Last June, the City forecast a 1981 deficit of $464 million on the State law basis. The recently released preliminary 1981 budget, however, estimated this gap at $677 million. The principal elements of the 1981 deficit outlook are as follows:

-- the Mayor's decision to reach budget balance one year early increases the potential deficit by $275 million.
This includes the elimination of $150 million of incremental capitalized expenditures and $128 million of incremental pension costs;

-- aside from this mayoral decision, Federal and State laws in effect already required the City to adjust for increases of $50 million in pension costs and $132 million in phased-out capitalized expenditures;

-- an assumed 4% wage increase in 1981 (the same as that in 1978) which the City estimates will cost approximately $142 million in that year. This is the first estimate by the City of its future labor costs;

-- an increase in Medicaid payments, of which the City's share is $102 million;

-- a $65 million increase in energy costs and a legally mandated $64 million increase in expenditures for special education;

-- these increased costs are somewhat offset by two categories of increased revenue: realization in 1981 of $155 million previously projected for this year; and a revised estimate that 1981 city tax receipts will be $33 million higher than the 1980 level.

City Deficit Reduction Actions

The City has proposed $507 million in its own deficit reduction actions to help close this $677 million potential gap. These include:

-- improved collection techniques and other steps resulting in $33 million of increased revenue;

-- the Mayor's decision to increase taxes and certain other charges to produce increased revenues of $175 million. This includes $39 million in increased water and sewer charges, $36 million in increased real estate taxes, and $35 million in increased excise taxes on beer and liquor;

-- expenditure reductions of $299 million consisting primarily of $165 million of reductions in the City's personnel budget and $83 million of non-personnel reductions.

Table II details the major items in this City program.
### TABLE II
#### 1981 City Program
\[\text{($ in millions)}\]

**Revenue Actions**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Improved Rental Income Collection</td>
<td>$6</td>
</tr>
<tr>
<td>Increased License and Permit Fees</td>
<td>5</td>
</tr>
<tr>
<td>Reduced Provision for Disallowances</td>
<td>10</td>
</tr>
<tr>
<td>Increase in Inter-Fund agreements</td>
<td>5</td>
</tr>
<tr>
<td>Other</td>
<td>7</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$33</strong></td>
</tr>
</tbody>
</table>

**Tax and Charge Increase to Yield $175 million/year**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Water and Sewer Charge Increase</td>
<td>$39</td>
</tr>
<tr>
<td>Real Estate Tax Increase</td>
<td>36</td>
</tr>
<tr>
<td>Excise Tax on Beer and Liquor</td>
<td>35</td>
</tr>
<tr>
<td>Financial Corporation Tax Revision</td>
<td>20</td>
</tr>
<tr>
<td>City Gasoline Tax Extension</td>
<td>13</td>
</tr>
<tr>
<td>Parking Garage Tax Increase</td>
<td>11</td>
</tr>
<tr>
<td>Hotel Tax Revision</td>
<td>11</td>
</tr>
<tr>
<td>Tax on Taxi Medallion Transfer</td>
<td>8</td>
</tr>
<tr>
<td>Real Estate Tax - Veterans Exemption</td>
<td>7</td>
</tr>
<tr>
<td>Other</td>
<td>12</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$192</strong></td>
</tr>
</tbody>
</table>

Less Possible Slippage  

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total</strong></td>
<td><strong>$175</strong></td>
</tr>
</tbody>
</table>

**Agency Expenditure Reductions**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Police</td>
<td>$29</td>
</tr>
<tr>
<td>Fire</td>
<td>11</td>
</tr>
<tr>
<td>Correction</td>
<td>14</td>
</tr>
<tr>
<td>Social Services</td>
<td>25</td>
</tr>
<tr>
<td>HRA</td>
<td>18</td>
</tr>
<tr>
<td>Board of Education</td>
<td>111</td>
</tr>
<tr>
<td>CUNY</td>
<td>5</td>
</tr>
<tr>
<td>All other</td>
<td>35</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$248</strong></td>
</tr>
</tbody>
</table>

**Other Reductions**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Transit, Housing and Other Subsidies</td>
<td>$9</td>
</tr>
<tr>
<td>HHC Subsidy</td>
<td>20</td>
</tr>
<tr>
<td>Energy Conservation Program</td>
<td>12</td>
</tr>
<tr>
<td>OTPS Cost Containment</td>
<td>10</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$51</strong></td>
</tr>
</tbody>
</table>

**TOTAL**  

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total</strong></td>
<td><strong>$507</strong></td>
</tr>
</tbody>
</table>
It will not be easy to realize the full $507 million of projected City actions. Most of the revenue actions and tax increases will require the cooperation of the City Council and/or the State Legislature. Although tax increases are never popular, some local support for these actions has been reported.

Concerning spending, Mayor Koch has proposed major cuts in the personnel budget totalling $165 million. This means a net reduction in City-funded jobs of approximately 5,000. It includes a net cut of 3,100 in education personnel, and 722 in the uniformed police force. The overall job reductions appear possible, although they may be particularly difficult in the education area.

Regarding non-personnel cuts, the $83 million projected 1981 reduction also appears attainable. In each of the past three years, the City's actual reductions in this area have exceeded those projected in each January's PEG plan.

There are several uncertainties among these City actions, however, including the following:

-- the ability of the Board of Education to sustain reductions of the magnitude proposed by the City while maintaining services at an acceptable level. New control procedures to provide additional oversight over the fiscal affairs of the Board have been instituted. These controls should facilitate the implementation of these cuts;

-- the City's plan to reduce its subsidy to the Health and Hospitals Corporation (HHC). Present projections of HHC revenues are uncertain today. Although the City is under no legal obligation to fund HHC deficits, it has done so in the past;

-- City expenditures for energy, which have been rising rapidly.

The City's 1981 Plan also calls for unspecified State and Federal actions totalling $170 million. It is simply too early to judge whether this estimate is realistic. Governor Carey's State budget was released only one week ago, and President Carter's proposed 1981 Federal budget will be released today. I will discuss in greater detail the prospects for intergovernmental aid in a later portion of my testimony.
Fiscal 1982

Fiscal 1982 will be a more difficult year for New York City. Assuming the City is able to close the $677 million gap in FY 1981, through significant and recurring City expenditure reductions, revenue actions and tax increases, and moderate increases of Federal and State assistance, a potential $462 million budget gap still remains. The principal cost elements in this additional gap are:

-- an additional $189 million provided to fund a 4% wage settlement;

-- $75 million to cover increasing energy costs;

-- an additional allocation of $62 million of City funds for Medicaid;

-- an additional $49 million allocated to the Board of Education for Special Education.

There is considerable uncertainty, however, as to whether this $462 million 1982 deficit estimate is realistic. It remains to be seen whether the City can negotiate fiscally restrained labor contracts covering 1981 and 1982. In addition, its projections call for a large increase in State and Federal aid for 1982, which will be difficult. Finally, the 1982 deficit will automatically be larger if the City fails to eliminate the full $677 million 1981 potential gap on a recurring basis. A judgment on whether a large 1982 gap can be closed depends on an assessment of (1) whether the City has the capacity to make further large cuts, and (2) what can be expected of Federal and State aid in the out-years.

The City's plan proposes an additional $222 million in City actions and $240 million in State and Federal actions to close this gap. Table III shows the major items in the 1982 program, their combined 1981 and 1982 values as well as their incremental value.

As you will note from Table III, the program the City proposes for fiscal 1982 consists primarily of actions initiated during the previous fiscal year. These actions have an increased value because they are expected to be more fully phased-in during the latter year. Therefore, the comments I made regarding the 1981 program are applicable here as well. It is a matter of some concern that the City has not identified alternative programs for 1982 given the likelihood that some of the PEG actions will fail to meet the City's expectations.
TABLE III
FY 1981-1982 Program ($ in millions)

<table>
<thead>
<tr>
<th>Revenue Actions</th>
<th>Total Value</th>
<th>FY 1982 Incremental Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Implement Semi-Annual Real Estate Tax Payments</td>
<td>$32</td>
<td>$32</td>
</tr>
<tr>
<td>Increase CUNY Tuition</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>Continuation of 1981 Actions</td>
<td>56</td>
<td>23</td>
</tr>
<tr>
<td><strong>Total Revenue Actions</strong></td>
<td>93</td>
<td>60</td>
</tr>
<tr>
<td><strong>1981 Tax and Fee Increases</strong></td>
<td>175</td>
<td>--</td>
</tr>
<tr>
<td><strong>Agency Expenditure Reductions PS/OTPS</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Police</td>
<td>38</td>
<td>9</td>
</tr>
<tr>
<td>Fire</td>
<td>17</td>
<td>6</td>
</tr>
<tr>
<td>Sanitation</td>
<td>9</td>
<td>7</td>
</tr>
<tr>
<td>Corrections</td>
<td>18</td>
<td>4</td>
</tr>
<tr>
<td>Social Services</td>
<td>33</td>
<td>8</td>
</tr>
<tr>
<td>HRA</td>
<td>20</td>
<td>2</td>
</tr>
<tr>
<td>Board of Education</td>
<td>182</td>
<td>71</td>
</tr>
<tr>
<td>CUNY</td>
<td>6</td>
<td>1</td>
</tr>
<tr>
<td><strong>All Other</strong></td>
<td>59</td>
<td>26</td>
</tr>
<tr>
<td><strong>Total Agency Reductions</strong></td>
<td>382</td>
<td>134</td>
</tr>
<tr>
<td><strong>Other Reductions</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transit, Housing and Other Subsidies</td>
<td>12</td>
<td>3</td>
</tr>
<tr>
<td>HHC Subsidy</td>
<td>20</td>
<td>--</td>
</tr>
<tr>
<td>Energy Conservation Program</td>
<td>26</td>
<td>14</td>
</tr>
<tr>
<td>OTPS Cost Containment</td>
<td>21</td>
<td>11</td>
</tr>
<tr>
<td><strong>Total Other Reductions</strong></td>
<td>79</td>
<td>28</td>
</tr>
<tr>
<td><strong>TOTAL CITY ACTIONS</strong></td>
<td><strong>$729</strong></td>
<td><strong>$222</strong></td>
</tr>
</tbody>
</table>
Since 1975, the City has shown the capacity to meet its budget goals and, year after year, it has eliminated huge projected deficits. The continuing commitment of City and State elected officials to the City's financial well being is solid. Mayor Koch's resolve to reach a GAAP balanced budget in FY 1981, a year ahead of an already rigorous schedule, is the best evidence of this commitment.

State Aid

New York State faces serious budget pressures of its own in its fiscal year 1981. Therefore, its recently announced Executive Budget is extremely tight. The combination of certain formula-driven increases in expenditures, tax-reduction programs and the possible impact on the State of a recession threaten future increases in aid to the City. Despite these budget difficulties, the State's commitment to the City's recovery remains undiminished. During the State's fiscal years 1976-1980 Governor Carey successfully supported significant increases in State aid to New York City. In FY 1980 alone, State assistance to the City increased by more than $200 million.

Federal Aid in 1981 and 1982

Our preliminary indications of the President's FY 1981 budget proposal are that Federal aid to the City will continue to increase into the 1980's as it has every year since 1976.

Modest increases in aid to the City may be forthcoming, but they are in the area of legislation. I am referring to programs such as targeted fiscal assistance, countercyclical revenue sharing, and Medicaid and welfare funding reform.

Specifically, the two anti-recession fiscal assistance programs (actually two parts of one bill), if passed by Congress in one of their present forms, would increase unrestricted aid to the City by as much as $45 million in City FY 1981 and perhaps a greater amount in FY 1982, depending on local economic conditions. In addition, the Administration is working on a proposal to broaden eligibility criteria for Medicaid, and the increased Federal reimbursement rate for the Aid to Families with Dependent Children (AFDC) program could free up additional City funds annually. None of these proposals, of course, are assured of passage.
In addition to these actions which will require legislative approval, the Administration continues to work on a series of administrative actions, primarily in the area of public housing, that would provide recurring fiscal relief.

The more limited ability of the State to provide additional significant amounts of budget aid means that the City may require major increases in Federal fiscal assistance to meet 1981 and 1982 budget goals. Obviously, the Administration has provided assistance to the City in the past. It continues to work for legislative programs to assist this country's urban areas with their unique problems. We are hopeful that Federal assistance, together with State and City actions will eliminate future budget gaps.

There are other areas of concern in the City's road to financial self sufficiency. A discussion of these follows.

THE NATIONAL AND LOCAL ECONOMY

A major factor in evaluating the City's prospects relates to the impact of the projected recession. A national recession was widely projected to begin during the last quarter of 1979 and continue into late 1980. The mixed signs over the past few months raised some doubt about the timing and duration of the recession. The major forecasting agencies are now projecting a moderate recession that will be more severe than the downturn projected in the late summer, but not as severe as the 1974-75 recession. In any event, it appears the local economy is better prepared for a recession than it was in 1973:

- the City's employment levels, after drastic decline since 1969, have stabilized;

- the decline in manufacturing employment and a move toward service oriented industries makes local employment generally less affected by cyclical swings in the economy;

- the automobile and construction industries appear to be on the leading edge of the forecasted recession -- the City does not have a heavy dependence on automobile production, and commercial construction is experiencing a boom, particularly in the borough of Manhattan;

- retail sales on a City-wide basis have continued to outperform the national averages.
Hence, if the severity of the recession is no worse than currently projected, our judgment is that the City's projections should not be seriously askew.

**WAGE SETTLEMENTS**

The City's estimates of budget deficits have not previously included the cost of potential wage settlements in FY 1981 and FY 1982. The City has now included in its baseline estimates the funding of a 4% wage settlement in FY 1981 and FY 1982. The prospective costs of such a wage settlement are estimated by the City at $142 million in FY 1981 and $331 million in FY 1982. Last Thursday the City's unions announced their unwillingness to settle for 4% annual increases as they did in 1978. On the other hand, Mayor Koch has indicated to the City's municipal labor leaders not to expect to receive the same increases provided in existing pacts -- which are 4%. Ultimately, the wage settlement will be negotiated, hopefully on reasonable terms, between the City and its unions.

**CAPITAL SPENDING**

Another important factor in the City's attempt to achieve economic stability and financial independence is its capital spending program. Though not specifically related to the City's near-term financial future, the City's ability to provide an attractive environment for its citizenry and for economic development purposes will be an essential element in the City's long-term fiscal health.

One critical factor in support of the Guarantee Act was the establishment of a credible financing package for the City so that improvement of its physical plant could get back on track.

Four years of neglect caused by the City's fiscal crisis have left the City's infrastructure in a somewhat deteriorated condition. Yet, the City has been slow in using capital funds provided for rebuilding. We appreciate the massive job of totally reactivating a capital program which has been dormant for four years. Nevertheless, the City must make a maximum commitment to improve its capital planning process.

Early projections for FY 1980 capital spending were $582 million. Subsequently, this estimate was lowered to $440 million. The City's new Four-Year Plan, however, indicates
further "slippage" to $394 million. We have carefully monitored the City's capital spending and consider this estimate reasonable. In connection with this latest reduction, however, the City did indicate that the $2.3 billion capital spending goal in the FY 1979-1982 period was reachable.

Over the last few months the City has shown signs of progress in this area by coordinating the activities of all City agencies under one central office and improving accountability throughout the capital budget system.

RESTORING ACCESS TO THE PUBLIC BOND MARKET

A major factor in the restoration of the City's long-term fiscal and economic independence will be its ability to find adequate sources of long-term credit in the public markets. Under the Guarantee Act, the City must attempt to sell its own bonds to meet a portion of its long-term financing needs in FY 1980.

Moody's Investors Services currently rates the City's bonds "B", which is below investment grade. Until an investment grade rating is achieved, the City will experience difficulties in attaining significant market access. In its review of the City's credit, Moody's commented that "fundamental credit elements are demonstrably weak and the City's long-term general obligation bonds continue to lack the characteristics of a desirable investment." The other major rating agency, Standard and Poors, has maintained its rating suspension of City securities since April 1975.

The absence of a suitable credit rating on its bonds has the practical effect of excluding, among other investment groups, banks, insurance companies, trust departments and municipal bond funds from purchasing long-term City bonds.

While there may be a limited demand for New York City bonds among individual investors, without the participation of institutional investors New York will not achieve full financing independence. The City has prepared a strategy to fully enter the public credit market.

The cornerstone of this strategy is to achieve budget stability and other management objectives which appear to be crucial in obtaining an investment grade rating. The City's budget progress in fiscal 1980 and its bold step in accelerating
the phase-in of a GAAP balanced budget for fiscal year 1981 can only improve its chances for an investment grade rating. The conclusion of the upcoming collective bargaining negotiations with the City's workforce will resolve another major uncertainty.

As for tapping the limited, individual investor market for City bonds, Mayor Koch has stated that "the existence of this uncertain market, while encouraging, cannot serve as the basis of any long-range solutions to the City's credit needs, since it simply cannot provide the substantial amounts of capital regularly required by the City." Current market conditions and the uncertainties surrounding the forthcoming labor negotiations seem to mitigate against such an attempt prior to FY 1981.

FY 1981 and 1982

As you are aware, Mr. Chairman, the City's financing schedule calls for it to sell $300 and $645 million of unguaranteed bonds to the public in FY 1981 and FY 1982, respectively. The Guarantee Act requires such an effort. Without an investment grade rating, however, institutional investors will be unlikely participants in such an offering. It is equally unlikely that the requisite amounts of bond sales under the Guarantee Act in FY 1981 and FY 1982 can be met solely through sales to individual investors on reasonable terms. Any amounts the City cannot finance independently are to be covered, in the first instance, by MAC.

If the City is unable to access the bond market over the next two years, MAC has sufficient bonding authority to issue, on behalf of the City, its own bonds. In addition, we believe that MAC will have sufficient market access so as to preclude the issuance of stand-by Federal guarantees.

The next twelve months will be pivotal in the City's self-financing quest:

-- the conclusion of the forthcoming wage negotiations with the City and its municipal unions will eradicate a major uncertainty in the City's financial plans;

-- the City will have provided a budget balanced in accordance with GAAP;

-- a successful sale of a limited amount of bonds in the public market, without an investment grade rating, will demonstrate investor confidence in the City's fiscal progress.
These factors should facilitate the City's ability to achieve an investment grade rating — a critical step in the City's ultimate goal of financing independence.

I will close by emphasizing that the City has shown the willingness and wherewithal to take whatever steps necessary to meet its statutory budget and financing requirements. The City's and State's commitment to continuing this record is clear. We, therefore, remain satisfied that the City, the State and other interested parties are making the maximum effort as required by the Guarantee Act to solve the City's fiscal and financing difficulties.

This concludes the prepared portion of my testimony. I will be pleased to respond to any questions at this point.

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SUMMARY

Statements Before Senate Committee
on Banking, Housing and Urban Development
January 28, 1980

Bigel

* contrasting state of affairs in 1975 vs. current: issuance of less than $600 M in short-term debt, surpluses in 1978 & 1979 with GAAP-balanced budget in 1981, City has one of leading municipal accounting and budgeting systems in the U.S.

* bankruptcy threat is gone; no more need to fund daily operations with long-term proceeds; should the City fail access to fund capital in 1983, daily functions will not suffer.

* NYC's current problems are in transit, health care and education, which are not unique but size of City magnifies them; Fed has failed to provide funds or comprehensive solutions.

* GAAP-deficit reduction progress since 1975; expenses kept behind inflation rate (better than other larger cities); from 7/1/75 6/30/80 City workforce will have declined by 23% while other cities show increases.

* substantial progress made by NYC in terms of financing: obtained seasonal financing from credit markets, reduced seasonal needs, eliminated $800 M State advance, ended 1978 and 1979 with high working capital, reduced interest expenses, improved beginning cash balances with decreased dependences on pre-paid revenues, elimination of outstanding short-term debt at 7/1/75.

* Federal aid from '76-'80 has not kept pace with inflation; Federal policies are negative-excessive public and medical assistance burden on the City and special ed costs for City increase at higher rate (almost twice) than Federal aid, all are mandated programs; federal discrimination in transit also against urban areas, but especially NYC; NYCTA only gets small percentage of aid in proportion to ridership.
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* bankruptcy threat triggered investments by retirement systems; participation of pension funds significantly strengthened those systems; fire department pension fund dispute should be solved; retirement systems do not intend to purchase any further City-related paper past 1982.

* market access is hampered by the rating agencies, oversight agencies and the size of the financing.

  rating agencies: inaccurate reports; fail to consider progress of NYC; irrespnsive to public needs; City has acted on major recommendations based on issues identified by rating agencies but it was ignored; their standards are inconsistent and constantly raised.

  oversight agencies: given the weight of their prognos-tications, their accuracy must be judged; their judgment has not been better than the City's but it is given more weight.

  size of financing: massive capital needs, as much as $4 billion per year per Comptroller's report, but that's overestimated and so City's $2.3 billion; City should revise capital plan based on spending.

* City workforce has had gross increase in spendable wages but real decline annually; fiscal crisis period was time of sacrifice for workforce (a detailed listing of wage and fringe benefit deferrals and cuts is shown); though settlements elsewhere were higher, NYC had fewer "labor actions".

NOTE: MAC's response to program Planners report in December refuted a number of the points which have been repeated here . . . Program Planners fails to recognize contribution of State aid, as well as the actual methodology by which NYC reduced its budget gaps largely by way of Federal/State revenues, debt service reductions primarily reached through MAC restructuring, and tax rate increases with significantly less involvement of City expenditure reductions.
* what Harries said two years ago holds true (City will be unable to borrow meaningfully unless it can demonstrate fiscal stability through balanced budgets with an outside monitoring system), but one year isn't enough.

* free access is still elusive; note sale is no test of credit because of State revenue basis; a small ($50-70 M) 15-year bond sale could have reached the market at a reasonable cost last August-September but this isn't possible now at a reasonable rate (15-year yield for NYC would have to be well in excess of the current scale, but not far off from Chicago-10% range).

* NYC is slowly and painfully meeting expenditures with more reliable revenues, but huge governmental sector makes retrenchment difficult.

* real progress is evidenced by 1/15/80 plan to move to GAAP in 1981 especially in light of gap reductions since 1976; short-term needs were reduced, but monitoring is needed and should be continued.

* January plan reflects deficit elimination largely by City actions (like Board of Ed, which is difficult); difficult situations loom (labor); inflation compounds the gap; Federal/State aid is still a major part of plan; Federal/State and City should move to synchronized cash flow calendars so all could reduce anticipatory borrowings; water and sewers should be moved to a self-supporting systems on an enterprise basis in light of large needs in that area; with MAC providing back-up financing and City's economy showing some signs of life, City could make a serious attempt to test the market by late 1982.
Ackerman, MOODY'S

* for credit analysts, evaluation of trend data is key to formulating credit assessments; NYC's financial and economic distress has parallels in other cities; NYC, however, has not been able to demonstrate an ability to manage its broad scope of operations within its limited resources.

* the end of FY 1982 will be the first real benchmark when City must GAAP balance its budget by law, when safeguards of the past will no longer be available, when MAC's debt limit is approached and loan guarantees expire along with pension fund and banks commitments, and oversight will not be over the wage settlements.

* the continued use of stop-gap measures and one-shot revenues is not acceptable; control has not been demonstrated over Board of Ed, Transit Authority and Health and Hospitals Corporation; outstanding litigation threatens, costly solutions may result effecting the very composition of the income base; capital needs are enormous with no plan to address them.

* relationship of MAC to the City needs clarification, MAC's scope and longevity raises questions; indefinite perpetuation of MAC's powers and debt-incurring ability could have a deleterious effect on NYC; the segregation of capital financing from the major governmental unit is not sound and could have serious ramifications.

* proposed amendments to Federal Bankruptcy Law hampers City's efforts to regain market access; NYS's willingness to give blanket consent to all its municipalities to file petitions under Chapter IX is disturbing.

* NYC has disregarded the sound precepts of public administrations and violated elementary principals of maintaining solvency; both the magnitude of problems yet to be addressed and the past history of poor performance must be considered in any calculation of future credibility; the City permitted a default in 1975 and the psychological impact of a default defies quantification but will be a long time in overcoming; regardless, a favorable opinion by a rating agency does not necessarily guarantee investor confidence.

* the City has made progress toward fiscal goals as recognized by improvement in bond ratings from Caa to B and the assignment of ratings to note issues; a definable positive trend has yet to be established, but in general, 3 years of sound balanced budgets would be called a trend.
* Moody's expects the end of FY 1981 or 1982 to mark the beginning of such a trend which, due to NYC's past shortcomings as an issuer, would require much longer than the general rules would indicate reflecting the fact that near term plans don't reflect structural defects and long-term remedial measures.
Rousseau

* successful sale of BANs due to perception of NYS backing - transfer of State aid to NYC from the State Comptroller directly to paying agent.

* the City has established itself in the lower range of acceptable credits in the market place and is subject to all the perils of lesser regarded credits.

* presently it is more a function of the severe stress in the bond market than of NYC's relative standing in that market that makes further NYC note sales uncertain.

* market acceptance is as much a matter of psychology as it is of budgets and balance sheets.

* the investing public will require four things:

(1) a debt service fund mechanism (investors should be exposed to the Debt Service Fund created by the State Legislature in late 1978).

(2) a record of achievement in budget balancing (confidence is elusive even in light of NYC's accomplishments; very high standards are set; early move to GAAP should contribute a great deal; creation of 4-year plan a positive innovation but calls attention to the large budget gaps in the out-years, although most other State/municipal budget projections would have them, too; we must more clearly define gap as opposed to deficit for success).

(3) a capital facilities plan (realistic and believable capital plans to maintain and upgrade the capital stock are a must; slim prospects of City raising $1 billion in a single year ('82) in the tax-exempt market, it would be a feat - NYC should have a detailed contingency plan; some projects should be funded on pay-as-you-go basis).

* a water and sewer entity charged with the operation of those services is recommended, similar to ECP and HDC - and why not hospital, equipment leasing - and retain MAC as an issuer for certain defined capital purposes. Disadvantages to this might be loss of operating flexibility if new revenue streams were restricted by bond covenants; legal structure involved may diffuse political power of Mayor and City Council; potential negative reaction of investors if too many revenues are diverted from General Fund or if it's too confusing.
(4) improved bond ratings (City needs at least minimum
grade rating to market several hundred million per year
under normal conditions; needs an A/A rating to do so
in uncertain markets. City shouldn't rush to market;
to insure lasting success, care and caution is required;
fewer bonds than market could absorb, generous pricing
of early issues).
* NYC has shown substantial achievements: more stringent accounting and budgeting procedures, reducing annual deficits, achieving a degree of public market acceptance.

* Move to GAAP-balance early is crucial since pension funds and financial institutions are nearing saturation point for MAC and unguaranteed City bonds (practical limitations and legal roadblocks).

* MAC cannot be depended on for long-term financing since it has a debt-ceiling, restrictive covenants, and additional issuances would increase contingent NYS debt; investors have viewed MAC as interim measure for NYC, otherwise perceptions of any lack of effort on City's part would negatively affect market acceptance of MAC debt.

* Investment grade rating is key; continuing efforts by City are high priority, strong commitments must be made in the face of labor, budget review, audits and elections; recommend showing raters first-hand how City copes with critical matters to prove its ability to produce predictable financial results.

* NYC is stronger now than in 1975, and meaningful actions have been taken; further improvement is still required, but market re-entry is in sight.
Gotbaum

* workers suffer greatly in time of fiscal austerity; sacrifices imposed on them from all levels of government; small wage increases well below inflation and CPI; there is no optimism regarding future CPI and inflationary trends.

* family income of City workers does not compare favorably to Bureau of Labor Statistics low and intermediate family budget; women with dependent children are especially hard hit.

* workers have suffered from take-backs and lay-offs since FY 1975: changes in work rules, reduction of overtime and summer hours, deferral of wage increases, reduction of ITHP benefits, deferral or reduction of fringe benefits and COLA payments, 30,000 lay-offs, strict attrition policy and non-replacement have caused ever-increasing workloads.

* ever-increasing workloads must be accomplished with old, poorly-repaired equipment, in facilities that are dangerous and deteriorated, creating counter-productive conditions with little City effort to improve them; NYC workers' accident rate is almost 4 times greater than that of all U.S. private business; it's bad workplaces not bad workers that impair productivity.

* union has cooperated with City on broadbANDING civil service titles; they have supported flexibility in internal transfer of personnel; pressed Mayor to institute City-wide productivity council; in general, City and labor have long-standing tradition of cooperation.

* Federal government has not taken lead on productivity; National Productivity Council has made no suggestions; many U.S. cities are going down the tubes, NYC is not unique - it just got there first; stressed need for American Urban Policy; NYC's burden of Medicaid and welfare translates into high unemployment, abandoned property, burdened school systems, postponed capital improvements and repairs.

* while we appreciate loan guarantees, they cost the Feds nothing but they cost NYC a great deal; treatment of NYC as unique has only served to put off dealing with the fundamental inequalities of today's cities.
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Altman

* since 1975, NYC has achieved each of its major fiscal goals; financial accomplishments such as reduction of GAAP-deficit, elimination of deficit entirely during FY 1981, independent audits, reduced borrowing needs and successful sale of notes in 1979 and 1980 deserve recognition.

* the remaining guarantee authority of $900 M will only be used if the City and MAC can't finance long-term needs over the next two years; U.S. has received prompt quarterly payments on the guarantee fee for bonds issued thus far.

* regarding compliance with the guarantee act, the City's continued fiscal reform enhances the security of guaranteed debt thereby meeting the "reasonable prospect of payment"; the financing commitments of financial institutions, pension funds and MAC have been honored; the independent fiscal monitor (FCB) continues; and two years of independent audits were accomplished.

* NYC's budget has shown improvement; 1979 results represent a year of true progress; 1980 budget balanced according to State Law; City has been able to cover problems in Board and Ed and Health and Hospitals Corporation which developed during this year through stronger than expected economy and further expenditure reductions.

* currently proposed City plan of 1/15/80 has not been evaluated although certain monitors place "worse-case" gaps at far greater than plan; NYC has historically ended with smaller than projected budget gaps so this trend may continue.

* even though the FY 1981 budget gap has expanded over projections of such gap last June, several factors can be cited: earlier achievement of GAAP-balanced budget, Federal and State laws already required City to adjust pension costs by $50 M and capitalized operating expense phase-out of $132 M for FY 1981, the inclusion of a provision for wage settlement, increased medicaid, special ed and energy costs, all offset somewhat by increased revenue projections for 1980 and 1981.

* NYC's deficit reduction program (PEG) is ambitious; some actions will be difficult as they require legislation and will be unpopular; overall job reductions appear possible (except maybe Board of Ed) and OTSP cuts appear attainable.
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* PEG uncertainties include ability of Board of Ed to sustain reductions in light of need to maintain services and evaluation of success of new control procedures; present projections of HHC revenues are uncertain and City may be pressed for greater funding; expenditures for energy have rapidly escalated so conservation may not offset costs; and it is too early to judge if increased Federal/State aid is realistic.

* FY 1982 will be a more difficult year for NYC; the FY 1982 deficit may not be realistic since it depends on eliminating gap in 1981, negotiation of restrained labor contracts, the City's ability to make necessary cuts and the uncertainty of prospects for increased Federal/State aid; because of carry-over value of FY 1981 PEG actions, it is disconcerting that alternative programs do not exist.

* recent State budget proposals threaten increased State aid although State commitment is not diminished; preliminary indications of Federal aid to NYC are that it will continue to increase although some increases require legislation; Federal aid is at least less limited than prospects for increased State aid.

* other areas of concern in City's road to fiscal self-sufficiency include uncertainty in the national and local economy, wage settlements, capital spending (past 2 years' slippage in light of recent signs of progress in coordinating and accounting throughout the capital budget system, and restoring access to the bond market through better bond ratings (the City has prepared a strategy for market re-entry with the cornerstone being the achievement of budget stability, management objectives and achieving an investment grade rating). Current limited market for City bonds is insufficient, and it probably couldn't be tapped until FY 1981 anyway.

* if City can't meet its financing needs in FYs 1981 and 1982, MAC has sufficient bonding authority so as to preclude the need for stand-by guarantees.

* the next 12 months will be pivotal for the City's self-financing quest: conclusion and outcome of labor negotiations, whether the City can actually produce a GAAP-balanced budget for 1981, whether a successful sale of a limited amount of City bonds can be accomplished to demonstrate investor confidence; these factors should all facilitate the attainability of an investment grade rating.
It is a pleasure to report that New York City has regained at least partial access to the public capital markets. Just one year ago, in January, 1979, the City sold an issue of $125 million Revenue Anticipation Notes due on June 29, 1979 to an underwriting group of 95 firms. The investing public oversubscribed the issue almost immediately. The City returned to the market once more in its 1979 fiscal year and later sold two more Revenue Anticipation Note issues in the current fiscal year, 1980. The public has purchased a total of $650 million New York City RAN's to date.

This success suggests that investors have regained faith at least in the City's ability to manage its affairs successfully during the span of a single year. It also probably reflects a perception that the notes are secured as much by New York State as they are by New York City. This perception arises from the fact that the repayment mechanism for the notes provides for the transfer of State aid to the City directly from the State Comptroller to paying agent for the notes. Which of these considerations sways investors, and to what degree, is not accurately known.

Although the City has been able to sell its notes publicly, it is important to realize that it has established itself in the lower range of acceptable credits in the marketplace. In this position it is subject to all the perils of lesser regarded credits; relatively high interest rates, less than universal acceptance and, perhaps most importantly, the risk of being crowded out of the market when general conditions deteriorate.
The bond markets are under severe stress now and New York City's ability to sell more notes at an acceptable rate just now is questionable. It is my opinion that this present uncertainty is a function of overall market conditions and does not represent any deterioration in New York City's relative standing in the market.

Although we know much about credit worthiness and how to establish and measure it, we do not know a great deal with certainty about market acceptance, especially in a situation where investor confidence has been completely lost and must be restored, as with New York City. Market acceptance is as much a matter of psychology as it is of budgets and balance sheets. Therefore, I approach with some humility the question of what steps or actions will ensure New York City's access to the long term bond market. In that humble spirit, I would suggest that the investing public will require four things before they will buy the City's bonds in substantial amounts. These are:

I. **A DEBT SERVICE FUND MECHANISM**

Some legally binding arrangement to set aside certain funds for the payment of interest and principal on the City's bonds. Such a mechanism has apparently benefited the Revenue Anticipation Notes sold to date. State Legislation enacted late in 1978 actually did create the Debt Service Fund. It requires a diversion of the City's property tax revenues first to a fund for the payment of interest on notes and bonds and principal on bonds before the money flows to the General Fund. I believe that investors will react very positively to this arrangement when they are exposed to it.
II. A RECORD OF ACHIEVEMENT IN BUDGET BALANCING -

This is an area where much has been accomplished, but confidence seems particularly elusive. From my perspective, the City has set and met increasingly tough goals in each of the past five fiscal years, including the present one. I find it interesting that all parties seem to agree that the City must conform to the very highest standards - full GAAP accounting, strict balance and the narrowest definition of eligibility for capital funding - before it will get any credit for balanced budgets. This is a test that many states and municipalities might find difficult, but is clearly a standard forced on the City by its former excesses. We have advised the City to methodically establish, announce, achieve and brag about achieving budgetary goals to help reinforce the notion that it can and will deliver on its commitments. Frankly, it would appear that public perceptions haven't recovered as much or as rapidly as we had hoped. The City's announced intention to move to full GAAP standards one year ahead of schedule should help materially here.

Ironically, some aspects of the City's much improved fiscal practices may in part be working against it. I refer to the existence of the Four Year Financial Plan, which is by law periodically updated and generally much discussed. I believe its creation and maintenance is one of the most positive innovations in municipal financial management anywhere. However, its existence has led to much discussion of the City's prospective budget gaps in future years. Although probably most state and municipal budget projections would show future gaps under the same analysis, New York City is almost alone in having to identify and discuss them at such great length.
I sense that there is continuing confusion, even among sophisticated observers, about the difference between prospective budget gaps and actual deficits. The continued discussion of future gaps probably reinforces the erroneous notion that the City's present operations are in deficit. They are not, but the impression seems to linger. The antidote we have prescribed again is a patient and repetitive education effort with the general public. Success in this effort is clearly necessary before the public will buy long term bonds.
III. A CAPITAL FACILITIES PLAN

Much has been said about the deterioration of the City's capital stock. We believe that investors will only believe in the City's long term viability when it can be shown that its capital assets are being and will be maintained adequately. The Capital Facilities Plan will thus have to include realistic, adequate and believable projections for capital stock renewal and replacement. It will also have to include current and projected expenditures for new capital facilities. We believe that, to a greater extent than ever before, investors will want to know the specific uses to which their bond investment dollars are being put.

I should interject here my own uncertainty about the total amount that New York City will be able to raise each year in the bond market. Projections beyond 1982 call for the City to raise approximately $1 billion per year there for capital projects. It should be noted that no issuer anywhere has regularly attempted to raise $1 billion per year in the tax exempt market, let alone a recently discredited and perhaps still suspect issuer like New York City. I am not sure that the City won't be able to raise this much, but I think it should have detailed contingency plans on hand in the event it cannot.

If it should develop that the City's capital needs simply to maintain its capital stock exceed the amount it can raise publicly, it will be on the horns of a dilemma. I believe it would have to resolve that dilemma
by funding some capital projects on a pay as you go basis, because I am convinced that the capital markets will not be open to it at all if it cannot demonstrate the ability to maintain its capital asset base. It is at least possible, though, that the City will find that some amount less than $1 billion per year will both be available and suffice for capital stock renewal and moderate expansion. This whole question cannot be addressed in detail until the City completes a list of current capital assets. This exercise, recommended by its outside auditors, is well underway under Comptroller Goldin's supervision.

Further with regard to capital projects, we have suggested that the City consider the creation of several user service enterprises for both operating and capital fund raising purposes. A Water and Sewer entity could be created and charged with the operation of the Water and Sewer System, collection and disbursement of user fees, payment of debt service on the City's existing G.O. water bonds and issuance and repayment of a new class of water and sewer revenue bonds. To a certain extent, this sort of thing has already been done through the creation of the Educational Construction Fund and the Housing Development Corp. It could be extended to include, for example, a Hospital Facilities Authority, and Equipment Leasing Authority, and also an extension of MAC as an issuer for certain defined capital purposes after its role as general capital raising agent for the City has ended.

The disadvantages would seem to be:

1) Possible loss of financial operating flexibility as and if new revenue
bond covenants restricted the City's general access to certain streams of revenue.

2) Depending on the legal structure necessary to establish separate enterprises, a possible diffusion of political strength or loss of control of City functions by the Mayor and City Council.

3) Potential negative investor reaction if the perception developed that too many revenue sources were being diverted away from the General Fund or if the new structure came to seem too complex and difficult to understand.

Even these few important potential advantages and disadvantages argue for a very careful analysis before any concrete steps are taken. We are advising the City to proceed with the analysis, though, and to establish any new enterprise funds before or concurrently with attempting to re-enter the long term bond market in order to provide investors with the clearest and most complete possible picture of the City's future capital raising mechanism from the beginning. New York City would be following the successful example of the City of Philadelphia and, to a lesser extent, other issuers in redeploying its capital raising activities along these lines.

IV. IMPROVED BOND RATINGS -

Progress on bond ratings and market access may have become a chicken and egg problem, although we are not convinced that they should be. We have attempted at all times to remind people that ratings are an effect, not a cause, and that the rating agencies should not be taken to task for what befell New York. On the other hand, I hope that New York City
will not have its past failings held against it to the extent that recent and continuing improvements in its basic condition and its financial management will not be recognized in its ratings.

We do not hold the view that the City has to be all the way back to investment grade status (Baa/BBB) before it can sell any bonds, but we do believe that investors will have to see at least some progress on the bond ratings before they will buy meaningful amounts of City bonds. For the longer run, as a practical matter, the City will have to achieve minimum investment grade ratings before it can expect to raise several hundred million dollars per year in the public markets under normal conditions, and will have to achieve A/A ratings before it can count on doing so even in troubled or uncertain markets.

To recapitulate, the four things that seem necessary for the City to regain access to the bond markets, beyond what it has already done, are:

1) A debt service fund mechanism.

2) A continuing and improving record of achievement in budget balancing.

3) A comprehensive and believable Capital Facilities Plan.

4) Some improvement in bond ratings.

Although achieving these four goals will not absolutely ensure reopening the market for City bonds, it will, especially if it occurs against a backdrop of reasonably normal bond market conditions, almost do so. I would like to emphasize that market psychology will continue to be a very important element of the re-entry process. For that reason, I think it is critically important that the City not be rushed into the market before it seems surely able to sustain itself there.
The first sale of City bonds will have to be carefully and cautiously developed to ensure that it is a success. So will the second. The City and its underwriters must develop a pattern of successful bond sales so that investors will be willing and even eager to buy additional issues as they come along. This will probably require, among other things, offering for sale fewer bonds than we think the market might be able to absorb at one time. It might also require deliberately erring a bit on the side of generosity in pricing early issues. Such a cautious and deliberate approach in re-entering the note market over the past year has, I believe, served the City very well. Lasting successes rather than transitory victories are what the City needs. They are also, I suggest, what the City's present creditors and its present guarantor, the U. S. Treasury, should most encourage. I hope that your Committee's oversight of and direction to New York City will aim to support such a long term program.
FOR RELEASE AFTER 6:30 P.M., SATURDAY, JANUARY 19, 1980.

Senator William Proxmire (D-Wis) awarded New York City Mayor Edward Koch a provisional "A" for his decision to balance the City's budget in the upcoming 1981 fiscal year, rather than delaying until 1982.

Proxmire said, "This shows that the City is getting out front and ahead of the game, rather than playing catch-up ball. If the Mayor carries through on his pledge to achieve full budget balance a year earlier than required by law, then he will get an unqualified "A", because this should do a lot to restore confidence in New York City's ability to put its financial house in order."

Proxmire is Chairman of the Senate Banking, Housing and Urban Affairs Committee, which has jurisdiction over the New York City Loan Guarantee Act. The Committee has scheduled oversight hearings for January 28 and 29 and February 7. The purpose of the hearings is to explore the City's progress toward balancing its budget and regaining access to the credit markets. New York City has been unable to sell its own long-term bonds in the market since the fiscal crisis broke in early 1975.

In a statement issued from his Washington Office late Saturday, Proxmire said:

"Mayor Koch deserves a lot of credit for recognizing the hard, tough facts of life, which are that the only way that New York City is going to get back on its feet and back in the bond markets is to show that it can balance its budget and keep it balanced. And that means budget balance in accordance with generally accepted accounting principles -- cutting out completely the operating expenses in the capital budget and the other reminders of the fiscal crisis that shut the City out of the market.

"However, it is important to note that announcing the budget will be balanced and doing it are two different things. The Mayor's program to eliminate the budget gap ("PEG" program) presents an impressive list of expenditure reductions and tax increases. This is strong medicine designed to cure large

---- MORE -----

OFFICE OF
SENATOR WILLIAM PROXMIKE
WISCONSIN
budget gaps forecast for both the 1981 and 1982 fiscal years. But the effectiveness of these actions is reliant on approval by other parties, including the City Council. It is also reliant on the achievement of a modest labor settlement for the coming two years along the lines of that agreed to in 1978.

"In the course of the oversight hearings, the Committee will take a careful look at the PEG plan to see if it is realistic and workable. There is likely to be particular attention paid to the assumptions of increased revenues from outside sources. The plan projects $150 million in additional State and Federal aid for fiscal 1981, rising to $410 million in 1982, of which at least one-half is expected to come from the Federal government. Inflation is the nation's number one problem, and balancing the Federal budget is a top priority. Thus it is highly debatable whether New York City can rely on balancing its budget on the back of the Federal government.

"The bottom-line question is whether the City is doing all it needs to do to meets its long-term financing needs without further Federal assistance after the loan guarantee program ends on June 30, 1982. In my view, the Federal guarantees were not needed to begin with, and New York City's problems might well have been resolved more quickly had the Federal government not intervened. Certainly there is no disposition on the part of the Congress to extend additional guarantees.

"The Mayor's decision to bite the bullet and balance the budget without taking further advantage of the loopholes in the law is commendable. It should speed the City's re-entry into the credit markets and make it unnecessary for any more Federal guarantees to be issued. The Committee will explore this and related issues in the forthcoming oversight hearings."
NYC Loan Guarantee Act
Jan 28-29, 1980
Feb 7, 1980
SUMMARY OF OVERSIGHT HEARINGS

United States Senate
Committee on Banking, Housing, and
Urban Affairs
New York City Loan Guarantee Act
January 28-29 and February 7, 1980

The City of New York
Summary of Oversight Hearings
United States Senate
Committee on Banking, Housing, and Urban Affairs
New York City Loan Guarantee Act
held on
January 28-29 & February 7, 1980
Summary of Oversight Hearings
United States Senate
Committee on Banking, Housing, and Urban Affairs

New York City Loan Guarantee Act
held on
January 28-29 & February 7, 1980

Senate oversight hearings held in Winter 1980 sought to determine what actions would be necessary for New York City to be able to regain access to the public credit markets in order to meet the ultimate goal of the Guarantee Act--for the City to fully finance itself in the public market.

This summary of the hearings includes the testimony of the witnesses and is intended to provide you with information concerning New York City's fiscal progress and prospects for the future.

Witnesses at the hearings

- U. S. Treasury
- Bond Rating Agencies, Institutional Investors and Underwriters
- Municipal Labor Leaders
- New York City
- New York State
- Municipal Assistance Corporation
- Financial Control Board
- Office of the Special Deputy Comptroller
Testimony focused on the historical causes of the City's fiscal "crisis", its recent fiscal progress, the City's need to achieve and keep a balanced budget according to GAAP in FY81, as announced by the Mayor in his January 16, 1980 PEG submission and the prospects for regaining access to the public credit markets.

**Major issues presented**

The major issues related to the City's ability to meet Mayor Koch's ambitious goal of GAAP balanced budget in FY 1981, a full year ahead of the State and Federal Statutory requirements, and, assuming this budget balancing success, what the prospects for public credit market access would be in determining the City's ability to balance its budget. The following uncertainties will, according to the various witnesses, affect New York City's budget balancing success:

1. **Continuity of State and Federal Aid**
2. **Adjustment of taxes subject to legislative approval by Non-City entities**
3. **Magnitude of deficits in the Transit Authority, Board of Education and HHC**
4. **Negotiation of Wage Settlements**
5. **National Economic Activity Impact on the Local Economy**

With respect to public credit market access, the following major issues were discussed:

1. **The attainability of an investment grade rating**
2. **MAC's ability to maintain public market access**
3. **The likelihood for Federal guarantees in the FY 1981-1982 period**
WITNESS LIST
UNITED STATES SENATE
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
OVERSIGHT HEARINGS ON NEW YORK CITY LOAN GUARANTEE ACT
MONDAY, JANUARY 28, 1980
10:00 A.M.

THE HONORABLE ROGER C. ALTMAN
Assistant Secretary for Domestic Finance, U. S. Department of the Treasury, Washington, D.C.

* * * * *

MS. FREDA STERN ACKERMAN
Senior Vice President & Director, Municipal Bond Department, Moody's Investors Service, New York, New York.

MR. HYMAN C. GROSSMAN
Vice President, Municipal Ratings, Standard & Poor's Corporation, New York, New York.

MR. JEAN J. ROUSSEAU
Managing Director, Public Finance Group, Merrill Lynch White Weld Capital Markets Group, New York, New York.

MR. AMOS T. BEASON
Senior Vice President, Morgan Guaranty Trust Company, New York, New York.

MR. JOHN R. VELLA
Executive Vice President, Bank Investment Securities Division
Bank of America, San Francisco, Ca.
WITNESS LIST

UNITED STATES SENATE

COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

OVERSIGHT HEARINGS ON NEW YORK CITY LOAN GUARANTEE ACT

MONDAY, JANUARY 28, 1980

3:00 P.M.

MR. VICTOR GOTBAUM
Executive Director, District Council 37, American Federation of State, County, and Municipal Employees, New York, New York.

MR. JACK BIGEL (Introduction Only)

MR. ALBERT SHANKER
President, United Federation of Teachers - Local 2, New York, New York.
WITNESS LIST

UNITED STATES SENATE
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

OVERSIGHT HEARINGS ON NEW YORK CITY LOAN GUARANTEE ACT

TUESDAY, JANUARY 29, 1980
10:00 A.M.

THE HONORABLE EDWARD I. KOCH
Mayor, City of New York
Accompanied by:
The Honorable Harrison J. Goldin, Comptroller.
The Honorable Carol Bellamy, President of the Council.

* * * * *

MR. COMER S. COPPIE
Executive Director, New York State Financial Control Board for New York City.

MR. JAMES R. BRIGHAM, JR. (No formal testimony was presented by Mr. Brigham)
Director, Office of Management and Budget, City of New York.

MR. SIDNEY SCHWARTZ
Special Deputy (State) Comptroller for the City of New York.

MR. STEPHEN BERGER
Professor of Public Administration, New York University, and Budget Consultant to the Municipal Assistance Corporation, New York, New York.

MR. EDWARD V. REGAN
Comptroller of the State of New York
WITNESS LIST

UNITED STATES SENATE
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

OVERSIGHT HEARINGS ON NEW YORK CITY LOAN GUARANTEE ACT

THURSDAY, FEBRUARY 7, 1980

THE HONORABLE HUGH L. CAREY
Governor of the State of New York

MR. FELIX G. ROHATYN,
Chairman, Municipal Assistance Corporation for the City of New York
FOR RELEASE ON DELIVERY
EXPECTED AT 10:00 A.M.
January 28, 1980

STATEMENT OF THE HONORABLE ROGER C. ALTMAN
ASSISTANT SECRETARY OF THE TREASURY (DOMESTIC FINANCE)
BEFORE THE SENATE COMMITTEE ON BANKING,
HOUSING AND URBAN AFFAIRS

Mr. Chairman and Members of this distinguished Committee:

I appear before you today to discuss the Treasury Department's activities under the New York City Loan Guarantee Act of 1978. My testimony will cover the following major areas:

--- a recent history of the City's budget and financing developments including the Federal guarantees of City debt and the conditions under which these guarantees were issued;

--- the status of the City's fiscal year (FY) 1980 budget, and the Program to Eliminate the Gap (PEG) for FY 1981 and FY 1982; and

--- a discussion of several key problems affecting New York's financial future, including prospects for the City's regaining access to the public bond market.

RECENT DEVELOPMENTS

Let me put this issue into some perspective by briefly reviewing the history of the New York City fiscal crisis.

M-297
It erupted in 1975 when the City lost access to conventional lending sources and teetered on the edge of bankruptcy. The City lost its ability to borrow because it was incurring enormous budget deficits and had already borrowed huge amounts to finance them. Lenders had lost confidence in the City's ability to repay.

The State of New York then undertook massive efforts to solve the City's fiscal problems. Among other things, it established the Municipal Assistance Corporation (MAC), the Emergency Financial Control Board (EFCB), and advanced $800 million to the City. It was not until Congress passed the New York City Seasonal Financing Act of 1975, however, that the City was actually saved from apparent bankruptcy.

In the intervening four years, New York has met each of its budget goals since Federal credit assistance was first provided in late 1975. It intends to achieve real budget balance -- balance in accordance with Generally Accepted Accounting Principles (GAAP) -- in its fiscal 1981, a full year ahead of schedule.

Several important recent financial strides deserve mention:

-- the City's 1980 budget will reduce its GAAP deficit to approximately one-fifth of the 1976 level and the City's budget has been balanced for the last two fiscal years in accordance with State law.

-- the City's proposed 1981 budget entirely eliminates its GAAP deficit. This compares to a $1.8 billion GAAP deficit in FY 1976.

-- the City was independently audited for the first time in fiscal year 1978 and this was repeated last year.

-- the overhang of short-term debt has been funded. Indeed, its short-term borrowing needs have been cut from as high as $8.4 billion in 1975 to $600 million in fiscal year 1980.

-- the City re-entered the public credit markets in 1979 for the first time since 1975. Two City sales of short-term notes totalling $275 million were oversubscribed by investors and only $375 million of the $750 million pension fund/bank standby credit line was used in fiscal 1979. In fiscal 1980, the City has already sold $375 million
of its notes to the public and now expects to sell up to $225 million more in the public markets, thereby avoiding any use of its standby credit facility, which now consists solely of financial institutions.

Federal Guarantees Issued to Date

Mr. Chairman, since I last testified before you in February 1979, Treasury has issued further Federal guarantees of City bonds as follows:

<table>
<thead>
<tr>
<th>Date</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>February 15, 1979</td>
<td>$150 million</td>
</tr>
<tr>
<td>June 28, 1979</td>
<td>50 million</td>
</tr>
<tr>
<td>August 30, 1979</td>
<td>100 million</td>
</tr>
<tr>
<td>January 3, 1980</td>
<td>150 million</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>$450 million</strong></td>
</tr>
</tbody>
</table>

To date, the aggregate amount of City bonds guaranteed is $650 million. An additional $100 million of guarantees are scheduled to be issued next month. This would complete the $750 million in Federal guarantees which are included in the $4.5 billion long-term financing plan as "up-front" guarantees. The $900 million of remaining guarantee authority will only be used in the unlikely event that both the City and MAC are unable to finance the City's long-term needs in the next two years.

The United States has received prompt quarterly payments from the City of the one-half percent guarantee fee provided under the Guarantee Act. At the end of December, these payments totalled $2,070,053.47.

The Guarantees

On each issuance of Federal guarantees, Treasury must determine that the City is in compliance with the conditions
of eligibility set forth in the Guarantee Act. Your Committee
staff has been provided with copies of the formal determinations
made before each issuance. I will devote a significant
portion of my testimony reviewing the most important aspects
of the City's compliance with the Guarantee Act -- budget
balance and credit market progress. I think it important,
however, to mention briefly the City's compliance with certain
other areas of the Guarantee Act.

Reasonable Prospect of Repayment

Federal guarantees of City debt cannot be issued unless
there is a "reasonable prospect" that the principal and
interest on the outstanding guaranteed indebtedness will be
repaid. Since these Federally-guaranteed obligations have
maturities of up to fourteen years, Treasury evaluates this
"reasonable prospect" in terms of the City's long-term fiscal
and economic health. We have found that both the strength
of the City's economy and the demonstrated local commitments
to continued budgetary and financial reform enhance the
security of the guaranteed debt.

One recent change in the financing program will be of
interest to you, Mr. Chairman. According to the City's latest
financial plan, in FY 1983 the City anticipates refunding $180
million of its Federally-guaranteed bonds. This represents
24% of the principal amount of guaranteed bonds projected to be
outstanding by the end of FY 1980, exceeding the 15% refunding
requirement under the Guarantee Act.

Financing Commitments

The local financial institutions and City pension funds
have maintained their commitments to purchase unguaranteed
Municipal Assistance Corporation securities. Also, MAC has
sold its bonds to the public on schedule. We expect these
parties to continue to meet their financing commitments
in FY 1981 and FY 1982 in accordance with the City's
financing plan.

Independent Fiscal Monitor

Section 103(6) of the Guarantee Act requires that "an
independent fiscal monitor" -- the Financial Control Board -- "has
the authority to control the financial affairs of the City...."
The Control Board has exhibited broad financial control, review
and supervisory powers over the City on its course toward fiscal recovery.

Financial Reporting and Accountability

Another aspect of the City's creditworthiness relates to the City's financial reporting and control systems. Since 1975 the City improved significantly in this area through the implementation of its Integrated Financial Management System (IFMS).

To comply with Section 103(7)(a) of the Guarantee Act, the City has been audited in two consecutive years by a consortium of independent certified public accountants. There are few large municipalities that can claim a like accomplishment.

Beyond this major improvement, and as a result of the Guarantee Act, the City has established an actively functioning Audit Committee in order to address and review major accounting issues affecting New York City. The improvement of the City's record-keeping system, the implementation of annual independent audits, and the establishment of an Audit Committee are all positive developments.

THE NEW YORK CITY BUDGET

The key to restoring New York's ability to finance itself is for it to attain true balance in the City budget and to maintain that balance. On this basis, institutional lenders and the credit rating agencies will regain confidence in the City's debt. The Guarantee Act recognized this by requiring the Treasury Department to determine, prior to each issuance of a Federal guarantee, that the City's budget is in balance under New York State law and that the City is making substantial progress toward balance according to GAAP in FY 1982.

FY 1979 Results

The City incurred a $422 million deficit on a GAAP basis in fiscal 1979. This represented an improvement of $290 million over the 1978 deficit level. Indeed, this improvement occurred even though $116 million of revenues, originally projected for 1979, will be realized in later years. The principal reason that New York remains in GAAP deficit at all is its continued practice of funding certain operating expenses from its capital budget.
The Guarantee Act requires the City to phase out this practice by budgeting no more than $450 million of these so-called capitalized expenses in fiscal 1979, $300 million in fiscal 1980, $150 million in fiscal 1981 and zero in fiscal 1982. In fiscal 1979, the City voluntarily began to accelerate this phase-out schedule.

In contrast to the $422 million GAAP deficit, under accounting principles prescribed by New York State law the City realized a $216 million surplus in 1979. Thus, fiscal 1979 was a year of financial progress for the City.

**FY 1980**

Fiscal 1980 has also been another year of budget improvement. In January 1979, the City announced its preliminary 1980 budget, that included a set of actions to eliminate a potential deficit under State law of $433 million. These measures included up to $250 million of City actions and at least an additional $183 million in State and/or Federal assistance.

The actual 1980 budget, adopted in June 1979, was balanced on a State law basis. A substantial increase in City's revenue, in addition to a proportional mix of City, State and Federal actions eliminated the potential deficit. Due to various uncertainties, the Financial Control Board (FCB) requested that the City detail a contingency program of more than $100 million of City actions if FY 1980 balance could not be maintained as the year progressed.

As fiscal 1980 unfolded, serious budget problems developed in the Board of Education and the Health & Hospitals Corporation (HHC). In December, the City was required to establish an additional reserve of $50 million to cover potential budget gaps in HHC and allocate an additional $19 million of support for the Board of Education.

Yet, stronger than expected revenue growth and further expenditure reductions enabled the City to tackle these mid-year problems and still remain in balance under State law without implementing the contingency program required by the FCB. Indeed, even though $135 million of forecasted FY 1980 revenues are now targeted for FY 1981, the City's net revenues are projected at $38 million above the adopted budget.

This reserve strength enabled New York to avoid in 1980 the type of sharp spending cuts which would have resulted if the
The City had to implement its contingency program. It might have been wise to voluntarily reduce City expenditures further, in light of the large potential 1981 and 1982 budget gaps, but the City chose a milder course.

**The Fiscal 1981 and Fiscal 1982 Budgets**

On January 16, Mayor Koch released his preliminary 1981 budget. The Treasury Department has had only 11 days to evaluate this plan and our conclusions, therefore, are highly preliminary. We are not required by the Loan Guarantee Act to make findings concerning the success of this plan until the next issuance of guarantees, currently scheduled for February 21.

The PEG plan would attain the long sought goal of true budget balance according to GAAP next year. This would be one year earlier than required by Federal and State law and is a courageous step.

The City estimates that attaining this FY 1981 goal will require eliminating a potential deficit of $677 million. Moreover, if this 1981 gap is not closed, it will grow to approximately $1.1 billion in 1982. Certain fiscal monitors, using various "worst-case" assumptions, have estimated considerably larger potential gaps in each of these years -- in excess of $1 billion in FY 1981 and growing to $2 billion in FY 1982.

These estimated gaps are large, but it is important to put them into perspective.

**Background**

Table 1 below compares the City's performance against its budget goals for FY 1976-FY 1979. As you will note, the City has met or exceeded each of its budget goals over this period.
TABLE I
Actual Budget Results Compared to Original Budget Goals ($ millions)

<table>
<thead>
<tr>
<th></th>
<th>City's Goal Under State Law</th>
<th>Year-End Budget Results Under State Law</th>
<th>Year-End Budget Results Under GAAP</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY 1976</td>
<td>$1,051 deficit</td>
<td>$968 deficit</td>
<td>$1,822 deficit</td>
</tr>
<tr>
<td>FY 1977</td>
<td>$ 686 deficit</td>
<td>$329 deficit</td>
<td>$1,039 deficit</td>
</tr>
<tr>
<td>FY 1978</td>
<td>Balance</td>
<td>$ 32 surplus</td>
<td>$ 712 deficit</td>
</tr>
<tr>
<td>FY 1979</td>
<td>Balance</td>
<td>$216 surplus</td>
<td>$ 422 deficit</td>
</tr>
</tbody>
</table>

The large differences between the original projections and the actual results reflect the inherent conservatism in revenue and expenditure assumptions in the City's budget methodology. In effect, the process itself requires that potential budget gaps be overstated.

Specifically, the City did not include non-recurring revenues in its forecasts, even though varying amounts of such revenue occur each year. Furthermore, the City did not reduce its expenditure forecasts to reflect likely spending shortfalls ("underspending") even when such shortfalls appeared certain.

Finally, the City has generally used conservative assumptions to forecast its economically-sensitive revenues. Actual revenues have frequently exceeded plan, as they did in FY 1980.

In short, the real budget gaps have invariably been smaller than the originally estimated gaps. This could again be the case in the future.

Fiscal 1981

Last June, the City forecast a 1981 deficit of $464 million on the State law basis. The recently released preliminary 1981 budget, however, estimated this gap at $677 million. The principal elements of the 1981 deficit outlook are as follows:

-- the Mayor's decision to reach budget balance one year early increases the potential deficit by $275 million.
This includes the elimination of $150 million of incremental capitalized expenditures and $128 million of incremental pension costs;

-- aside from this mayoral decision, Federal and State laws in effect already required the City to adjust for increases of $50 million in pension costs and $132 million in phased-out capitalized expenditures;

-- an assumed 4% wage increase in 1981 (the same as that in 1978) which the City estimates will cost approximately $142 million in that year. This is the first estimate by the City of its future labor costs;

-- an increase in Medicaid payments, of which the City's share is $102 million;

-- a $65 million increase in energy costs and a legally mandated $64 million increase in expenditures for special education;

-- these increased costs are somewhat offset by two categories of increased revenue: realization in 1981 of $155 million previously projected for this year; and a revised estimate that 1981 city tax receipts will be $33 million higher than the 1980 level.

**City Deficit Reduction Actions**

The City has proposed $507 million in its own deficit reduction actions to help close this $677 million potential gap. These include:

-- improved collection techniques and other steps resulting in $33 million of increased revenue;

-- the Mayor's decision to increase taxes and certain other charges to produce increased revenues of $175 million. This includes $39 million in increased water and sewer charges, $36 million in increased real estate taxes, and $35 million in increased excise taxes on beer and liquor;

-- expenditure reductions of $299 million consisting primarily of $165 million of reductions in the City's personnel budget and $83 million of non-personnel reductions.

Table II details the major items in this City program.
### TABLE II
1981 City Program
($ in millions)

#### Revenue Actions

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Improved Rental Income Collection</td>
<td>$6</td>
</tr>
<tr>
<td>Increased License and Permit Fees</td>
<td>5</td>
</tr>
<tr>
<td>Reduced Provision for Disallowances</td>
<td>10</td>
</tr>
<tr>
<td>Increase in Inter-Fund agreements</td>
<td>5</td>
</tr>
<tr>
<td>Other</td>
<td>7</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$33</strong></td>
</tr>
</tbody>
</table>

#### Tax and Charge Increase to Yield
$175 million/year

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Water and Sewer Charge Increase</td>
<td>$39</td>
</tr>
<tr>
<td>Real Estate Tax Increase</td>
<td>36</td>
</tr>
<tr>
<td>Excise Tax on Beer and Liquor</td>
<td>35</td>
</tr>
<tr>
<td>Financial Corporation Tax Revision</td>
<td>20</td>
</tr>
<tr>
<td>City Gasoline Tax Extension</td>
<td>13</td>
</tr>
<tr>
<td>Parking Garage Tax Increase</td>
<td>11</td>
</tr>
<tr>
<td>Hotel Tax Revision</td>
<td>11</td>
</tr>
<tr>
<td>Tax on Taxi Medallion Transfer</td>
<td>8</td>
</tr>
<tr>
<td>Real Estate Tax - Veterans Exemption</td>
<td>7</td>
</tr>
<tr>
<td>Other</td>
<td>12</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$192</strong></td>
</tr>
</tbody>
</table>

Less Possible Slippage

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less Possible Slippage</td>
<td>(17)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$175</strong></td>
</tr>
</tbody>
</table>

#### Agency Expenditure Reductions

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Police</td>
<td>$29</td>
</tr>
<tr>
<td>Fire</td>
<td>11</td>
</tr>
<tr>
<td>Correction</td>
<td>14</td>
</tr>
<tr>
<td>Social Services</td>
<td>25</td>
</tr>
<tr>
<td>HRA</td>
<td>18</td>
</tr>
<tr>
<td>Board of Education</td>
<td>111</td>
</tr>
<tr>
<td>CUNY</td>
<td>5</td>
</tr>
<tr>
<td>All other</td>
<td>35</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$248</strong></td>
</tr>
</tbody>
</table>

#### Other Reductions

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Transit, Housing and Other Subsidies</td>
<td>$9</td>
</tr>
<tr>
<td>HHC Subsidy</td>
<td>20</td>
</tr>
<tr>
<td>Energy Conservation Program</td>
<td>12</td>
</tr>
<tr>
<td>OTPS Cost Containment</td>
<td>10</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$51</strong></td>
</tr>
</tbody>
</table>

**TOTAL**

<table>
<thead>
<tr>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>$507</strong></td>
</tr>
</tbody>
</table>
It will not be easy to realize the full $507 million of projected City actions. Most of the revenue actions and tax increases will require the cooperation of the City Council and/or the State Legislature. Although tax increases are never popular, some local support for these actions has been reported.

Concerning spending, Mayor Koch has proposed major cuts in the personnel budget totalling $165 million. This means a net reduction in City-funded jobs of approximately 5,000. It includes a net cut of 3,100 in education personnel, and 722 in the uniformed police force. The overall job reductions appear possible, although they may be particularly difficult in the education area.

Regarding non-personnel cuts, the $83 million projected 1981 reduction also appears attainable. In each of the past three years, the City's actual reductions in this area have exceeded those projected in each January's PEG plan.

There are several uncertainties among these City actions, however, including the following:

--- the ability of the Board of Education to sustain reductions of the magnitude proposed by the City while maintaining services at an acceptable level. New control procedures to provide additional oversight over the fiscal affairs of the Board have been instituted. These controls should facilitate the implementation of these cuts;

--- the City's plan to reduce its subsidy to the Health and Hospitals Corporation (HHC). Present projections of HHC revenues are uncertain today. Although the City is under no legal obligation to fund HHC deficits, it has done so in the past;

--- City expenditures for energy, which have been rising rapidly.

The City's 1981 Plan also calls for unspecified State and Federal actions totalling $170 million. It is simply too early to judge whether this estimate is realistic. Governor Carey's State budget was released only one week ago, and President Carter's proposed 1981 Federal budget will be released today. I will discuss in greater detail the prospects for intergovernmental aid in a later portion of my testimony.
Fiscal 1982

Fiscal 1982 will be a more difficult year for New York City. Assuming the City is able to close the $677 million gap in FY 1981, through significant and recurring City expenditure reductions, revenue actions and tax increases, and moderate increases of Federal and State assistance, a potential $462 million budget gap still remains. The principal cost elements in this additional gap are:

-- an additional $189 million provided to fund a 4% wage settlement;

-- $75 million to cover increasing energy costs;

-- an additional allocation of $62 million of City funds for Medicaid;

-- an additional $49 million allocated to the Board of Education for Special Education.

There is considerable uncertainty, however, as to whether this $462 million 1982 deficit estimate is realistic. It remains to be seen whether the City can negotiate fiscally restrained labor contracts covering 1981 and 1982. In addition, its projections call for a large increase in State and Federal aid for 1982, which will be difficult. Finally, the 1982 deficit will automatically be larger if the City fails to eliminate the full $677 million 1981 potential gap on a recurring basis. A judgment on whether a large 1982 gap can be closed depends on an assessment of (1) whether the City has the capacity to make further large cuts, and (2) what can be expected of Federal and State aid in the out-years.

The City's plan proposes an additional $222 million in City actions and $240 million in State and Federal actions to close this gap. Table III shows the major items in the 1982 program, their combined 1981 and 1982 values as well as their incremental value.

As you will note from Table III, the program the City proposes for fiscal 1982 consists primarily of actions initiated during the previous fiscal year. These actions have an increased value because they are expected to be more fully phased-in during the latter year. Therefore, the comments I made regarding the 1981 program are applicable here as well. It is a matter of some concern that the City has not identified alternative programs for 1982 given the likelihood that some of the PEG actions will fail to meet the City's expectations.
<table>
<thead>
<tr>
<th>Revenue Actions</th>
<th>Total Value</th>
<th>FY 1982 Incremental Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Implement Semi-Annual Real Estate Tax Payments</td>
<td>$32</td>
<td>$32</td>
</tr>
<tr>
<td>Increase CUNY Tuition</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>Continuation of 1981 Actions</td>
<td>56</td>
<td>23</td>
</tr>
<tr>
<td><strong>Total Revenue Actions</strong></td>
<td>93</td>
<td>60</td>
</tr>
<tr>
<td>1981 Tax and Fee Increases</td>
<td>175</td>
<td></td>
</tr>
<tr>
<td><strong>Agency Expenditure Reductions PS/OTPS</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Police</td>
<td>38</td>
<td>9</td>
</tr>
<tr>
<td>Fire</td>
<td>17</td>
<td>6</td>
</tr>
<tr>
<td>Sanitation</td>
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<td>7</td>
</tr>
<tr>
<td>Corrections</td>
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<td>Social Services</td>
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<td>2</td>
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<tr>
<td>Board of Education</td>
<td>182</td>
<td>71</td>
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<tr>
<td>CUNY</td>
<td>6</td>
<td>1</td>
</tr>
<tr>
<td><strong>All Other</strong></td>
<td>59</td>
<td>26</td>
</tr>
<tr>
<td><strong>Total Agency Reductions</strong></td>
<td>382</td>
<td>134</td>
</tr>
<tr>
<td><strong>Other Reductions</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transit, Housing and Other Subsidies</td>
<td>12</td>
<td>3</td>
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<tr>
<td>HHC Subsidy</td>
<td>20</td>
<td></td>
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<tr>
<td>Energy Conservation Program</td>
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<td>14</td>
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<tr>
<td>OTPS Cost Containment</td>
<td>21</td>
<td>11</td>
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<tr>
<td><strong>Total Other Reductions</strong></td>
<td>79</td>
<td>28</td>
</tr>
<tr>
<td><strong>TOTAL CITY ACTIONS</strong></td>
<td>$729</td>
<td>$222</td>
</tr>
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</table>
Since 1975, the City has shown the capacity to meet its budget goals and, year after year, it has eliminated huge projected deficits. The continuing commitment of City and State elected officials to the City's financial well being is solid. Mayor Koch's resolve to reach a GAAP balanced budget in FY 1981, a year ahead of an already rigorous schedule, is the best evidence of this commitment.

State Aid

New York State faces serious budget pressures of its own in its fiscal year 1981. Therefore, its recently announced Executive Budget is extremely tight. The combination of certain formula-driven increases in expenditures, tax-reduction programs and the possible impact on the State of a recession threaten future increases in aid to the City. Despite these budget difficulties, the State's commitment to the City's recovery remains undiminished. During the State's fiscal years 1976-1980 Governor Carey successfully supported significant increases in State aid to New York City. In FY 1980 alone, State assistance to the City increased by more than $200 million.

Federal Aid in 1981 and 1982

Our preliminary indications of the President's FY 1981 budget proposal are that Federal aid to the City will continue to increase into the 1980's as it has every year since 1976.

Modest increases in aid to the City may be forthcoming, but they are in the area of legislation. I am referring to programs such as targeted fiscal assistance, countercyclical revenue sharing, and Medicaid and welfare funding reform.

Specifically, the two anti-recession fiscal assistance programs (actually two parts of one bill), if passed by Congress in one of their present forms, would increase unrestricted aid to the City by as much as $45 million in City FY 1981 and perhaps a greater amount in FY 1982, depending on local economic conditions. In addition, the Administration is working on a proposal to broaden eligibility criteria for Medicaid, and the increased Federal reimbursement rate for the Aid to Families with Dependent Children (AFDC) program could free up additional City funds annually. None of these proposals, of course, are assured of passage.
In addition to these actions which will require legislative approval, the Administration continues to work on a series of administrative actions, primarily in the area of public housing, that would provide recurring fiscal relief.

The more limited ability of the State to provide additional significant amounts of budget aid means that the City may require major increases in Federal fiscal assistance to meet 1981 and 1982 budget goals. Obviously, the Administration has provided assistance to the City in the past. It continues to work for legislative programs to assist this country's urban areas with their unique problems. We are hopeful that Federal assistance, together with State and City actions will eliminate future budget gaps.

There are other areas of concern in the City's road to financial self sufficiency. A discussion of these follows.

THE NATIONAL AND LOCAL ECONOMY

A major factor in evaluating the City's prospects relates to the impact of the projected recession. A national recession was widely projected to begin during the last quarter of 1979 and continue into late 1980. The mixed signs over the past few months raised some doubt about the timing and duration of the recession. The major forecasting agencies are now projecting a moderate recession that will be more severe than the downturn projected in the late summer, but not as severe as the 1974-75 recession. In any event, it appears the local economy is better prepared for a recession than it was in 1973:

- the City's employment levels, after drastic decline since 1969, have stabilized;

- the decline in manufacturing employment and a move toward service oriented industries makes local employment generally less affected by cyclical swings in the economy;

- the automobile and construction industries appear to be on the leading edge of the forecasted recession -- the City does not have a heavy dependence on automobile production, and commercial construction is experiencing a boom, particularly in the borough of Manhattan;

- retail sales on a City-wide basis have continued to outperform the national averages.
Hence, if the severity of the recession is no worse than currently projected, our judgment is that the City's projections should not be seriously askew.

WAGE SETTLEMENTS

The City's estimates of budget deficits have not previously included the cost of potential wage settlements in FY 1981 and FY 1982. The City has now included in its baseline estimates the funding of a 4% wage settlement in FY 1981 and FY 1982. The prospective costs of such a wage settlement are estimated by the City at $142 million in FY 1981 and $331 million in FY 1982. Last Thursday the City's unions announced their unwillingness to settle for 4% annual increases as they did in 1978. On the other hand, Mayor Koch has indicated to the City's municipal labor leaders not to expect to receive the same increases provided in existing pacts -- which are 4%. Ultimately, the wage settlement will be negotiated, hopefully on reasonable terms, between the City and its unions.

CAPITAL SPENDING

Another important factor in the City's attempt to achieve economic stability and financial independence is its capital spending program. Though not specifically related to the City's near-term financial future, the City's ability to provide an attractive environment for its citizenry and for economic development purposes will be an essential element in the City's long-term fiscal health.

One critical factor in support of the Guarantee Act was the establishment of a credible financing package for the City so that improvement of its physical plant could get back on track.

Four years of neglect caused by the City's fiscal crisis have left the City's infrastructure in a somewhat deteriorated condition. Yet, the City has been slow in using capital funds provided for rebuilding. We appreciate the massive job of totally reactivating a capital program which has been dormant for four years. Nevertheless, the City must make a maximum commitment to improve its capital planning process.

Early projections for FY 1980 capital spending were $582 million. Subsequently, this estimate was lowered to $440 million. The City's new Four-Year Plan, however, indicates
further "slippage" to $394 million. We have carefully monitored the City's capital spending and consider this estimate reasonable. In connection with this latest reduction, however, the City did indicate that the $2.3 billion capital spending goal in the FY 1979-1982 period was reachable.

Over the last few months the City has shown signs of progress in this area by coordinating the activities of all City agencies under one central office and improving accountability throughout the capital budget system.

RESTORING ACCESS TO THE PUBLIC BOND MARKET

A major factor in the restoration of the City's long-term fiscal and economic independence will be its ability to find adequate sources of long-term credit in the public markets. Under the Guarantee Act, the City must attempt to sell its own bonds to meet a portion of its long-term financing needs in FY 1980.

Moody's Investors Services currently rates the City's bonds "B", which is below investment grade. Until an investment grade rating is achieved, the City will experience difficulties in attaining significant market access. In its review of the City's credit, Moody's commented that "fundamental credit elements are demonstrably weak and the City's long-term general obligation bonds continue to lack the characteristics of a desirable investment." The other major rating agency, Standard and Poor's, has maintained its rating suspension of City securities since April 1975.

The absence of a suitable credit rating on its bonds has the practical effect of excluding, among other investment groups, banks, insurance companies, trust departments and municipal bond funds from purchasing long-term City bonds.

While there may be a limited demand for New York City bonds among individual investors, without the participation of institutional investors New York will not achieve full financing independence. The City has prepared a strategy to fully enter the public credit market.

The cornerstone of this strategy is to achieve budget stability and other management objectives which appear to be crucial in obtaining an investment grade rating. The City's budget progress in fiscal 1980 and its bold step in accelerating
the phase-in of a GAAP balanced budget for fiscal year 1981 can only improve its chances for an investment grade rating. The conclusion of the upcoming collective bargaining negotiations with the City's workforce will resolve another major uncertainty.

As for tapping the limited, individual investor market for City bonds, Mayor Koch has stated that "the existence of this uncertain market, while encouraging, cannot serve as the basis of any long-range solutions to the City's credit needs, since it simply cannot provide the substantial amounts of capital regularly required by the City." Current market conditions and the uncertainties surrounding the forthcoming labor negotiations seem to mitigate against such an attempt prior to FY 1981.

FY 1981 and 1982

As you are aware, Mr. Chairman, the City's financing schedule calls for it to sell $300 and $645 million of unguaranteed bonds to the public in FY 1981 and FY 1982, respectively. The Guarantee Act requires such an effort. Without an investment grade rating, however, institutional investors will be unlikely participants in such an offering. It is equally unlikely that the requisite amounts of bond sales under the Guarantee Act in FY 1981 and FY 1982 can be met solely through sales to individual investors on reasonable terms. Any amounts the City cannot finance independently are to be covered, in the first instance, by MAC.

If the City is unable to access the bond market over the next two years, MAC has sufficient bonding authority to issue, on behalf of the City, its own bonds. In addition, we believe that MAC will have sufficient market access so as to preclude the issuance of stand-by Federal guarantees.

The next twelve months will be pivotal in the City's self-financing quest:

-- the conclusion of the forthcoming wage negotiations with the City and its municipal unions will eradicate a major uncertainty in the City's financial plans;

-- the City will have provided a budget balanced in accordance with GAAP;

-- a successful sale of a limited amount of bonds in the public market, without an investment grade rating, will demonstrate investor confidence in the City's fiscal progress.
These factors should facilitate the City's ability to achieve an investment grade rating -- a critical step in the City's ultimate goal of financing independence.

I will close by emphasizing that the City has shown the willingness and wherewithal to take whatever steps necessary to meet its statutory budget and financing requirements. The City's and State's commitment to continuing this record is clear. We, therefore, remain satisfied that the City, the State and other interested parties are making the maximum effort as required by the Guarantee Act to solve the City's fiscal and financing difficulties.

This concludes the prepared portion of my testimony. I will be pleased to respond to any questions at this point.
ORAL TESTIMONY PRESENTED BEFORE
THE SENATE COMMITTEE
ON BANKING, HOUSING, AND URBAN AFFAIRS

MONDAY, JANUARY 28, 1980

BY

FREDA STERN ACKERMAN
SENIOR VICE PRESIDENT
MOODY'S INVESTORS SERVICE
My name is Freda Stern Ackerman. I am Senior Vice President and Director of the Municipal Bond Department of Moody's Investors Service, headquartered in New York City.

You have asked for our opinion as to "whether the requirements of the New York City Loan Guarantee Act are being met and to assess what progress New York City is making toward balancing its budget in accordance with generally accepted accounting principles and toward regaining access to the credit markets."

* * * * *
As credit analysts, we look to historical trend data in order to assist us in making evaluations as to future performance. This is an established procedure of credit analysis. Whether governmental administrations change or not, observation of trends in the basic areas of general obligation bond analysis provide the foundation for the credit analyst's judgment. Certainly, more than just trend data are looked to in formulating our assessments, but they constitute the core.

The term trend is commonly defined as the general movement in the course of time of a statistically detectable change. That is exactly the kind of measurement we make as credit analysts and is the kind of performance the City must demonstrate before their numbers become believable.

Ideally, a unit of government is able to demonstrate that it is in a sound condition before the incurrence of debt. Within its current financial structure and using current economic conditions as a guide, a unit should have no difficulty in making projections that show budgetary balance can be maintained, supplemented by positive margins available to deal with possible future adversities. As we all know, however, ideal conditions do not always exist, and we in fact have assigned investment grade ratings to many situations where less than optimum conditions prevail. To keep repeating that New York's case is made unique by many factors including the sheer magnitude of the numbers involved avoids addressing this point. There are numerous other large cities which are experiencing both financial and economic distress, and while New York is surely the largest, many parallels can be seen. Why then, do we and the financial community in general
express so much skepticism about New York while we are able to characterize those other cases as adequate? The basic reason relates to a unit of government's ability to demonstrate control within its limited resources. Indebtedness derives protection by virtue of the municipality's capability to deal with budget problems in a budgetary context. New York City has not yet been able to meet this test. It has not demonstrated an ability to manage its broad scope of operations with all their attendant problems within its resources. Until this is achieved, financial health will remain elusive.

* * * * *

* * * * *
We see the end of the 1981-82 fiscal year as the first real benchmark for a number of reasons. Failure to maximize savings and deficit reduction during the early years of the 1975-79 carry-over period now places the City in the position of having to achieve its required balanced operations by 1982 at the latest, a year when the City will no longer be able to rely on certain past safeguards.

MAC is expected to be near its presently constituted debt limit, debt issuance under the federal guarantee program will have expired, the commitments of the pension funds and Clearing House Banks will have been fully honored, wage settlements will no longer fall under the oversight of the FCH and the inclusion of expense items in the capital budget will no longer be permitted.

Certain remedial measures must be taken in order to provide for substantive and not merely technical reform. Revenues and expenditures must be brought into balance, something not yet realistically accomplished. The continuation of the use of stop-gap measures and one-shot revenues is not acceptable.

There must be demonstrated control over the operations of the covered and mayoral agencies: namely the Board of Education, Transit Authority and Health and Hospitals Corporation.

As yet unresolved are numerous pieces of outstanding litigation against the City which carry the threat of very costly solution. The very composition of the income base of the City is currently precariously tied to the whole question of mandated re-assessments which could
easily cause dramatic shifts in taxpayer components. As a lifetime resident of New York City, I unfortunately can attest to the well documented deterioration which has occurred in the physical plant. Capital needs are enormous and no long term plan of action exists to address this problem.

The relationship between the Municipal Assistance Corporation and the City needs further clarification. MAC has served a useful purpose and has served it well; however, numerous questions are raised as to MAC's scope and longevity. Indefinite perpetuation of the Corporation's powers and debt incurring ability could possibly have a deleterious effect on the formulation of the City's remedial plans. Over and above this, it is not considered a sound principle of public administration to segregate so important a function as capital financing from the body of the government; the loss of control to the unit can have serious ramifications.

Proposed amendments to the Federal Bankruptcy Law (Chapter IX) will, if allowed to remain in their present form, have the undesirable effect of hampering the City's efforts of regaining access to the public credit markets through the sale of general obligation bonds. Another disturbing point relating to Chapter IX remains New York State's willingness to give blanket consent (contained in Title 6-A of the Local Finance Law), without prior approval on a case by case basis, to all its municipalities to file petitions under Chapter IX.
Restoration of creditor confidence in New York City will be a burdensome task. The City's problems go far deeper than accounting practices. The City has disregarded the sound precepts of public administration; it has violated the most elementary rules for maintaining fiscal solvency. Although it has adhered rather well to date to the conditions prescribed by the various fiscal monitors, the long term perspective remains clouded. The magnitude of the problems yet to be addressed and the history of past poor performance must both be included in any calculation of future credibility. One very significant point not to be overlooked is the fact that the City, in the winter of 1975, permitted a default to occur, regardless of the euphemism created to characterize the action. Defaults in the municipal bond industry in the post-war period have been rare occurrences. There are various federal regulations prohibiting bank purchase of securities for a period of years after a default which will curtail potential buyers dramatically. More importantly, the negative psychological impact of a default on private as well as institutional purchasers almost defies quantification. The building and maintaining of confidence can be a tenuous act and one has great difficulty when trying to assess the future state of trust in overlooking or discounting past violations of that trust. For all the words and numbers coming out of the City and all its monitors, there have as yet been few concrete, positive actions taken toward resolving the problems; the one overriding action that was taken, the default on the $2,419,395,000 general obligation tax and revenue anticipation notes, carries a negative connotation that will be a long time in overcoming.
As credit analysts and raters of municipal securities we represent one viewpoint out of many in the marketplace. Our opinion, expressed in the form of ratings and the research we publish, is generally looked to by other market elements in making their judgments as whether to buy or sell a security and at what price. Certainly the Committee is aware that we have no fundamental control over these other judgments; a favorable opinion by a rating agency of an issuer's debt does not necessarily guarantee investor acceptance.

The City of New York has undeniably made progress toward restoring order to its finances. We recognized that progress by revising the rating on its general obligation bonds from Caa, a default level, to B in 1977 and by assigning ratings to the City's note issues. However, recognition of progress should not obscure the fact that the City started out from a position of extreme disorder which has yet to be fully remedied by the City itself. We have spent a large portion of this testimony discussing the importance of analyzing past performance trends in order to make future projections. We have yet to see a clearly definable positive trend for the City. The general rule in financial analysis is that three years of sound, realistically balanced operations can be defined as a trend. We expect the end of fiscal 1981 or 1982, whichever the City chooses, to mark the beginning of that trend which, in the case of an issuer so previously unmindful of the principles of sound administration, would require much longer than the generally accepted rules for it to be adequately characterized. As we stated in our municipal credit report of May 7, 1979, reviewing the City's bond rating:
Although the crisis atmosphere of earlier years has abated, the need for timely and comprehensive City action to cope with existing, fundamental weaknesses is paramount to restoration of credit worthiness. Near term plans now in place do not address structural defects and long range remedial measures have yet to be adopted. The overall credit outlook remains highly uncertain.
Statement of Hyman Grossman, Vice President, Municipal Ratings

Standard & Poor's Corporation

U. S. Senate Committee on Banking, Housing & Urban Affairs

For Release after 10:00 a.m., January 28, 1980

Mr. Chairman, as you know, I am here on behalf of Mr. Brenton W. Harries, President of Standard & Poor's Corporation, whose prior business travel commitments made his personal appearance here impossible. Your invitation to appear today indicated that the purpose of the hearing was to assess what progress New York City is making towards balancing its budget in accordance with generally accepted accounting principles and toward regaining access to the credit markets.

Perhaps a good point of departure would be to recall some of the points made by Mr. Harries a little over two years ago before this same committee. Mr. Harries indicated then that "... the City will be unable to borrow in the public debt market in a meaningful way until it can demonstrate fiscal stability through dependably balanced budgets with an outside
monitoring system." The same thing can pretty much be repeated today; and showing only one year would probably not be enough. That is why the Mayor's January 15 modification of the Financial Plan, bringing the City within the guidelines of generally accepted accounting principles in fiscal 1981, a year ahead of the 1982 requirement by law, assumes great potential significance. More about that a bit later.

My message to you today is that the City has made progress in moving to generally accepted accounting principles, but full access to the free public marketplace for other than limited note sales remains elusive -- and even the recent note sales are no real test of the City's credit, as their security is based upon state aids received late in the year after the State itself does its own spring borrowing. I had frankly thought that a relatively small City bond sale, even without an investment-grade rating, could have reached the market at a reasonable cost last August or September. What I had in mind was a 15-year bond issue of some $50 to $75 million. However, with the escalated yield trend since early October of last year, that chance has disappeared; and I do not see a current marketing of City bonds at what one could consider a reasonable rate. New York City bonds would have to carry a yield in fifteen years well in excess of the current scale of 9.50 percent for Detroit or 9 percent for Philadelphia, compared with the 8.25 percent for the Municipal Assistance Corporation. About the only municipal entity now close to the
New York City problem is the Chicago Board of Education, whose bonds in the secondary market (such as are available) are in the 10 percent range for fifteen years.

Much has been said in the past about New York City's unique attributes -- its size, its strengths and its weaknesses. Indeed, New York City over the years bit off more than it could chew. Spending patterns developed that could not be reversed and when ongoing solid revenues were not there to pay for it, the shortfall was borrowed and rolled over year after year until the snowball, if you will, just got too heavy and the collapse resulted. New York City is now showing the symptoms of withdrawal. The City is slowly and painfully moving off the crutch of easy short-term borrowing for deficit financing and on to meeting expenses with a more reliable stream of revenues. The large scale governmental service sector in the City, built over many years with comparatively easy money, makes retrenchment very difficult indeed.

Progress has been made, however; and the January 15 modification is an accelerated step in the same direction. Beginning with the year ending June 30, 1976, the unaudited year-end deficit under generally accepted accounting principles was $1.87 billion, followed by $1.04 billion in 1977. The City's first outside audit report covered the 1978 year which reported a deficit of $712 million, followed by a deficit of $422 million at June 30, 1979. This is good progress, and the outside audit process and fiscal monitoring in place is also
something that must be maintained to enhance credibility and keep the City's feet to the fire. The estimated deficit for 1980 is placed at about $400 million.

This brings us to the January 15 modification in the Financial Plan, which calls for elimination of the deficit beginning in Fiscal 1981 -- that is, in the next budget. The estimated gaps to be closed are $677 million in 1981 and $1.1 billion in 1982. Although the City portion of the program to eliminate the gap rightly represents the largest portion of the program -- $507 million in 1981 and $729 million in 1982 -- dependence upon prospective federal and state legislative actions also remain an important ingredient and are of some concern in examining the total picture. Most of the City reductions will be in the area of education; a most difficult part of the City's operations and labor negotiations loom on the horizon. The new modification also shows the impact of inflation -- especially fuel costs upon City operations, which compound the problem of closing the gap.

Although progress can be said to have been made in the City's movement to GAAP, it has been and continues to be a difficult process. It is also important to note that continued federal and state aids remain an important part of the fiscal picture.

In the area of borrowing, progress has been made here, too, as the City's short-term needs have been reduced to the $500 to $800 million annual range, down from over $2.1 billion
four years ago. We have for more than ten years suggested that the City and the State of New York work together to even out the cash flow calendar so that anticipatory borrowing could be reduced for all units. The State has only recently indicated a movement in that direction, and it is possible that New York State's movement to GAAP will also prove to be a painful experience -- the dimensions of which have, as yet, not been at least publicly explored.

We have suggested that the City consider moving its water and sewer systems to a fully self-supporting enterprise basis and the subsequent issue of enterprise revenue bonds. Since a good deal of long-range capital borrowing will have to be done in this area over the years, it would seem logical to pull this substantial financing package away from the general purpose type of capital borrowing. With the Municipal Assistance Corporation providing some backstop borrowing power and the City's economy (which is so important to long-term viability) showing some signs of at least blotting the seepage of the last twenty years, the City could by late 1982 make a serious attempt to test the market on its own.

To the extent we can be of additional assistance, we will be glad to answer questions at this time.

HG:dmh
It is a pleasure to report that New York City has regained at least partial access to the public capital markets. Just one year ago, in January, 1979, the City sold an issue of $125 million Revenue Anticipation Notes due on June 29, 1979 to an underwriting group of 96 firms. The investing public oversubscribed the issue almost immediately. The City returned to the market once more in its 1979 fiscal year and later sold two more Revenue Anticipation Note issues in the current fiscal year, 1980. The public has purchased a total of $650 million New York City RAN's to date.

This success suggests that investors have regained faith at least in the City's ability to manage its affairs successfully during the span of a single year. It also probably reflects a perception that the notes are secured as much by New York State as they are by New York City. This perception arises from the fact that the repayment mechanism for the notes provides for the transfer of State aid to the City directly from the State Comptroller to paying agent for the notes. Which of these considerations sways investors, and to what degree, is not accurately known.

Although the City has been able to sell its notes publicly, it is important to realize that it has established itself in the lower range of acceptable credits in the marketplace. In this position it is subject to all the perils of lesser regarded credits; relatively high interest rates, less than universal acceptance and, perhaps most importantly, the risk of being crowded out of the market when general conditions deteriorate.
The bond markets are under severe stress now and New York City's ability to sell more notes at an acceptable rate just now is questionable. It is my opinion that this present uncertainty is a function of overall market conditions and does not represent any deterioration in New York City's relative standing in the market.

Although we know much about credit worthiness and how to establish and measure it, we do not know a great deal with certainty about market acceptance, especially in a situation where investor confidence has been completely lost and must be restored, as with New York City. Market acceptance is as much a matter of psychology as it is of budgets and balance sheets. Therefore, I approach with some humility the question of what steps or actions will ensure New York City's access to the long term bond market. In that humble spirit, I would suggest that the investing public will require four things before they will buy the City's bonds in substantial amounts. These are:

I. A DEBT SERVICE FUND MECHANISM

Some legally binding arrangement to set aside certain funds for the payment of interest and principal on the City's bonds. Such a mechanism has apparently benefited the Revenue Anticipation Notes sold to date. State Legislation enacted late in 1978 actually did create the Debt Service Fund. It requires a diversion of the City's property tax revenues first to a fund for the payment of interest on notes and bonds and principal on bonds before the money flows to the General Fund. I believe that investors will react very positively to this arrangement when they are exposed to it.
II. A RECORD OF ACHIEVEMENT IN BUDGET BALANCING

This is an area where much has been accomplished, but confidence seems particularly elusive. From my perspective, the City has set and met increasingly tough goals in each of the past five fiscal years, including the present one. I find it interesting that all parties seem to agree that the City must conform to the very highest standards — full GAAP accounting, strict balance and the narrowest definition of eligibility for capital funding — before it will get any credit for balanced budgets. This is a test that many states and municipalities might find difficult, but is clearly a standard forced on the City by its former excesses. We have advised the City to methodically establish, announce, achieve and brag about achieving budgetary goals to help reinforce the notion that it can and will deliver on its commitments. Frankly, it would appear that public perceptions haven’t recovered as much or as rapidly as we had hoped. The City’s announced intention to move to full GAAP standards one year ahead of schedule should help materially here.

Ironically, some aspects of the City’s much improved fiscal practices may in part be working against it. I refer to the existence of the Four Year Financial Plan, which is by law periodically updated and generally much discussed. I believe its creation and maintenance is one of the most positive innovations in municipal financial management anywhere. However, its existence has led to much discussion of the City’s prospective budget gaps in future years. Although probably most state and municipal budget projections would show future gaps under the same analysis, New York City is almost alone in having to identify and discuss them at such great length.
I sense that there is continuing confusion, even among sophisticated observers, about the difference between prospective budget gaps and actual deficits. The continued discussion of future gaps probably reinforces the erroneous notion that the City's present operations are in deficit. They are not, but the impression seems to linger. The antidote we have prescribed again is a patient and repetitive education effort with the general public. Success in this effort is clearly necessary before the public will buy long term bonds.
III. A CAPITAL FACILITIES PLAN

Much has been said about the deterioration of the City's capital stock. We believe that investors will only believe in the City's long term viability when it can be shown that its capital assets are being and will be maintained adequately. The Capital Facilities Plan will thus have to include realistic, adequate and believable projections for capital stock renewal and replacement. It will also have to include current and projected expenditures for new capital facilities. We believe that, to a greater extent than ever before, investors will want to know the specific uses to which their bond investment dollars are being put.

I should interject here my own uncertainty about the total amount that New York City will be able to raise each year in the bond market. Projections beyond 1982 call for the City to raise approximately $1 billion per year there for capital projects. It should be noted that no issuer anywhere has regularly attempted to raise $1 billion per year in the tax exempt market, let alone a recently discredited and perhaps still suspect issuer like New York City. I am not sure that the City won't be able to raise this much, but I think it should have detailed contingency plans on hand in the event it cannot.

If it should develop that the City's capital needs simply to maintain its capital stock exceed the amount it can raise publicly, it will be on the horns of a dilemma. I believe it would have to resolve that dilemma
by funding some capital projects on a pay-as-you-go basis, because I am convinced that the capital markets will not be open to it at all if it cannot demonstrate the ability to maintain its capital asset base. It is at least possible, though, that the City will find that some amount less than $1 billion per year will both be available and suffice for capital stock renewal and moderate expansion. This whole question cannot be addressed in detail until the City completes a list of current capital assets. This exercise, recommended by its outside auditors, is well underway under Comptroller Goldin's supervision.

Further with regard to capital projects, we have suggested that the City consider the creation of several user service enterprises for both operating and capital fund raising purposes. A Water and Sewer entity could be created and charged with the operation of the Water and Sewer System, collection and disbursement of user fees, payment of debt service on the City's existing G.O. water bonds and issuance and repayment of a new class of water and sewer revenue bonds. To a certain extent, this sort of thing has already been done through the creation of the Educational Construction Fund and the Housing Development Corp. It could be extended to include, for example, a Hospital Facilities Authority, and Equipment Leasing Authority, and also an extension of MAC as an issuer for certain defined capital purposes after its role as general capital raising agent for the City has ended.

The disadvantages would seem to be:

1) Possible loss of financial operating flexibility as and if new revenue
bond covenants restricted the City's general access to certain streams of revenue.

2) Depending on the legal structure necessary to establish separate enterprises, a possible diffusion of political strength or loss of control of City functions by the Mayor and City Council.

3) Potential negative investor reaction if the perception developed that too many revenue sources were being diverted away from the General Fund or if the new structure came to seem too complex and difficult to understand.

Even these few important potential advantages and disadvantages argue for a very careful analysis before any concrete steps are taken. We are advising the City to proceed with the analysis, though, and to establish any new enterprise funds before or concurrently with attempting to re-enter the long term bond market in order to provide investors with the clearest and most complete possible picture of the City's future capital raising mechanism from the beginning. New York City would be following the successful example of the City of Philadelphia and, to a lesser extent, other issuers in redeploying its capital raising activities along these lines.

IV. **IMPROVED BOND RATINGS**

Progress on bond ratings and market access may have become a chicken and egg problem, although we are not convinced that they should be. We have attempted at all times to remind people that ratings are an effect, not a cause, and that the rating agencies should not be taken to task for what befell New York. On the other hand, I hope that New York City
will not have its past failings held against it to the extent that recent and continuing improvements in its basic condition and its financial management will not be recognized in its ratings.

We do not hold the view that the City has to be all the way back to investment grade status (Baa/BBB) before it can sell any bonds, but we do believe that investors will have to see at least some progress on the bond ratings before they will buy meaningful amounts of City bonds. For the longer run, as a practical matter, the City will have to achieve minimum investment grade ratings before it can expect to raise several hundred million dollars per year in the public markets under normal conditions, and will have to achieve A/A ratings before it can count on doing so even in troubled or uncertain markets.

To recapitulate, the four things that seem necessary for the City to regain access to the bond markets, beyond what it has already done, are:

1) A debt service fund mechanism.
2) A continuing and improving record of achievement in budget balancing.
3) A comprehensive and believable Capital Facilities Plan.
4) Some improvement in bond ratings.

Although achieving these four goals will not absolutely ensure reopening the market for City bonds, it will, especially if it occurs against a backdrop of reasonably normal bond market conditions, almost do so. I would like to emphasize that market psychology will continue to be a very important element of the re-entry process. For that reason, I think it is critically important that the City not be rushed into the market before it seems surely able to sustain itself there.
The first sale of City bonds will have to be carefully and cautiously developed to ensure that it is a success. So will the second. The City and its underwriters must develop a pattern of successful bond sales so that investors will be willing and even eager to buy additional issues as they come along. This will probably require, among other things, offering for sale fewer bonds than we think the market might be able to absorb at one time. It might also require deliberately erring a bit on the side of generosity in pricing early issues. Such a cautious and deliberate approach in re-entering the note market over the past year has, I believe, served the City very well. Lasting successes rather than transitory victories are what the City needs. They are also, I suggest, what the City's present creditors and its present guarantor, the U. S. Treasury, should most encourage. I hope that your Committee's oversight of and direction to New York City will aim to support such a long term program.
Statement

of

Amos T. Beason
Senior Vice President
Morgan Guaranty Trust Company

before the

Committee on Banking, Housing, and Urban Affairs

of the

Senate of the United States

January 28, 1980
Washington, D.C.
Senator Proxmire, Members of the Committee,

My name is Amos T. Beason. I am a Senior Vice President of Morgan Guaranty Trust Company, responsible for the bank's activities in the underwriting and trading of municipal securities and in providing public finance advisory services.

I appreciate the opportunity to share with you my thoughts about the City of New York's fiscal recovery process and where it is in that process. Naturally, I can speak only for my own bank, but I believe the views I express are shared rather widely by other financial-market observers of New York City's affairs.

I am sure I speak for the financial community generally in commending the Committee, its Chairman, and its staff for the constructively critical interest they have shown in New York City.

New York City needs access to short-term credit for its legitimate seasonal financing requirements and access to long-term credit to finance the maintenance of its infrastructure and the addition of capital improvements needed to serve its citizens.

New York City will have completed its fiscal recovery when it once more can meet those financing needs - short term and long term - on its own, when it no longer must resort to the props that were devised to keep it going after its loss of access to the public markets.

When the recovery process was started in 1975 no one thought that it would be easy. In magnitude the City's financial problems were unprecedented. During the last five years the Federal government, the State of New York, the City's elected officials, its labor unions, and New York financial institutions have all had to stretch in order to keep New York City financed. Today, the human, financial, and political resources applied to the process of fiscal recovery have
began to show substantial, measurable results.

These results include:

1. Operating under more stringent budgeting and accounting procedures, including an annual independent audit, and under the review of the Financial Control Board,
2. Reducing annual budget deficits, and
3. Achieving a degree of public-market acceptance as evidenced by four successful public note sales totaling $650 million in the past two fiscal years.

Mayor Koch recently stated his intention that the City would operate under a balanced budget - balanced in accordance with generally accepted accounting principles - one year earlier than had been scheduled.

Such progress is crucial because some of the financial support that has carried the City for the last five years will not be available after fiscal 1982. Even if municipal pension funds were to consider adding to the substantial amounts of MAC bonds and unguaranteed City bonds they hold, Congressional approval would be required before they could act. The financial institutions that have come to the City's aid are limited in how much further credit they can extend by their duties to depositors, policy holders, and shareholders.

Nor can the Municipal Assistance Corporation be regarded as a long-term financing vehicle for the City. MAC has a debt ceiling, which cannot be changed without legislative and bond-holder approvals. It also has restrictive covenants which could limit its long-term financing flexibility, and the issuance of additional MAC bonds would increase the contingent debt of the State of New York. Further, I believe that investors regard MAC as a secure device meant to serve until the City regains access to the marketplace and
that if they came to feel that the City were not making every effort to return to the bond market under its own name, market acceptance of MAC bonds would be negatively affected.

In the minds of most professionals, a prerequisite to the City's full return to the debt market is that its bonds carry investment grade ratings. Because of the complexity of the City's finances and its recent history, sufficient time must be devoted to obtaining even minimum investment grade ratings. For that reason, continuing efforts leading to improved ratings must remain a high priority of key City officials. This will require a strong commitment despite the demands of labor negotiations, budget reviews, independent audits, and election campaigns. In view of the difficulty of understanding and rating a complex credit, the City's approach to the rating agencies must be on-going, with the objective of seeing that the City is accorded the highest rating consistent with its financial condition at a given time. I should think that credit analysts may want to gain first-hand impressions over time of how City officials cope with such critical matters as labor negotiations, revenue shortfalls, expenditure over-runs, and capital planning. After all, a rating and its improvement over time will be based not only on analysis of financial data, but equally important, on the confidence of the analysts in the willingness of City officials to retain financial practices which they embraced in adversity and their ability to produce predictable financial results in the future.

I believe the City has a significant message to convey to the rating agencies today. The last time the rating agencies gave the City an "A" rating was in the spring of 1975. New York is a stronger city today than it was then. Its financial results are measurable and its revenue base has grown. The public sector as a percentage of City gross product has declined. Elected
officials, recognizing that affordable government can be equated with good politics, have taken meaningful actions to improve the way the City's financial affairs are handled.

Further improvement clearly is still required of New York City, but I think the worst is behind it and its goal of regaining entry to the public debt markets is in sight.
There has been considerable discussion in recent months by a variety of concerned parties on the question of whether the City of New York can sell bonds in the national marketplace during the next fiscal year. The question, obviously, is a very delicate one, and while the institution which I represent is a major participant in the tax-exempt bond market, it would be presumptuous of me to speak for any institution other than my own regarding the underwriting or investment viewpoints of non-New York firms on City of New York securities. My opinions, as they are expressed here today, reflect only the considered judgment of my colleagues at the bank, and do not represent — or pretend to represent — a consensus view of out-of-state commercial banks and investments dealers on the question of market access by the City of New York.

The city has been unable to sell its bonds in the public market since 1975. In our opinion, this situation will continue to prevail until, at the least:

1) a balanced budget can be produced and maintained for at least three consecutive fiscal years;

2) a comprehensive, long-term economic development program is firmly in place, describing specific objectives and procedures which can be quantified and measured during the course of the program relative to a timetable of interim and final goals;
3) a systematic, long-range capital improvement program is adopted, such that major elements of the city's infrastructure are sufficiently established and maintained to ensure a viable context for future growth and development.

It may be possible, as some have suggested, for the city to sell a modest amount of bonds in the public market during the next fiscal year. We believe, however, that beyond the token effect which such a sale would signify, the rates would be so high and the class of investors so limited that the effort would be scarcely worthwhile. The principal objective, after all, is for the city to be able to access the public market in size and at reasonable interest rate levels, such that: 1) the capital needs of the city may be financed, fully and dependably; and 2) the borrowing costs of such financing are tolerable, relieving the city of any excessive outlays for interest payments of funds which could otherwise be used for productive purposes.

The City of New York has made noticeable progress in recent years towards rationalizing its budgetary position and embarking upon a surer path to financial and economic well-being. But the journey on that path has just begun, given the length of the path and the milestones which have yet to be reached. Nonetheless, it is the opinion of Bank of America that such milestones are in fact achievable, in the form mainly of consistently balanced budgets, a comprehensive economic development plan, and a systematic program for capital improvements. We believe, furthermore, that once such results are demonstrated: 1) the likelihood in due course of obtaining an investment-grade credit rating will be measurably enhanced; and 2) the opportunity for a full-scale market entry by the City of New York will once more become a reality.
TESTIMONY OF VICTOR GOTBAUM, EXECUTIVE DIRECTOR
OF DISTRICT COUNCIL 37, AMERICAN
FEDERATION OF STATE, COUNTY AND
MUNICIPAL EMPLOYEES

Before the U.S. Senate Committee
on Banking, Housing and Urban Affairs

January 28, 1980
I am pleased to be here today to speak on the contributions of New York City's workers to the present solvency of the City.

I am a labor leader and I expect that when I am asked to speak it is the point of view of labor that is desired. I shall leave the fiscal analyses to the fiscal experts and the issue of market entry to those who make their livings trying to read the market.

I will address myself to what I know best, the workers of the City of New York. I can tell you that they are hurting badly from their share of the fiscal belt tightening and sacrifices imposed by all levels of government.

In addition to the fiscal austerity there has been the onslaught of inflation, continually eroding their paychecks and preventing the small wage increases won in collective bargaining from being worth much at all. Since June, 1975, the New York City area CPI has increased about 35%. A conservative projection would be that by June 1980 it will have gone up almost 40%. During this same period, New York City's workers' net pay has gone up considerably less. (See Table I) For lower-paid workers, such as the Nurses Aide or Senior Clerk, inflation rose faster than pay by 11-12%; for Librarians and Social Workers, the gap is about 15%; for Accountants, 18½%; and for Engineers the difference approaches 25%. The dollar losses in monthly purchasing power range from approximately $60/month for the lower paid workers to approximately $125/month for the Librarians and Social Workers to almost $250/month for the Engineer. And, these workers cannot look forward at the moment to any likely slowdown of inflation.
PREPARED BY: The Department of Research and Negotiations, District Council 77, New York City

January 1980

over the period relatively more than other titles which did not receive an equivalent increase.

1. Social Workers had an education differential built into their rate during 1975 under the terms

of a contract agreed to before the fiscal crisis, boosting the social worker's monthly net wage.

2. Clerical titles were broadbanded during this period; the former senior clerk was automati-

cally reassigned to the title of office aide but experienced no adjustment in salary level.

3. Clerical titles were broadbanded during this period; the former senior clerk was automati-

cally reassigned to the title of office aide but experienced no adjustment in salary level.

The New York area CPI and real net wages for 6/75 are estimates based on a 4% change in the

annual average CPI for 1974-75 and an 8% change 1976-80.

<table>
<thead>
<tr>
<th>Title</th>
<th>Monthly Net Wage</th>
<th>NYC Area CPI</th>
<th>Change in Real Monthly Net Pay</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ - 448.91</td>
<td>16.3%</td>
<td>33.6%</td>
<td></td>
</tr>
<tr>
<td>$ - 420.83</td>
<td>17.64%</td>
<td>32.68%</td>
<td></td>
</tr>
<tr>
<td>$ - 149.39</td>
<td>18.6%</td>
<td>32.68%</td>
<td></td>
</tr>
<tr>
<td>$ - 128.67</td>
<td>19.5%</td>
<td>31.54%</td>
<td></td>
</tr>
<tr>
<td>$ - 105.42</td>
<td>21.4%</td>
<td>31.54%</td>
<td></td>
</tr>
<tr>
<td>$ - 77.82</td>
<td>23.3%</td>
<td>31.54%</td>
<td></td>
</tr>
<tr>
<td>$ - 65.80</td>
<td>25.2%</td>
<td>31.54%</td>
<td></td>
</tr>
<tr>
<td>$ - 57.47</td>
<td>27.1%</td>
<td>31.54%</td>
<td></td>
</tr>
<tr>
<td>$ - 49.1%</td>
<td>29.0%</td>
<td>31.54%</td>
<td></td>
</tr>
<tr>
<td>Engineer</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Social Worker</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accountant</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Motor Vehicle Operator</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Librarian</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Custodial Assistant</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Senior Clerk/Ollege Aide</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nurse's Aide</td>
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<td></td>
<td></td>
</tr>
</tbody>
</table>

(6/80 DOLLARS)
Economic hardship is very real for our members. The inadequacy of their salaries to provide life's necessities cannot be ignored. A study by our Research Department, examining our members' family circumstances and their family income in the summer of 1978 revealed that 20-30% of our members were then earning less than the Bureau of Labor Statistics' (BLS) low budget amount appropriate to their family size, and 45% more were earning less than the appropriate intermediate family budget. In total, then, about 75,000 District Council 37 members are likely to be in families where the earnings fall below the appropriate BLS intermediate family budget for New York City. Counting dependents, there may be as many as a quarter of a million people experiencing this hardship.

Many of our members are women who are not currently married and have dependent children. Our Research Department estimates that 40% of them earn less than the appropriate BLS low budget, with another 52% falling between the low and intermediate budget levels. Thus, more than 90% of our members who are not currently married and have dependents earn less than the BLS New York City intermediate family budget for their appropriate sized family. And, we all know that segment of our workforce is growing very rapidly.

Now, it is true that we do not take workers' family considerations into account directly when determining their pay. But, we must take account of their economic hardship. Their sacrifices have been real and their economic hardship is tangible. That is borne out by the data I have presented.

But their sacrifices and their hardship go beyond the ravages of inflation on their paychecks. In the immediate days
of the fiscal crisis of 1975 it was take-backs and layoffs:

WAGE AND FRINGE BENEFIT CUTS AND DEFERRALS SUFFERED BY THE GENERAL WORKERS OF NEW YORK CITY

11/74 - 1/75  Waiving of past due welfare fund contributions, changes in work rules, reductions in scheduled overtime, elimination of summer hours, etc.

6/75  Deferral of all or part of a scheduled 6% wage increase due on July 1, 1975

4/76  Reduction of Increased-Take-Home-Pay benefit (Increased 2% pension contribution)

6/76 - 6/78  Deferred/reduced fringe benefits, fiscal years 1977-1978

6/76 - 6/78  Deferral of difference between a .4 COLA and a .3 COLA, fiscal years 1977 and 1978

The value of the losses in pay and fringe benefits exceed $400 million.

Layoffs of our members numbered about 30,000. Layoffs and a strict attrition policy have resulted in a drop of almost a quarter of New York City's filled full-time positions since the end of FY75. The elimination of more than 60,000 full-time positions and thousands more part-time positions has been no small accomplishment. It has meant a considerable increase in the workloads for those who remain.

At the same time the fiscal crisis austerity has meant that this increased workload is often performed with out-moded and unmended equipment and in deteriorated and dangerous conditions. For too many of the City's workers, there are offices with broken windows, no heat, and peeling paint; welfare centers with rats and roaches; work-sites without functioning toilets and with exposed asbestos. Such demeaning conditions are clearly counter-productive; yet the City makes minimal effort to improve them.
Then, too, there is the danger. The sad fact is that too many City employees are being maimed on the job. Highway laborers on improperly marked work-sites are struck and seriously injured or even killed by passing vehicles. Drivers of City owned trucks are forced to drive improperly inspected vehicles which often lack brakes, proper lighting, or good tires. Such trucks are rolling death-traps for their drivers and other motorists. Tree sprayers use pesticides without proper protective equipment and training and are thus subjected to skin rashes, burns, anemia, stomach disorders, and even brain damage. Workers in hospital laundry rooms breathe cotton fibers and are subject to lung cancer and cancer of the digestive track.

New York City employees have an accident and injury rate which is astounding. As the table below indicates, in 1977, the accident rate for City employees was almost four times greater than for all private sector employees, and it exceeded that for coal miners, the most hazardous private sector occupation.

<table>
<thead>
<tr>
<th>ACCIDENT RATES FOR SELECTED GROUPS OF EMPLOYEES - 1977</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accidents per one Million hours of Work</td>
</tr>
<tr>
<td>--------------------------------------------------------</td>
</tr>
<tr>
<td>All U.S. Private Business</td>
</tr>
<tr>
<td>Coal Miners</td>
</tr>
<tr>
<td>New York City Employees</td>
</tr>
</tbody>
</table>

These facts and the working conditions they describe should tell you much about the demoralization of the workforce. Lack of productivity - anywhere - stems from bad workplaces,
not bad workers. With the best will in the world, three workers cannot be expected to do the work of five when equipment is deteriorated and dangerous and the workplace itself is decrepit and depressing.

And, still, efforts have been made toward increasing productivity in these circumstances. They have been made because they must. Because there are dedicated public employees who want to serve the public; because there are dedicated managers who want to see that the best services are provided; and because the public demands it.

This Union has co-operated with management in the broadbanding of civil service titles, to allow for greater management flexibility in staffing and to open up promotions and new responsibilities for workers. We also support a more flexible system of internal transfers of personnel within the City.

We also pushed the Mayor to set up the City-wide Productivity Council mandated by the Federal Loan Guarantee Act. It is not our fault that the Mayor placed responsibility with two Deputy Mayors who left in mid-year. I have strong hopes that a reconstituted Productivity Council, which will begin meeting in February, will address some of the pressing issues of the management of public services. New York City labor and management have a long tradition of co-operation on this issue. We want it to continue and will work in that direction.

However, national efforts are really needed on the question of improved service productivity -- public and private. New York City's productivity is certainly no worse than that in
other local governments and in non-governmental service industries. But so far the lead of Washington has not materialized. The Federal civil service has not led the way; nor have suggestions from the National Productivity Council. We hope there will be a serious and creative examination of this issue, because it is common to all local governments and to the wider, growing service sector.

One needs only to look at the fiscal problems in Chicago to know that, really, all the problems that this Committee has investigated with respect to New York City are pervasive urban problems. "The city that works" doesn't anymore. It never really did for many of its residents and its workers. One can add Detroit and Wayne County, Cleveland, San Francisco, St. Louis, New Orleans, Newark and others to the growing list of cities in trouble. New York City was not a special case; it was not unique. It simply got there first. And now that it has been followed, the need for an American Urban Policy becomes pressing.

We who have been to the brink and have painfully worked ourselves back from it know the stumbling blocks which were in the way. The nation's cities, particularly the old ones, carry the burden of the country's poor on their backs. New York City's share of Medicaid and welfare approach $1 billion. But, beyond that, the burden expresses itself in the higher unemployment rates, the abandonment of property, the tremendous burdens on the school systems for special classes, the post-ponement of capital improvements and repairs and its accompanying general aura of disrepair.
We in New York appreciate the loan guarantees. We feel we are demonstrating that they were the right thing for Congress to have done. But, ultimately they have not cost the Congress or the U.S. government anything. They have cost the workers of the City of New York plenty. But, too, they have cost the other cities of this country something. Treating New York City as if it were a special case has simply put off dealing with the fundamental inequalities of today's cities. Lost opportunities are real costs. I hope they can be eliminated.
Statement by Mr. Jack Bigel of Program Planners Inc.

INTRODUCTION

Senator Proxmire, the distinguished Chairman of this Committee, in his letter of January 8, clearly set forth the purposes of this hearing:

"[It] is to determine whether the requirements of the Act are being met and to assess what progress New York City is making toward balancing its budget in accordance with generally accepted accounting principles and toward regaining access to the credit markets."

In accordance with that mandate our statement will describe the achievement of amazing progress, using 1975 as the benchmark year. In fiscal year 1975 the City:

- issued $8.4 billion in short-term debt (see Table 1);
- its short-term financing was equal to 69.9% of the operating budget (see Table 1);
- it had an operating deficit (in accordance with generally accepted accounting principles) that exceeded $1.8 billion;
- the public financing markets were closing to the city;
- financial record keeping was at a minimal level;
- was on the verge of bankruptcy.

This should be compared with the current state of affairs:

- the City will issue less than $600 million of short-term debt in FY 1980;
Table 1

Comparison of NYC's Operating Expenses and Short-Term Debt Issue
For Fiscal Years 1940-1979

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Total Operating Expenses</th>
<th>Short Term Debt Issue</th>
<th>Year's Issue of Short Term Debt as a Percent of Operating Expenses</th>
</tr>
</thead>
<tbody>
<tr>
<td>1979</td>
<td>$12,755,776,000</td>
<td>$ 650,000,000</td>
<td>5.1%</td>
</tr>
<tr>
<td>1978</td>
<td>13,580,291,647</td>
<td>2,073,000,000</td>
<td>15.3%</td>
</tr>
<tr>
<td>1977</td>
<td>13,583,309,000</td>
<td>2,300,000,000</td>
<td>16.9%</td>
</tr>
<tr>
<td>1976</td>
<td>12,349,071,000</td>
<td>6,038,902,987</td>
<td>48.9%</td>
</tr>
<tr>
<td>1975</td>
<td>12,017,684,521</td>
<td>8,395,745,000</td>
<td>69.9%</td>
</tr>
<tr>
<td>1974</td>
<td>10,247,642,736</td>
<td>7,305,915,000</td>
<td>71.3%</td>
</tr>
<tr>
<td>1973</td>
<td>9,560,927,970</td>
<td>4,003,285,000</td>
<td>41.9%</td>
</tr>
<tr>
<td>1972</td>
<td>8,497,773,904</td>
<td>5,248,960,000</td>
<td>61.8%</td>
</tr>
<tr>
<td>1971</td>
<td>7,822,342,445</td>
<td>6,512,240,000</td>
<td>83.3%</td>
</tr>
<tr>
<td>1970</td>
<td>6,700,803,800</td>
<td>4,400,925,000</td>
<td>65.7%</td>
</tr>
<tr>
<td>1969</td>
<td>6,058,823,974</td>
<td>3,270,995,000</td>
<td>54.0%</td>
</tr>
<tr>
<td>1968</td>
<td>5,290,788,916</td>
<td>2,427,717,000</td>
<td>45.9%</td>
</tr>
<tr>
<td>1967</td>
<td>4,492,797,211</td>
<td>2,076,036,800</td>
<td>46.2%</td>
</tr>
<tr>
<td>1966</td>
<td>3,774,733,084</td>
<td>3,645,597,560</td>
<td>43.6%</td>
</tr>
<tr>
<td>1965</td>
<td>3,341,783,221</td>
<td>1,469,989,800</td>
<td>44.0%</td>
</tr>
<tr>
<td>1964</td>
<td>3,098,265,632</td>
<td>1,166,728,800</td>
<td>37.7%</td>
</tr>
<tr>
<td>1963</td>
<td>2,789,112,984</td>
<td>807,658,800</td>
<td>29.0%</td>
</tr>
<tr>
<td>1962</td>
<td>2,601,408,634</td>
<td>842,238,000</td>
<td>32.4%</td>
</tr>
<tr>
<td>1961</td>
<td>2,428,223,378</td>
<td>697,700,000</td>
<td>28.7%</td>
</tr>
<tr>
<td>1960</td>
<td>2,244,808,814</td>
<td>703,743,000</td>
<td>31.3%</td>
</tr>
<tr>
<td>1959</td>
<td>2,081,308,139</td>
<td>665,643,000</td>
<td>32.0%</td>
</tr>
<tr>
<td>1958</td>
<td>2,002,500,191</td>
<td>534,190,000</td>
<td>26.7%</td>
</tr>
<tr>
<td>1957</td>
<td>1,912,607,869</td>
<td>563,300,000</td>
<td>29.5%</td>
</tr>
<tr>
<td>1956</td>
<td>1,782,260,575</td>
<td>479,230,000</td>
<td>26.9%</td>
</tr>
<tr>
<td>1955</td>
<td>1,630,706,797</td>
<td>499,501,450</td>
<td>30.6%</td>
</tr>
<tr>
<td>1954</td>
<td>1,517,417,222</td>
<td>493,100,000</td>
<td>32.5%</td>
</tr>
<tr>
<td>1953</td>
<td>1,476,319,752</td>
<td>422,000,000</td>
<td>28.6%</td>
</tr>
<tr>
<td>1952</td>
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<td>1940</td>
<td>751,411,617</td>
<td>8304,300,000</td>
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- the City will have a balanced budget under generally accepted accounting principles in FY 1981, and had budgetary surpluses (as defined by State law) in FY 1978 of $32 million, and in FY 1979 of $213 million;
- the City sold $275 million of short-term notes in the public market in FY 1979 and will accomplish all of its seasonal financing in FY 1980 in the public market;
- the City now has one of the leading municipal accounting and budgetary systems in the United States.

Of critical importance has been the elimination of any real threat of bankruptcy to the City. In 1975 this could have occurred because a significant part of the financing was required to fund daily operations. This is no longer the case. The City will have eliminated the financing of current operations from the proceeds of capital bond sales by FY 1981. Should the City be unable to obtain financing for its capital needs in FY 1983 the daily operations of the City would continue. This is a 100% reversal from the circumstances in FY 1975.

The City has for the most part resolved the major problems that existed in FY 1975. The current problems are
in three areas: transit, health care, and education. These financing problems are not peculiar to New York City; every major urban area in the United States faces similar problems. The size of New York City magnifies the problem. The common thread that binds these problems is that the national government has failed to adequately provide funds or provide comprehensive solutions and direction in these areas. Until adequate national financing and solutions are made available, these problems will continue to plague America's urban centers, as well as New York.
Testimony

of

Albert Shanker
President, United Federation of Teachers

at the

Oversight Hearing on the
New York City Loan Guarantee Act

of

The Senate Committee on Banking,
Housing and Urban Affairs

January 28, 1980
Mr. Chairman, members of the Committee--

Thank you for this opportunity to appear before you in behalf of New York City. I recall that the last time I did so, in June 1978, you were most responsive. At that time I urged you strongly to recommend long-term loan guarantees for our city, so that, over a period of time, the city could put its financial house in order. I am here today with my colleagues representing New York City employees to assure you that the terms and conditions of the help you extended to New York City are being met—not easily, not without substantial sacrifice by all, but being met. And they will continue to be.

From time to time, we in New York will shout and scream at each other over differences in approach and timing as we move toward the required balanced budget. This is not only inevitable, it is also healthy. No one is God, with perfect wisdom and the omniscience to know what specific moves are in the best interests of the city as it strives to meet its obligations. Out of the debate come better alternatives, ones all of us—we in labor and management in the city and you in Washington—can live with. So, as you read the Times' headlines on our school budget fights, our forthcoming round of negotiations and other confrontations over the next few months, I urge you to keep in mind that none of us has lost sight of the mutual goal: a balanced budget that will inspire investor confidence
and permit our successful reentry into the private credit market.

The evidence is strong that New York has taken giant steps, made Herculean efforts, to live and spend within its means. I will not take the time to reiterate the details which you will find in the document prepared on behalf of the Municipal Labor Committee by Program Planners. I endorse its findings and I urge you to study it carefully.

Instead, I should like to share with you some thoughts and concerns I have as we move into the Eighties that impinge upon New York's finances and affect every other large city as well, concerns which this Committee, I believe, has a right and an obligation to address.

We in education in New York City are having a terrible time making ends meet. During a five-year period, 1973-74 to 1978-79, the Consumer Price Index went up 42% while our education budget went up only 2.6%. Thus the 1978-79 $2.8 billion education budget was really worth only $2 billion in 1974 dollars and could buy $1 billion less in 1979 dollars than the 1973-74 school budget. The cost of fuel to heat our buildings, the cost of repairs to our buildings, the costs of supplies from paper clips to textbooks, the cost of transportation have all hit us hard, despite sacrifices on the part of employees, who settled for barely an 8% wage increase over a two-year time period when the rate of inflation is likely to be well over 20%.

Inflation is bad enough, but at the same time we have been socked with a federal mandate--one among many--that is hurting
our schools and our city because Congress hasn't done what it promised, and what it promised isn't enough. I will give you the New York figures, but I assure you that every city and every hard-pressed local school district is finding similar problems.

Under P.L. 94-142, we are mandated to seek and find every handicapped child and provide that child with a free, appropriate education at public expense. The legislation, as you know, is highly detailed, and the courts, as you also know, have interpreted it strictly and ordered expensive implementation. And the dollars are coming out of the hides of those who can afford it least, local governments like New York City.

The formula Congress enacted for federal reimbursement is extremely stingy to the cities. It set rates of reimbursement ranging from 5% in 1977 to 40% in 1982 of the average non-handicapped per pupil expenditure nationwide. That average is $1,400, but there is no large city in the country which expends only $1,400 per pupil. It is nearly impossible to do so and provide decent education in urban America. Moreover, the cost of educating a handicapped child is usually far greater than that for non-handicapped children. Next year in New York City we expect to have more than 60,000 handicapped children in our school system, and the Board has budgeted over $8,100 for each--not out of our generosity of spirit or any spendthrift urge, but because that is the cost of the programs the federal courts have ordered us to put in place.

Now, not only is the formula itself inadequate, but Congress has not even lived up to its part of the bargain. Instead of providing 20% of the "excess cost" this year and 30% next year, as
authorized in the legislation, Congress has only provided 12% this year and 12% next year. If something doesn't happen soon, New York City will have to spend at least $1.2 billion between now and 1983 to satisfy this federal mandate.

I submit to you, Mr. Chairman and members of the Committee, that we are on the horns of a dilemma. It is not our fiscal irresponsibility in New York that has created this particular dilemma--it is yours here in Washington. You have acted nobly with respect to the handicapped--no one would want it otherwise--but if you want us to balance our budget, don't saddle us with a federal mandate that you are not willing to pay for. In this I can only echo the plea of our Mayor to you last week.

We in New York are trying desperately to keep faith with you. But we are not being kept faith with by this Administration in ways that are crucial to the survival of our city.

We were promised welfare reform and a gradual federal assumption of the local costs of welfare. Where is it? Is it even on the drawing board? We were promised that, unlike the policies of the Nixon-Ford Administrations, soaring interest rates and unemployment would not be used as weapons to fight inflation--but now we have high interest rates and, once again, creeping unemployment. If you've read page one of The New York Times lately, you know that we have a housing vacancy rate of 1% in New York, and that those who might wish to return to our city and contribute to its health, bringing their children to strengthen our school system, are put off as much by the unavailability of affordable housing as by a school system which is fiscally hampered from competition with
those in nearby suburbs. How can we make new housing starts with these interest rates? Our employees are taking a terrible beating on the costs of health care—their insurance coverage is seven years behind the inflation rate. Where is national health insurance? As crucial as it is to focus now on Teheran and Afghanistan, these are events of the last few months—what’s happened over the last three years? And even as we line up solidly to support our country's international policies, can we afford domestic paralysis?

I point out these things only because they have a direct effect on the health of New York City, and I urge you to consider them even as you monitor our compliance with the terms of your loan guarantees—on which, I might add, the government of the United States has made substantial money at no cost.

Finally, let me return to an earlier point: we intend to meet our obligations and balance our budget. We expect a successful return to the credit market. But I hope that what we gain in that market as a result of balancing our budget is not offset among those who worry about the long-range viability of our city when its education system is impaired beyond the capacity to function. Without a healthy public school system, one that produces an educated, sophisticated workforce and attracts taxpayers, we cannot have a healthy city. That is why I urge you once again to look at how many burdens you have placed on our schools and how much better the federal government should be doing in support of them.
STATEMENT BY MAYOR EDWARD I. KOCH
BEFORE THE
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE
WASHINGTON, D.C.

Tuesday, January 29, 1980

Senator Proxmire, Members of the Senate Banking Committee:

Today I appear before you to make my second report on the City's progress toward financial stability and independence. In making my first report to you a year ago, I thanked you and the Congress for passage of the New York City Loan Guarantee Act, and I will now thank you again. The guarantees have made it possible for us to obtain the financing we need as the City moves toward a truly balanced budget. I believe the City can and should accelerate its budgetary objectives by a full year: my goal is a City budget balanced in accordance with generally accepted accounting principles, starting next July 1 -- less than six months from today. I have presented a revised financial plan that will achieve this. There is no more important step the City can take to ensure that at the end of the four year plan, on July 1, 1982, the City will be able to stand on its own. Before I bring you up to date on the City's financing program, let me describe the new budget plan.

BALANCING THE BUDGET

The financial plan presented to Secretary Blumenthal and the Congress in January 1978, which was the basis for the Loan Guarantee Act, called for the City to balance its budget by fiscal 1982. The financial plan presented on January 16 establishes a program for the City to balance its budget under generally accepted accounting principles in fiscal 1981, a year ahead of
schedule. The purposes of achieving a fully balanced budget a year in advance are clear: First, the City will address its fiscal condition realistically by taking early action to close the enormous deficit projected for 1982. Second, the City's reentry to the public credit markets will be accelerated. Finally, with market access and a balanced budget the City will become financially self-sufficient, enabling it to deal more effectively with the problems of government and stabilize the delivery of services.

This plan continues the trend of financial accomplishments by the City over the past few years. The budget deficit has been reduced by about $1.5 billion since fiscal 1976, from $1.9 billion that year to $422 million in the 1979 audited statements. The remaining deficit will be totally eliminated next year, and the City workforce will have been reduced by over 25 percent, from 254,000 at the start of fiscal 1976 to 188,000 at the end of fiscal 1981.

It is important to understand the basic sources of the persistent imbalance between the City's projected expenditures and revenues. On the expenditure side, mandated programs and inflation have increased the City's costs enormously. For example, the cost to the City of medicaid, public assistance and special education -- all mandated by State and Federal law -- was over $1.1 billion in fiscal 1979; by fiscal 1982 these costs will have increased by about one-third, to $1.5 billion. Energy costs will have more than doubled during this period, reaching $450 million in fiscal 1982.

As has been true in the City for the past two decades, such mandated costs have absorbed an increasing portion of the City's locally raised funds. The result has been a continuing reduction in the portion of City funds available for personnel who perform services -- policemen, firemen, sanitationmen, schoolteachers and the like.
The growth of City revenues has been insufficient to fund such costs, requiring continuing cuts in City agencies. Net revenues from the real estate tax, the City's major tax source, have not increased significantly since 1976; the yield from this tax has declined from 51 percent of locally raised taxes in 1976 to 47 percent in 1980. The City's other taxes, principally the personal income tax and sales tax, can be expected to grow at roughly the same rate as inflation, but these taxes amount to less than half the City expenditures that are driven upward with inflation. State and Federal revenue sharing programs, a major source of City funds, have not grown significantly and are projected to remain about constant.

Having outlined the fundamental reasons for our persistent budget gaps, I will now turn to the gaps we face in fiscal 1981 and 1982: $677 million in 1981, rising to $1.14 billion in 1982. These gaps reflect the cost of a new labor settlement comparable to the settlement negotiated in 1978, although negotiations have not begun with the municipal labor unions and no such offer has been made. The gap for 1981 also reflects the one-time $278 million cost of balancing the budget under generally accepted accounting principles: $150 million to eliminate capitalized expenses, and $128 million to fund City pension liabilities on the accrual basis.

To close these gaps, I have proposed City actions amounting to $507 million in fiscal 1981 and $729 million in fiscal 1982. The plan has two essential components -- a major expenditure reduction program and limited, though not insubstantial, tax increases.

I propose to cut back expenditures in 1981 by $299 million and in 1982 by $461 million. The 1981 cut will be twice 1980's, and, taken together, these reductions will be more difficult than any taken since 1975. Every agency will
be cut. But we have attempted to target reductions to reflect basic City goals, and we have tried to make cuts in a way that reduces service delivery as little as possible. To make clear our commitment to service delivery we have imposed, where possible, a 10 percent cut in administrative costs, even for the highest priority agencies. And we have imposed dramatic reductions in the Cultural Affairs, Consumer Affairs, and Buildings Departments -- all important agencies but with lower priority than some others. The Department of Ports and Terminals will be eliminated -- along with many other actions.

To illustrate my earlier point about the effect of mandated costs: of the massive cuts required for 1981 and 1982, more than half will take the form of personnel reductions, which will total over 7,800; of these reductions, more than two-thirds will be in police, fire, sanitation and -- most of all -- education.

In addition to these expenditure reductions, the plan would raise certain local taxes and user charges, which will yield an additional $175 million annually in revenues for fiscal years 1981 and 1982. In reviewing the tax options, I rejected increases in the City's personal income tax and corporate earnings tax because of their likely impact on the local economy; I believe the City was right in 1977 to have lowered taxes. Instead, I am seeking actions that are equitable, bring tax receipts in line with inflation, and establish user charges at appropriate levels. For example, I propose to increase the real estate tax by 10 cents per $100 of assessed value; to increase water and sewer charges by about 15 percent; and to increase excise taxes on beer and liquor. These kinds of revenue measures are not expected to have any significant negative effect on the City's economy.
Even with all the cuts and taxes I have proposed, the City will still need the additional aid from Washington and Albany now in the Financial Plan. The State and Federal governments must continue to be partners in solving New York's budgetary problems.

We are expecting increases in State and Federal aid, but such increases are less than half of the $1.2 billion the City itself is undertaking in expenditure reductions and tax increases during fiscal 1981 and 1982. The plan assumes $170 million in additional Federal and State aid in fiscal 1981 and $410 million in fiscal 1982, for a combined total of $580 million over the two fiscal years. This is less than the amount originally included in the 1978 plan.

With respect to State aid, the Governor has pledged -- publicly and privately -- that the additional aid we require will be forthcoming. With respect to Federal aid, while we have made some progress in obtaining additional aid through administrative actions, the major initiatives will have to be approved by Congress as part of the Federal budget. I think the record demonstrates that we have been able to obtain the additional State and Federal aid we need to meet our budgetary objectives.

The January 15 plan is by no means easy to implement. The tax increases and expenditure reductions proposed will be the subject of continuing analysis and controversy. But I believe that the job of balancing the budget must and will be undertaken in 1981. Putting an end to the City's years of fiscal dependency will carry rewards fully commensurate with the struggle we now face.

FINANCING

Status of Financing Plan: As you know, the $4.5 billion four-year financing package we developed in late 1978 is one of the largest, most complex financings ever arranged. Less than 20 percent of this financing -- or $750 million -- is
scheduled to be implemented with Federal guarantees. The remaining $3.75 billion -- over 80 percent -- is to be provided by issuing unguaranteed bonds of the City or the Municipal Assistance Corporation (MAC). This means that the City plans to use less than half of the $1.65 billion of Federal guarantees now authorized. In line with my wishes, as well as yours, the bulk of the City's financing is being provided through local efforts. Local financial institutions, as well as State and City employee pension funds, are participating in this financing plan, and New York State is playing a major role through MAC debt issuances.

I am pleased to report that the financing plan is on schedule. To date, $1.79 billion of MAC bonds have been sold, of which $938 million were issued to financial institutions and City employee pension funds under a four-year bond purchase agreement made in November 1978; the other $847 million on MAC bonds were sold to the public in six separate issues, the most recent of which has just closed. In addition to the $1.79 billion of MAC bonds, $650 million of Federally guaranteed City bonds have been issued to City and State employee pension funds. Another $100 million of guaranteed bonds is scheduled to be issued on February 21. This will be the final planned sale of guaranteed bonds under the four-year plan.

Public Note Sales; Seasonal Financing: During fiscal 1979, the City was able to sell short-term notes to the public for the first time since March 1975. The first public note sale was in January 1979, for $125 million; it was followed by another public issue the next month, for $150 million. All these notes were paid on time. These public sales were accomplished one year ahead of the schedule set by the Guarantee Act. The remainder of our $650 million of seasonal financing needs was met by a credit facility with local banks and City employee pension funds.
In connection with the City's short-term borrowings, you should be aware that our seasonal borrowings have decreased by about 70 percent, from $2.1 billion in fiscal 1977 to $650 million in fiscal 1979. During the current fiscal year, we project that seasonal borrowing needs will drop to $600 million. To date, the City has met these fiscal 1980 needs with two public note sales for a total of $375 million -- already an improvement of $100 million over the fiscal 1979 total of publicly issued notes. As a back-up to public note sales in fiscal 1980, we arranged another credit facility with private lenders. The lending group in the facility was expanded to include forty local, foreign and out-of-state banks, eliminating the need for participation by the City's pension funds in meeting this year's seasonal borrowing needs. I consider these developments as important steps toward securing sustained access to the public credit market.

Capital Spending: As I reported to you last year, capital spending for the initial year of the four year plan was below the level we originally anticipated. Because of the urgent need to restore the City's capital plant to sound condition, I instituted a series of measures to ensure that we spent promptly and prudently the capital funds available to us. While I cannot be entirely satisfied with the progress of our capital program, I am greatly encouraged to see that we have begun to meet our spending targets in programs that are consistent with our priorities.

Before we presented the City's new budget program on January 16, we reviewed the City's entire four-year capital program. Part of meeting our spending targets, as we have begun to do, is to set those targets at appropriate levels.
I believe we have done so. The systems for planning and reporting capital expenses are being almost completely overhauled. This major effort is the final phase of the process that made our expense budget auditable by independent accountants. As the capital budget is brought fully on line with the new system, our ability to analyze and forecast capital expenses is steadily improving.

The results of our recent analysis showed that, while interim spending forecasts require significant corrections, the overall $2.3 billion estimate of capital spending during the four year plan remains our best estimate. We will continue to monitor spending results and regularly reevaluate our projections. As we move closer to the half-way mark of the four year plan, our projections can become progressively more firm because of increased information and experience with the capital program. The monthly financial plan statements to the Treasury Department, as well as our quarterly financial plan modifications, will continue to keep the Federal Government and the public fully informed of any changes in our projections.

**Market Access -- Outlook:** When the four year plan expires in mid-1982, the City will have to obtain capital funds without any Federal presence in our financing. Whether we can then stand on our own -- without Federal guarantees -- will be the real measure of our success. I have underscored my commitment to this goal with my decision to balance the City's fiscal 1981 budget in accordance with generally accepted accounting principles, a year ahead of the schedule set forth in the Guarantee Act. This program should significantly improve our prospects for access to the long-term credit market; it is a clear signal to potential investors, as well as the rating agencies, that the City has both the will and the ability to finish putting its financial house in order.
Any discussion of market access must acknowledge the importance of improving the City's bond rating. An investment grade rating appears to be essential for the City to achieve true market access. No municipal issuer has been able to sell bonds in significant amounts, on a regular basis, without the minimum investment grade from one of the rating agencies. In the case of short-term notes, the City was able to succeed after a one-grade advancement by Moody's, from MIG-4 to MIG-3. In the case of bonds, no comparable advance has been made. The City's bond rating was suspended by Standard and Poor's in 1975 and has not been restored; Moody's continues to give our bonds a B rating. For City bonds to be of investment grade, the Moody's rating would have to advance two steps, to Baa, and Standard and Poor's would have to rate the bonds as BBB.

A truly balanced City budget, one year ahead of schedule, should accelerate the process. If we stick to our program to balance the City's budget -- under the most stringent financial auditing and reporting standards applied to any municipality in this country -- the City's bonds will deserve an investment grade rating. As you know, the Guarantee Act and the financial plan require that the City attempt to sell bonds during the coming fiscal year, unless any such attempt would be against our financial interests. I am firmly committed to achieving a public sale of City bonds at the earliest possible date. It will clearly be a step of enormous significance in the City's continuing effort to regain full market access. Therefore, it is vital that the City's first bond sale be a success -- that it be favorably received by the marketplace as the beginning of a renewed City presence in the municipal bond market. An unsuccessful attempt, like the aborted City note offering in 1977, will only serve to set back the City's long-term goal of full market access. Having
Having made this point, I will now say that I believe a successful bond sale should be possible in fiscal 1981, and I stand ready to move ahead with it as soon as the City's financial advisor and underwriters advise me that the time is right.

If the City begins to sell bonds in fiscal 1981, as I believe will be the case, we will have begun to set the stage for the period after the end of the guarantee program. The prospects for market access in fiscal 1982 are even better because we should by then have an audit confirming that the City balanced the budget a year in advance. Nonetheless, prudence requires us to deal with the possibility that the City will not have full market access before the expiration of the four year plan. We are beginning to assemble the elements of a financing program for the period after fiscal 1982, in order to ensure that the City will be able to obtain long term capital without resort to Federal guarantees. Last November, I outlined three general areas for consideration:

- the creation of authorities that would issue special purpose revenue bonds, such as water and sewer bonds, which would be backed by user charges.
- authorization of additional MAC bond issues.
- reduction of the City's capital program.
A combination of measures such as these can be taken and will be taken to ensure that, even if the City's market reentry is incomplete, we can nevertheless function without Federal guarantees after the four year plan expires. The City, MAC and other local parties will work together, as we have in the past, to put such a program in place well before the June 30, 1982 deadline. This program will not assume or require any Federal presence in City financing.

THE ECONOMY

Since we are counting on local revenues to fund a large portion of our budget, the state of the City's economy is critical to the success of the four year plan. During the second year of my administration, the City's economy continued to show progress, due to the City's improved business climate, as well as the long upswing the nation's economy. We are forecasting that the nation will experience a recession in 1980, and the January 16 plan takes into account the impact a national recession could have on our local tax revenues.

However, a recession now should not have the disastrous impact of the last recession five years ago. At that time the City was on a declining path. Even in 1973, a relatively prosperous year for the national economy, the City lost 160,000 jobs. The situation is different now. During the year after my election in November 1977, jobs in the City increased by 53,000, reversing a seven-year decline. In the following year, between November 1978 and 1979, an additional 13,300 jobs were added, mostly in the private sector. The bulk of these new jobs are in business services, and the finance, insurance and real estate businesses. These industries are not as sensitive to downturns in the economy as manufacturing, which now makes up a smaller proportion of the jobs in the City.
Retail sales have shown surprising growth. Sales advanced about 12 percent above 1978. This is far above the City inflation rate, implying that the City's real growth for 1979 was greater than that shown for the nation. Among the reasons for the extremely good showing in sales are the Sunday openings of stores, the attractiveness of prices expressed in dollars for foreign tourists, and the additional expense of using automobile transportation to trade outside the City. These factors, which increase the attractiveness of urban area shopping, will continue into the future.

Another strong sector has been construction. Additional residential housing is in the works. A recent survey has shown that 6,800 new apartments will go on the market by the end of 1980. American Telephone and Telegraph, Continental Insurance, IBM, and Phillip Morris are constructing new headquarters buildings in the City. The strong flow of foreign investment has led to increased demand for space as a result of their corporate presence here. Other projects in the works include a new office tower on Wall Street for the American International Group, and the new American Exchange at Battery Park. The Convention Center will help revive the far west side at midtown. Since the financing is already arranged, the work will go forward even if there is a recession.

The City's tourist industry had a particularly good year, with hotel occupancy rising to over 90 percent, the highest level since the 1964-65 World's Fair.

The relative improvement in the local rate of inflation has been an important ingredient in our economic recovery. The City's inflation rate has been below the nation's since 1974, with the cumulative increase since 1967 below the national average. In 1979, our average inflation rate was 8.9
percent, compared with the national increase of 11.4 percent. This has put us in a better position to compete with the rest of the nation for new business and new jobs. The rise in available jobs has caused the City's unemployment rate to drop to 7.2 percent as of last December, our lowest unemployment rate since the beginning of 1975.

Of course, in view of the national recession expected in 1980, we have projected downturns in all of these areas. And even now, our unemployment rate is higher than the national average of 5.9 percent. While the City is now in a much better position to withstand a recession, without the enormous damage we experienced in 1974-75, the adverse effects on our economy and budget cannot be ignored.

On balance, I think we have good reason to believe that the long term outlook for the City is encouraging. We are dealing with the fiscal problems that for so long have clouded the City's credit. Of course, many of the actions required are controversial and difficult. But despite the controversy, despite the difficulty, one fact should be apparent: the program we brought to you in 1978 is succeeding. Since our achievements would not have been possible without Federal loan guarantees, you have every right to be satisfied with the role played by this Committee in bringing them about.

Again, I thank you.
Senator Proxmire, members of the Senate Banking Committee:

Hello again. We are here today to meet the City's continuing obligation under the Loan Guarantee Act of 1978 to explain our past progress, present problems and future prospects.

Last year, in urging further extensions of loan guarantees by the Treasury pursuant to the Act, I presented the consensus that the City's full financial recovery would be signaled by its ultimate full re-entry into the public credit markets.

That is still true.

I also presented the prevailing view that the City would regain full and unrestricted, albeit disciplined, access to public credit by fiscal year 1982 when its expense budget would be in GAAP balance, that is, in balance according to Generally Accepted Accounting Principles.

That can still be true and most of our strategies are still premised on that accepted wisdom.
But it ain't necessarily so. It does not follow as the night the day that once the City achieves GAAP balance everybody's uncle will be willing to lend the City whatever it asks for and needs. What does follow is that certain steps can be taken that will give the City a better chance to re-enter the credit markets and that we must plan for the contingency that while the City will complete its fiscal reforms, lenders will not flock to our doors.

Much affecting New York City and the restoration of its credit has changed since we last testified nearly a year ago. Unsettling world events, national reactions and local economic conditions everywhere have engendered a jittery urgency which has affected all markets with a deep uneasiness and uncertainty.

Indeed, as far back as October, at an Arden House Conference on municipal priorities, I suggested that market psychology may have changed sufficiently for us to need to plan for the contingency that a balanced budget will not ipso facto immediately pry open the doors to public credit.

By the end of the year we had received enough signals from the investment community to warrant my stating flatly that the City's two major fiscal goals, a GAAP-balanced budget and complete access to public credit, can no longer
be considered to follow quickly one from the other. We must now recognize the possibility that despite the City's achievement of GAAP budget balance, it may not be able to re-enter the public credit markets to the extent and within the time frame contemplated. On the other hand, I would emphasize that there would be no possibility for the City to accomplish the second goal, the re-establishment of public credit, without achieving the first, GAAP budget balance.

We must acknowledge the possibility of less than full re-entry and plan for it despite our pride in the extraordinary fiscal accomplishments of the City since the crisis began in 1975, accomplishments conceded both by the City's severest critics and outside independent auditors:

1. An operating deficit estimated at $1.87 billion in 1976 was cut to $422 million by June 30, 1979.

2. Almost $6 billion of short-term debt was either repaid or exchanged for long-term MAC financing.

3. All subsequent seasonal financing--Federal, negotiated or public--was repaid before June 30 of any given year; that is, we have had no more rollovers of temporary debt.

4. We have achieved limited re-entry to the short-term credit markets. The City raised $275 million in two note sales to the public in fiscal year 1979.

5. The credit rating on City notes was upgraded by Moody's from MIG-4 to MIG-3.
6. The State's annual $800 million advance was eliminated, half through the sale of MAC bonds and half through a much improved cash position.

7. Our cash flow has improved dramatically: the City borrowed only $650 million short-term during fiscal year 1979, compared with the high of $2.1 billion under the Federal Seasonal Loan Program.

8. Our budgetary situation has improved markedly: the City finished fiscal year 1979 in a budgetary position some $200 million better than planned.

9. Despite the need to finance our deficits, our net outstanding debt, including City bonds, MAC bonds and capital lease obligations, is actually $480 million less than it was as of June 30, 1976. (The net debt figure takes into consideration the specifically defined reserves that exist under law for payment of some of the outstanding gross debt.)

10. The real estate tax collection rate in 1979 was 94%, up for the third consecutive year.

11. A four-year decline in assessed valuation of taxable real property was reversed.

12. Obsolete accounting procedures and uncoordinated accounting practices have been eliminated; for the second year in a row the City's financial statements, which my
Office prepares, have been certified by independent accounting firms.

In spite of all this, we now know that none of these improvements alone, nor all of them together, will necessarily guarantee full City access to the public credit markets at any early date.

In light of this, what has been our strategy for fiscal year 1980? We have laid out a number of intermediate goals in a drive toward full market re-entry. Let me tell you first about the goals the City has reached:

1. We negotiated a seasonal loan agreement this year with many more banks than last year. Last year, 11 Clearing House Banks and the City's pension funds participated in our standby credit facility. This year, the pension funds (certainly not a traditional money source for tax-exempt securities) were not needed; 12 Clearing House banks joined 28 other City banks, out-of-town banks and banks representing 11 different foreign counties.

2. So far in fiscal year 1980 the City has met its goal of not using this standby $600 million credit facility; we have gone directly to the public for $375 million in two note sales. If conditions stay favorable, we will obtain the remaining $225 million of our short-term needs from the public, rather than from the credit facility—a further indication of growing investor confidence in the City.

3. The City is now in the midst of the largest physical inventory of fixed assets in municipal history. Once the
inventory is complete, a General Fixed Asset Group of Accounts can be established and the City will be able to meet the last remaining requirement of accounting according to GAAP. My Office will complete this requirement in time for inclusion in the City's financial statements for fiscal year 1980—a year earlier than required.

In addition to meeting GAAP requirements, we are also developing an inventory of the City's water distribution and sewage collection systems which will lay the groundwork for future billing and financing decisions in this vital life-support area. As a planning tool, we will establish replacement costs for the City's fixed assets to help in the development of priorities in the City's effort to reconstruct its deteriorating physical plant. The use of replacement cost will enable us to measure our progress or lack of progress in replacing our plant.

On the other hand, I must report on goals we set for this year, but have not yet achieved, largely because of unsettled market conditions. First, the City has not yet secured the rating improvement that we need for our notes. Second, all the City's short-term notes sold to date have been Revenue Anticipation Notes. These RANs are backed by specially set aside state aid revenues. So far, the City has not sold any Tax Anticipation Notes backed only by City real estate tax collections.

Third, the City has still not yet sold notes through competitive bidding by underwriters; thus far, notes have been
sold only through negotiations.

What then are our strategic goals for fiscal year 1981? Obviously, at the very least, to accomplish whatever goals we fail to accomplish this year; they may include competitive bidding by underwriters, a TAN sale and a better note rating.

Beyond that, we will seek to improve the standby short-term credit facility—even if we never have to use it—by having more lenders participate and by winning a better deal for the City.

But now, what about long-term bonds? As you know, the City’s Four Year Financial Plan requires it to enter the long-term market during fiscal year 1981 and try to sell $300 million of City bonds to the public without a Federal guarantee. One of the reasons Mayor Koch proposes that GAAP budget balance be accelerated from 1982 to 1981 is to hasten the achievement of long-term market re-entry and enhance the likelihood that the 1981 goal of $300 million sold long-term in the public credit markets can be achieved.

One thing is clear: without a GAAP-balanced budget in fiscal year 1981, the City bonds in the $300 million sale planned for that year are not likely to bear an investment grade rating. If the bonds do not carry such a rating, many banks and other institutional investors may not be able to buy them under internal regulations or as a matter of law.

That means the $300 million of bonds will have to be sold to a more speculative class of investor willing to take
a chance on unrated securities. It's hard to say how many such investors there are, and what determines their risk-taking or risk-avoiding posture at any given moment.

Furthermore, in the case of a city seeking to regain investor confidence, one can question the wisdom of the first sale of long-term bonds in six years being labeled risky by independent rating agencies. Maybe speculators would buy them, but how easy would it be to shuck that image the following year when the City must appeal to a different category of investor: one more conservative and less disposed to risk.

Would it promote restoration of New York's credit for its first bond sale in six years to be considered speculative by Moody's or Standard & Poor's? I think not. Would such a rating tend to make it more difficult to broaden the market the following year when more bonds must be sold? I think yes.

There is no question that GAAP balance in 1981, as the Mayor proposes, rather than a year later will improve the City's fiscal position. But will it mean that the $300 million in bonds to be sold next year will assuredly be given an investment grade rating?

We have to answer again—we hope it will, but not necessarily so.
Speaking optimistically, should the credit rating agencies award those bonds an investment grade rating, we have a better chance of selling them to institutional as well as individual investors in fiscal year 1981. This will be an important first step for a City which aspires to the re-establishment of regular market access. On the other hand, many experts feel that investors may want to see GAAP balance in place and working for at least a full year, maybe more, before they put their money in size on the line.

That could mean--on the side of melancholy--that City bonds could not be sold in significant quantity before fiscal year 1982 at the earliest and that the full extent of the $650 million contemplated under the Plan might not be realized.

Should we be optimistic or pessimistic? Without more facts or visible trends, it's hard to say right now and one is left with one's own outlook or attitude.

The optimist could say that the subways are running, the Statue of Liberty is attracting more tourists than ever and the Rockettes are happy. The pessimist could say that the subways are in a hole, the Statue of Liberty is on the rocks and the Rockettes are kicking. Same reality, different viewpoint.
The City has no choice but to be optimistic. Our Financial Plan requires that we try to sell $300 million of bonds in fiscal year 1981 whether GAAP balance is achieved or not, whether the bonds win a good rating or not.

At the moment we are thinking of offering for sale $75 million of bonds in each quarter beginning next July 1. One positive effect of such regularized sales is that the market knows where it stands vis-a-vis the City, investors know the issue will not change in size and other municipal bond issuers, particularly those in New York State, have some flexibility in scheduling their own sales.

Assuming GAAP balance in the next budget, assuming real investor interest in buying City bonds before a second consecutive GAAP-balanced budget is developed and even assuming an investment grade rating for the bonds, we must still consider various contingencies as we prepare to sell City bonds:

1. General market conditions: wild gyrations in the stock, bond, commodities, metals and money markets—no longer an improbable textbook hypothetical—could undermine any of the four proposed issues at any given moment.

2. General municipal market: this particular market could be seriously impacted by bullish or bearish disruptions in the other markets, as well as by certain factors affecting both issuers and purchasers. For example, the fiscal problems of other cities have a probable impact on the saleability of
New York City bonds. Among many urban difficulties, Cleveland, as you know, defaulted; Chicago's fiscal condition is a troubled one and Mayor Byrne flew to New York just last week to seek a favorable bond rating from Moody's and Standard & Poor's. We cannot simply dismiss other cities' problems and say investors will not consider the nation's overall urban crisis when New York City offers its bonds for sale half a year from now.

3. Development of a New York City market: as I noted, no matter how great the City's fiscal progress, investor perception of it may not be favorable enough for the creation of a sizeable market for New York City bonds. This could be affected by many factors, including, for example, the forecast last week by the Wharton Econometric Forecasting Associates that in the coming recession job losses, output of goods and services, retail sales and personal income would all be worse in New York City than in either the region or the nation. Correct or not, the prediction cannot be overlooked as a factor in any contemplated New York City bond sale.

4. The spread between interest rates and the difference in likely maturity schedules of MAC bonds and City bonds: even if all signals are "go" for a City bond sale, the cost differential could be too high a price to pay for the pleasure of entering the long-term market. The City will be sensitive to any differentials between MAC and City bonds and their
implications for the budget.

What will the City do if it fails, for whatever reason, to sell its bonds in fiscal year 1981, or 1982 for that matter, as contemplated by the Financial Plan? As you know, the Plan provides for this contingency, if in fact the City cannot obtain credit in the public credit markets in amounts and on terms sufficient to meet its financing needs: the Plan provides for MAC to take up the slack. If MAC cannot, then the Federal guarantees come into play for sales of City bonds to the pension funds. If even the guarantees are denied to the City, then the City will simply have to reduce its spending for capital purposes.

Of course, there are steps which Congress can take to make it easier for New York City to sell its securities in the public markets:

1. Amend the Bankruptcy Reform Act of 1978 to protect the position and rights of holders of municipal general obligation revenue securities in the event of a bankruptcy.

2. In establishing the new Energy Security Corporation, allow eligible projects sponsored by public entities, as well as private sector firms, to be considered for Federal financing.

3. Develop a final version of the Urban Bank bill that calls for loan guarantees and/or direct loans to businesses located in economically depressed areas; it also provides grants to states and localities for various economic development purposes.
The first step would be of great help to the City in its efforts to sell securities publicly. Senate Bill 658 proposes to amend the Bankruptcy Reform Act of 1978 to protect specifically only the holders of straight revenue bonds and not the holders of general obligation bonds which additionally have defined revenues earmarked for repayment.

The short-term debt recently issued publicly by the City of New York has been in the form of "general obligation" revenue anticipation notes. As provided by State law, the monies earmarked for repayment of these notes are segregated for the benefit of noteholders. However, given the "hybrid" nature of these obligations, they would not be protected by the proposed amendment to the Bankruptcy Act.

Were the City, all of whose debt must by law be general obligation debt, able to represent to prospective lenders that its debt instruments would remain in a protected position in the event of bankruptcy, such a representation would significantly improve the City's ability to market its bonds. Indeed, the amendment we seek would improve materially the ability of all municipalities to meet both their long and short-term financing needs in the public credit markets.

We agree with and support the Public Securities Association, which represents about 230 dealers and dealer banks providing underwriting and financial advisory services to state and local governments, in its call for Federal protections for holders of general obligation revenue bonds.
Congress can help our credit problem in a second way by making cities, as well as private firms, eligible for energy conservation financing through the Energy Security Corporation.

New York City is considering the construction of eight resource recovery plants over the next ten years at a cost of $1.25 billion. An achievement of this magnitude would not only satisfy the City's solid waste disposal needs, but would also produce energy for both heating and the generation of electricity.

As I understand it, as now contemplated, the Energy Security Corporation would not be able to assist the City in building direct waste-to-energy resource recovery plants. Yet, the generation of energy that causes a reduction in the use of oil does not differ from the development of synthetic fuels which the ESC is empowered to assist.

Federal assistance for such projects which obviously fulfil a national need would permit the City either to reduce the amount of money it must try to borrow on its own or to use some of its borrowed money for other urgent capital purposes.

Finally, I hope that the Urban Bank legislation will come out of the Senate-House Conference—the sooner the better—with its two major purposes intact. As the nation slides into
recession, cities need a Federal program that provides loan guarantees and direct loans to businesses located in economically depressed areas and that would permit grants to states and localities for various economic development projects.

It should be clear that any action that improves New York City's economic climate will make it easier for its government to market its notes and bonds.

These are some areas in which Congress can be helpful. But I want to make clear that we are also exploring the possible additional actions we can take on our own to accelerate improvements in the City's fiscal position.

First, the creation of a truly funded Contingency Reserve Fund is under consideration. We will have $25 million to $30 million available in June, 1980 after redemption of bonds in one of the City's Sinking Funds and there will be more redemptions in the future.

As a trustee, I do not intend to allow this money to be "used up" or dribbled away; instead, I have introduced local legislation to place it into a special funded reserve which will have only two uses: reduction of seasonal borrowing needs and financing unexpected deficits which might occur after 1982. Moneys borrowed in this manner will have to be repaid to the Fund.

Second, we are studying the potential issuance by the
City of revenue bonds, particularly in the water distribution and sewage collection areas. As I mentioned before, we are in the midst of a physical inventory of these particular fixed assets. Once the accounting is complete, we will be able to consider an appropriate financing mechanism.

Third, we are studying the feasibility and potential effectiveness of expanding the City's existing General Debt Service Fund (GDSF). As you know, this Fund was established under the Financial Emergency Act on January 1, 1979. It is funded throughout the year by the direct deposit of City real estate tax collections, as well as any additional funds that may be required, and has as its custodian the State Comptroller. Under the law, amounts necessary to pay monthly debt service must be deposited in the GDSF in advance of the month in which the debt service is payable.

We would like to see this General Debt Service Fund expanded to the point where an entire year of debt service, principal and interest, would be funded from the City's first collections of real estate taxes. In this way investors would be reassured at the beginning of each year respecting the availability of cash sufficient to pay all principal and interest payments due at any time during that year. With this kind of protection in place, the City's chances for unrestricted access to the public credit markets should improve significantly. Under the current real estate tax
collection procedures implementation of this concept would exacerbate our seasonal borrowing needs. However, if the Mayor's plan to accelerate real estate tax payments from a quarterly to a semi-annual basis is implemented, beginning in fiscal year 1982 this approach could become feasible.

In conclusion: we continued to make fiscal progress during the past year; we are actively moving to make even further improvements in the City's fiscal position; but unsettling world events and a poor national economic outlook have clouded the City's prospects for re-entering the public credit markets; we are, therefore, planning ahead respecting these additional steps that may be necessary to help us achieve the goals of the City's Financial Plan.

Thank you.
STATEMENT BY CITY COUNCIL PRESIDENT CAROL BELLAMY  
BEFORE THE  
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS  
UNITED STATES SENATE  
WASHINGTON, D.C.  
TUESDAY, JANUARY 29, 1980

I AM PLEASED TO TESTIFY AGAIN BEFORE THIS DISTINGUISHED COMMITTEE.

TEN DAYS AGO SENATOR PROXMIRE CONGRATULATED MAYOR KOCH ON HIS DECISION TO BRING THE CITY'S BUDGET INTO BALANCE ACCORDING TO GENERALLY ACCEPTED ACCOUNTING PRINCIPLES A YEAR AHEAD OF SCHEDULE, CONGRATULATIONS THAT OUR MAYOR AND CITY RICHLY DESERVE, FOR WE HAVE TAKEN A GREAT LEAP FORWARD. WHILE OTHERS HAVE BEEN TALKING ABOUT FISCAL AUSTERITY, WE HAVE BEEN LIVING IT IN THE CITY OF NEW YORK. WHILE OTHERS HAVE BECOME RECENT CONVERTS TO BALANCED BUDGETS, WE HAVE MADE THEM AN ARTICLE OF FAITH. OUR PAST HAS CHASTENED US, AND THE LAST FOUR YEARS HAVE TOUGHENED US. WE CAN STAND UP TO FAIR JUDGMENT.

AS THE MAYOR HAS JUST REPORTED, WE ENDED FISCAL YEAR 1979 WITH A FINANCIAL PLAN SURPLUS OF $216 MILLION, EXCEEDING THE BUDGETARY GOALS OF THE FEDERAL AND STATE GOVERNMENTS. WE REDUCED OUR BUDGET DEFICIT, AS DEFINED BY GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, BY $290 MILLION SINCE FISCAL YEAR 1978. WE REDUCED OUR ANNUAL BORROWING NEEDS FROM $1,875 BILLION IN 1978 TO $650 MILLION IN 1979. WE PUBLICLY SOLD $275 MILLION WORTH OF SHORT TERM NOTES AT INTEREST RATES BELOW THE COST PROVIDED BY A LOAN AGREEMENT WITH PRIVATE LENDERS.

(MORE)
WE OBTAINED THIS FINANCING IN PART BECAUSE OF THE FEDERAL
LOAN GUARANTEES YOU PASSED -- AND AGAIN, WE THANK YOU FOR
THEM. ON BALANCE, I AGREE WITH THE MAYOR AND THE COMPTROLLER,
THAT OUR PROSPECTS FOR FULL MARKET REENTRY BY 1982 ARE GOOD --
IT'S UNLIKELY THAT WE'LL BE BACK TO YOU AGAIN FOR ANY LOAN
GUARanteES. THAT, BY NO MEANS, HOWEVER, IS MEANT TO SUGGEST
YOU WON'T BE HEARING FROM US ANY MORE.

Indeed, we in New York have taken many steps that some
of you on this committee said wouldn't be taken. So I am
puzzled that along with his congratulations, Senator Proxmire
last week insisted on once again taking us to task for
seeking to balance our budget "on the back of the federal
government." Allow me, Senator, not only to differ with
this characterization . . . but to say that if the emperor of
this drama is the federal government, then it may well be the
emperor who wears no clothes.

The 1978 plan to save New York City, though not written
in stone, made a number of basic assumptions about prospective
actions on the part of the federal, state and city governments.
The City, has made good on its part of the plan, buffeted
by some favorable economic trends, but also in the face of
some adverse ones.

Yes, it is true that our jobs picture, which as much as
anything was key to the decline of the late sixties and
early seventies, is now beginning to turn around. We lost
600,000 jobs from 1969 to 1976, but payroll employment in
the City has risen marginally in the years since --

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As has personal income -- and the city reaps the benefits of these developments in the growth of that substantial portion of our tax base derived from personal income and corporate profits.

So too, Manhattan's commercial and residential real estate is booming -- with evidence of some spillover effect on our outer boroughs. We're experiencing a growth in retail sales; tourism is at record levels; 17.5 million people visited our city in 1979 -- spending more than ever before, and producing an estimated $180 million in direct tax revenues. Foreign capital continues to pour across our shores -- in part a response to the happy fact that our consumer price index continues to rise at a slower rate than elsewhere in the nation and abroad.

But it is also true that New York's overall employment rate continues to lag behind national growth levels. The future is particularly unpromising for the large numbers of blue-collar and unskilled workers in our city whose inability to find jobs has severe implications for a city treasury that pays out billions of dollars each year in welfare, medical and housing costs for the poor. So too, it should not be forgotten that Manhattan's skyscrapers cast shadows on acres of abandoned housing in our city -- the burden of which falls on local government to maintain.

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In sum, even as we see promising signs of growth in the City's revenue base, we see those gains eroded by burgeoning costs for social services, housing, health and especially for energy -- costs that even the most pessimistic of our forecasters find difficult to reconcile.

The City then has found it necessary to meet our budgetary goals not just by growth but also by severely cutting services -- laying off police officers, firefighters, sanitation workers and teachers. In 1975, New York City employed 282,858 workers. Today that figure is 193,626, a decline just short of 32%. And our financial plan for 1981 proposes 5,000 additional workforce reductions. Regrettably the full force of these reductions is not reflected in a parallel budgetary decline because of the impact of inflation, wage hikes and pension costs.

Those who continue to believe that New York City is a model of profligacy thus cling to a fiction. We have whittled our budget down to the core. Any more severe cuts may damage the essence of what it seems to me a City must provide in order to survive -- basic police and fire protection, education for our children, an energy-efficient public transportation system which is essential to the continued health of our economy.

Of course we in New York City are not without fault. Management improvements, -- such as further civilianization of our uniformed services, and reduced manning in sanitation -- still elude us.

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We still lag behind in our capital program, an inexcusable waste of valuable financing. But we are paying locally for these failures by coupling expenditure reductions with proposed tax increases. As we ask our citizens to get along with less, we also demand that they pay more.

What then can we say about the records of our partners in the endeavor to assure New York City's future? We are, after all, not an island unto ourselves. Are we wrong to point out that Washington has fallen woefully short of its commitment to the Four Year Plan? And Albany, a valued partner in the past, now plays coy with us, saying on the one hand that the State expects to balance its budget at the expense of localities, while hinting of other dollars hidden away to close our gap?

Honorable Senators, it is time the federal government recognize its obligation to New York City's Four Year Plan. The dollars we seek represent money to which, by any reasonable standard, New York City and the rest of Urban America are entitled. In three critical areas -- unrestricted gap-filling aid; reimbursements for welfare, health, transportation and energy; and, finally, as the Mayor has so clearly demonstrated -- in the full funding of federal mandates -- we must have the full assistance to which the federal and State governments have in the past committed themselves.

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Last week I challenged the Mayor's financial plan for fiscal years 1981 and 1982, because it incorporates a total of $580 million just in "gap-filling" assistance from Albany and Washington. What is more, it counts on total amounts of intergovernmental assistance that may be unrealizable, if history is a useful guide. Rough calculations by my staff -- determined that in fiscal year 1979, for example, the City's actual receipt of total intergovernmental aid fell short of projections in the 1978 plan by 10-1/2 percent, a difference of over a half billion dollars.

My skepticism, however, was not meant to excuse Washington and Albany from its commitments. I say again, New York City has lived up to its commitments -- in fact, we've exceeded them. Albany and Washington have not.

Permit me just a few examples:

First, with respect to "gap-filling" aid, there is little more to say than that general revenue sharing for localities must be continued at a minimum of current levels, while, at the same time, a countercyclical program is reinstituted.

Second, in the area of mandates, last spring my office released a study on the costs of Special Education for the Handicapped. The number of handicapped children processed by New York City's Board of Education has grown by 20,000 over the last five years. Local costs of special education have increased 55 percent, while our general education budget grew only four percent.

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Regrettably, federal assistance to cope with this growth is being phased in at a snail’s pace; instead of federal aid to the handicapped for FY ’81 covering 30% of our costs, we now expect to receive only 12 percent. So too, while we received slightly over $100 million for special education from the State for this current fiscal year, an increase of 8% over 1979, this figure, which was calculated on the prior year’s expenditures, still fell far short of our actual costs. The fact is that the increased costs of the additional handicapped children in New York City’s school system this year and next will largely be absorbed by City tax levy dollars. And what that means is quite simply that $11½ million in administrative and pedagogical cuts are now being proposed for the Board of Education -- cuts that some say will translate into a dramatic impact on regular classroom size.

Third, on the subject of health and welfare costs: I have said that New York City’s total receipt of federal dollars is falling substantially behind projections. Let me further explain how federal formulas in our major social welfare programs discriminate against us.

My office last year commissioned research on inequities in the current medicaid financing formula. Washington spends $10 billion annually in local and state reimbursements, that vary substantially from state to state, ranging from a base of 50 percent in New York and 14 other states to more than 70 percent elsewhere.

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Senator Moynihan has since introduced legislation to equalize this formula and remedy an antiquated and unjust system. The implications of such a change for New York City alone would be $200 million a year in increased funding. Increased federal costs nationwide would be $2.1 billion.

We are spending nearly $2 billion a year in New York State out of our own resources just to pay for what is termed our share of the national Medicaid program — and hundreds of millions more to cover the full costs of health care for needy individuals and families not eligible for the federal program.

This is an exact parallel to our situation with respect to the federal welfare program (AFDC). Yet the Carter Administration's current "welfare reform" proposals, while they cost a total federal $5.7 billion nationwide, would yield New York at most $150 million in "fiscal relief," -- a return of about 22¢ on our federal tax dollar, and just ten percent of what New York State and its counties currently spend on cash assistance -- out of our own resources.

The fact is we cannot even maintain our programs on this basis, much less improve them. Our welfare benefits, frozen since 1974, as a consequence of the State's fiscal difficulties, lose more of their purchasing power to inflation every year. Our Medicaid program, which cannot, and ought not be "frozen" grows more expensive every year.

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I repeat:

The federal government has reneged on gap-filling commitments. You've cut back on categorical aid. You've piled new mandates on top of the City's current work programs without adequate funding. Mandates for special education, clean air, sludge removal, handicap accessibility and water pollution are legislated without matching financial support.

As Mayor Koch said last Thursday to a conference of mayors from 28 cities, these burdens are not New York City's alone. They now plague cities across the country.

When we approached you back in 1975, our circumstances were, indeed, very special. Today the questions of New York City and its relationship to a nation are questions of the relationship of a nation to all of its aging urban centers.

We are seeing a scenario all too familiar to us in New York replayed in Chicago, Detroit and Philadelphia. Fiscal nightmares, unmet payrolls, massive layoffs. Until and unless we develop new mechanisms for municipal finance -- mechanisms free of categorical strings or costly mandates -- all of us in these cities will continue to perform precarious balancing acts.

We must begin now to plan together for the future of America's cities. For unless we plan now, we will discover that the quality of life in our cities will not be determined by us, but by events beyond our control.

Thank you very much.

#  #  #
FROM:
State of New York
Financial Control Board
270 Broadway
New York, N.Y. 10007

FOR RELEASE:
Tuesday, January 29, 1980

TESTIMONY

OF
Comer S. Coppie
Executive Director

BEFORE
The Committee on Banking,
Housing and Urban Affairs
Washington, D.C.
Mr. Chairman and Members of this Distinguished Committee:

I am pleased to be here today to discuss New York City's Financial Plan and to share my perspectives on the problems which, I believe, continue to face the City. Federal guarantees of New York City bonds were requested nearly two years ago in order to provide the City with necessary time — time to develop and implement a budget balanced in accordance with Generally Accepted Accounting Principles and time to demonstrate to the credit markets that it had reformed past fiscal practices. In concert with the establishment of the Federal Loan Guarantee Program, the New York State Legislature continued the responsibility and authority of the Financial Control Board under the Financial Emergency Act to assure the City's adherence to those fiscal objectives through the financial planning process.

The staff of the Control Board is currently in the midst of a review of the City's program to close the budget gaps for FY 1981 and FY 1982. This submission represents an important policy initiative by the City to accelerate the timetable for a GAAP-balanced budget. Mayor Koch has demonstrated the commitment of his administration to the goals of fiscal reform and market reentry by going beyond the requirements of the Financial Emergency Act and the Loan Guarantee Act of 1978 and proposing to achieve a GAAP-balanced budget in FY 1981.

Past presentations of the PEG program have relied heavily on City-wide attrition, O.T.P.S. expenditure reductions, and unspecified management improvements. By contrast, this program outlines agency specific expenditure reductions for both FY 1981 and FY 1982, and presents a sense of priorities with regard to expenditure reductions. In addition, the Mayor has attempted to target tax increases so as to minimize economic disincentives. I believe that the initiative to accelerate the movement to GAAP deserves the support of all the partners in the City's financial recovery program.

Nevertheless, New York City continues to face major problems in achieving its fiscal objectives. The questions remain whether the actions proposed by the City in this PEG program can be effectively implemented and whether these actions will be sufficient to achieve true budget balance as projected. These questions will be extensively analyzed as part of our review of the PEG program. My staff will examine the underlying social, economic, demographic and workload assumptions, checking both their internal consistency and their relationship with similar projections made by other governmental and private organizations. We will also evaluate the methodology used to relate these assumptions to the projections of revenues and expenditures.
In analyzing the specific proposals to close projected budget gaps, we will focus on the salient factors that are likely to affect the potential success or failure of the proposals. These include: (i) the degree to which the actions are within the City's administrative control; (ii) the service impact of the proposed actions; (iii) the City's record in implementing similar proposals in the past; (iv) the quality of the City's description of the actions and the timetables for implementing them; and (v) the practicability of the proposed actions.

The Control Board's staff report reviewing the December modification of the Financial Plan identified what continue to be the most critical issues in evaluating the feasibility of the City's proposed plan. The factor over which the City has least control is the state of the national and local economies. During the first half of the 1970s the City's private sector contracted sharply, eroding the tax base and contributing to the City's developing fiscal distress. A gradual recovery has occurred since 1976, in part reflecting the general national prosperity. The staff of the Control Board monitors key economic indicators, such as employment, retail sales, and consumer prices, and consults with economists from the City's major commercial banks, the Regional Plan Association, the Port Authority and the Federal Reserve Bank of New York. There is increasing agreement among these economists that the City's economy is regaining its health and should be able to avoid significant losses from the moderate national recession that is expected to occur this year. However, it is possible that this recession could be more severe and lead to greater revenue losses in the City than are currently projected. The City and the Control Board must be prepared to take appropriate action should this occur.

A second major uncertainty facing the City is the cost of the labor settlement which must be negotiated this Spring. It is impossible to quantify the costs of future collective bargaining agreements with precision. However, given the magnitude of the amounts potentially involved, the need to plan realistically for the cost of future collective bargaining agreements is an issue of serious concern. A reasonable labor settlement, one that can be funded within the City's Financial Plan, is necessary if the City is to achieve and maintain a GAAP-balanced budget.

In order to provide some coverage for these problems, the Financial Plan modification approved by the Control Board in December contained an unallocated general reserve of $180 million. We will continue to be mindful of these problems as we review the pending modification and the ways in which that modification proposes to deal with these issues.
Another critical problem is the potential of two covered organizations -- the Health and Hospitals Corporation and the Board of Education -- to significantly and adversely affect City finances. The December modification of the Financial Plan reflected a serious deterioration in the financial positions of these two huge agencies whose combined annual expenditures exceed $4 billion. The City's methods of monitoring and controlling these agencies have not proved effective.

Accordingly, the Board has taken a series of actions with regard to the covered organizations. The Health and Hospitals Corporation has developed a pattern of deficits largely because of its inability to collect sufficient third party revenues to meet Financial Plan targets. The Board has required that the City establish special reserves allocated to cover potential HHC deficits projected by the Board's staff. In FY 1979 a $28 million reserve was established before the Financial Plan was approved. This reserve was adequate to offset the revenue shortfall for that year. The reserve in the current plan for FY 1980 is $54 million, which we project will again be adequate to cover the projected shortfall. In this fashion, through our review process, we have been requiring the City to plan for projected HHC deficits in advance rather than attempting to deal with those deficits in the last quarter of the fiscal year.

In addition to requiring increased reserves for HHC, the Board's staff initiated an extensive review of HHC's revenue collection problems. This special study was undertaken because of the enormous drain on City funds created by HHC's chronic revenue shortfalls. Our report, which was issued last September, was highly critical of the implementation of HHC's new computerized collection system and presented twenty-one recommendations to improve the collection process. We have since received commitments from HHC management and from the City that these recommendations will be implemented, and HHC has retained Touche Ross and Company to assist in improving its revenue collection procedures.

On the expenditure side, both HHC and the Board of Education experienced significant cost overruns during the first quarter of FY 1980. Both organizations were unable to schedule by operating program the proposed total expenditure reductions reflected in the Mayor's Executive Budget. These developments underscored the need for the City to strengthen its methods of monitoring and controlling the finances of these agencies, both of which have traditionally exercised significant degrees of operational and fiscal autonomy. As a result, the Financial Control Board insisted that the City develop and implement control plans for these agencies in order to maintain the viability of the Financial Plan. The control plans which have been developed provide for improved reporting and monitoring procedures and require prompt and effective action to correct any significant variances which develop.
The latest submission of the Financial Plan which is currently under review depends heavily upon the City's ability to improve revenue collections in the Health and Hospitals Corporation and to control expenditures in both agencies. Implementation of the control plans will be closely monitored by the Financial Control Board in the coming months.

The City's plan also requires substantial annual increases in recurring intergovernmental assistance to close the budget gaps in FY 1981 and FY 1982. Because of the pressures to contain expenditure at all levels of government, this additional aid may prove unattainable. The Control Board will monitor the progress of the City's intergovernmental aid proposals carefully and realistically. We will require that the City undertake further action if shortfalls in projected intergovernmental assistance occur.

I must, nevertheless, point out that the City's capacity to make expenditure reductions is increasingly limited by mandated service levels in a growing number of agencies. The recent court decisions on Special Education provide an excellent example of the escalation of this trend. Program restructuring has been required within the plan to fund Federal and State mandated programs and at the same time to achieve the level of expenditure reduction currently estimated by the City.

The success of the City's effort to reduce expenditures while maintaining adequate service levels will also depend upon efforts to make necessary management improvements and to increase productivity. As we stated in our year-end report on the New York City Productivity Council, the Council has initiated no significant productivity programs to date. The record of productivity efforts in New York City during the last decade, however, reflects innovation and, in varying degrees, general accomplishment. It is our hope that the recently restructured Council will make a more effective contribution in the future.

The ultimate goal of New York City's financial planning process is full market reentry. This fiscal year the City has already made two successful public offerings of Revenue Anticipation Notes and is planning a third offering next month. If successful, as expected, the City will meet its total seasonal borrowing needs of $600 million for this fiscal year in the public market.

However, a number of observers have recently questioned whether the schedule for reentry into the long-term public market in FY 1981 is realistic. This skepticism has been based
on the difficulty of obtaining an investment-grade rating for City bonds before GAAP budget balance is achieved in FY 1982, and upon the possibility that credit analysts may require the City to show more than one balanced budget. In view of those concerns, the City's prospects for reentry into the bond market may be improved by the recently announced acceleration of the City's timetable for achievement of a GAAP-balanced budget.

Contingency plans exist to meet the financing needs of the City in FY 1981 and FY 1982 if the City does not achieve reentry to the public bond market in those years. However, the Proposed Financial Plan for FY 1983 reflects no assured source of financing for the City upon the expiration of existing agreements. In spite of the significant progress to date on budget problems, there remains the possibility that the City may not be able to meet all of its long-term capital requirements through the public sale of City bonds in FY 1983, and contingency plans should be developed for that period as well. It is important to recognize that failure to regain full access to the public credit markets no longer poses a threat to the City's solvency, although it will limit the size of the City's capital program.

The City continues to experience chronic difficulties in realizing its original capital expenditure projections. The Financial Plan originally approved by the Control Board in November, 1978 projected an aggregate of $2.3 billion in City-funded capital expenditures during the four year period ending June 30, 1982. Annual expenditures in that plan were expected to almost double from $382 million in FY 1979 to $749 million in FY 1982. However, actual expenditures during the first year were only $264 million, a decrease of approximately 30% from the original projections.

In the proposed Financial Plan modification, the City continues to project that capital spending over the four year period will aggregate approximately $2.3 billion. However, the projection of cash spending for the current year has been reduced to $394 million, approximately 18% less than the projections originally made in November 1978. In view of the spending shortfalls experienced during the last two years, maintenance of the $2.3 billion spending objective has required a dramatic increase in projected capital spending for FY 1982. The proposed modification contemplates a spending level of $970 million for FY 1982, more than twice the level of spending currently projected for this year and nearly 30% more than the City's original spending projections for FY 1982.

The City has begun an in-depth analysis of its capital program and the methodology used to develop and monitor capital commitment and spending projections. We have been closely monitoring the progress and results of that analysis in cooperation with representatives of the Municipal Assistance Corporation and will continue to do so.
It is all too obvious that realization of the City's very ambitious capital spending objectives will, at a minimum, require a major commitment to capital planning and management that has already been too long delayed. We are insisting that the City make that commitment and that it begin to detail the steps necessary to realize its goals. The analysis of the capital program recently begun is just the beginning of an effort which we believe could result in more reliable projections of capital commitments and spending and in a vastly increased capacity to realize those projections.

In conclusion, I wish to underscore the importance of the recent decision to accelerate the timetable for achievement of a GAAP-balanced budget. During the complex process leading to the final adoption of a new City budget, modifications in the Mayor's intricate package of expenditure reductions and revenue increases will undoubtedly be required. However, the critical factor is the commitment of all of the participants in the process to the Mayor's goal of a GAAP-balanced budget in FY 1981. Realization of this objective would represent a truly significant milestone toward the achievement of full fiscal recovery for the City of New York.

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Mr. Chairman and distinguished members of the Committee: thank you for this opportunity to present some of the views of my office as they relate to New York City's fiscal situation. As you may know, in the past I have had a reputation as one who prodded the City most strongly to do more to help ensure a balanced budget, and to take the necessary budget actions earlier in light of the financial problems that lay ahead. At this point, however, it gives me satisfaction to be able to give praise to the City and its Mayor.

The City's decision, as evidenced in its Financial Plan submission presented on January 16, 1980, to accelerate by one year the statutory timetable for balancing its budget in accordance with Generally Accepted Accounting Principles, or GAAP, is a significant action. It deserves recognition for three very important reasons:

- First, it can provide for a more orderly process of retrenchment than would be possible if the major expenditure reductions were left until fiscal year 1982. This more graduated timetable should allow the necessary cost reductions to be phased in, so as to minimize, to the degree possible, the impact of those reductions on the City and its residents. State Comptroller Edward V. Regan has repeatedly urged the City to formulate detailed gap-closing programs on a multi-year basis, and to implement a more systematic and rational expenditure reduction process. I believe that the most recent Financial Plan submission shows an intent to provide this much needed fiscal discipline. However, I believe there is a need for the City to present to the public its best estimate of the service impact of
the proposed budget reduction, and the estimated economic
effect of its programs for increased revenues. Here, too,
State Comptroller Regan has taken the position that this type
of fiscal planning is for the ultimate benefit of the
government involved.

Second, the accelerated plan for achieving a budget balanced
pursuant to GAAP demonstrates to the City's oversight bodies and
to the financial community the City's commitment to meeting
its budgetary obligations. If successfully accomplished, the
City will be able to test the long-term credit markets - after
having met all the goals of the Four-Year Financial Plan - at
a time when alternate means of financing are still available
from the sources provided for in the City's four-year financing
plan. Thus, the City's planned reentry into the markets would
occur in an atmosphere of order and discipline. In contrast, a reentry
program would be more strained if it occurred without the alternative
of other financing options available, and with the prospect
of insufficient cash to meet obligations if market entry proved
more difficult than anticipated. During fiscal years 1979 and
1980, the City's reentry in the short-term market occurred within
such a controlled environment, at a time when loan agreements were
in place to assure the City the short- and long-term financing
it needs. In my opinion, the existence of this facility was
a most significant factor in the City's successful reentry into
the short-term credit markets last January.

Third, by eliminating the need to borrow in fiscal year 1981 for
capitalized operating expenditures, the City has reduced the need
for new debt issuances. This, in turn, will reduce the budgetary
pressures in future fiscal years, and increase the debt restructuring
options.
In this same positive vein, and assuming a successfully balanced budget in fiscal year 1981, I would like to discuss two financing situations that may result in fiscal year 1982.

The first and best situation would be that the City achieves full entry into the long-term public credit market - something we all hope for. In that event, I would recommend that in fiscal year 1982 the City also attempt to finance some or all of its fiscal year 1983 capital spending requirements. Until a solid history of continuing access to long-term financing is assured, it would seem desirable to take maximum advantage of borrowing opportunities in order to help assure continuity of capital funding. This advance bonding is one of these expediens. The proceeds of such financing must by law be set aside to be used only for their intended purposes.

A second and less desirable situation would be if the City is unable to achieve entry into the public long-term market in fiscal year 1982, or if such entry is limited to only a portion of the City's needs. Even in this instance, however, there would still be time for those responsible for managing the City's finances to develop alternate financing strategies for fiscal year 1983 and beyond, to ensure that the City's capital funding requirements can be met.

In spite of these positive elements, however, one should not be deluded into believing that the City's major fiscal problems have been resolved. Therefore, my testimony would not be complete if I did not continue to carry out my responsibilities by pointing out not only the positive aspects of the City's proposed financial plan modification, but also some of the significant risks the City faces in continuing to achieve a balanced budget.

First, the plan submission relies on significant tax increases whose enactment is dependent upon local and in some cases State legislative actions - actions which are far from assured at this time.
Second, accomplishment of the plan is subject to a number of other major uncertainties, including:

. The realization of the increased amounts of State and Federal aid anticipated in the plan;
. The impact of inflation and recession on the revenue and expenditure estimates;
. The size of the projected deficits of the City's semi-autonomous agencies, known as covered organizations;
. The City's continued failure to resolve managerial shortcomings; and
. The size of future labor settlements.

I would like to elaborate on each of these items.

The plan submission anticipates the receipt of $170 million in increased State and Federal assistance in fiscal year 1981 and an additional $240 million in fiscal year 1982. Previous City submissions provided for standby cost reduction programs in case these levels of aid were not achieved. However, no such standby program is either contained or proposed in the most recent submission. In light of the pressure for fiscal restraint evident at both the State and Federal levels, and absent an absolute commitment by these levels of government that they will fulfill the City's expectations, the lack of a standby program is a matter of concern.

The City's plan could also be adversely affected by the negative economic events that are now forecast on a national basis. Economists are predicting an inflation-driven recession having potentially serious adverse affects. The City's plan already anticipates substantial expenditure increases as a result of inflation, particularly in the field of energy. Even greater increases, however, may result if the inflationary pressures of the last calendar year are not abated. For instance, the plan assumes a 25 percent annual increase in fuel costs in fiscal years 1981 through 1984; however, in calendar 1979, such costs increased by about 75 percent.

In addition, the problems of the covered organizations have yet to be
solved. Substantial deficits still loom in the Transit Authority and Health and Hospitals Corporation, and if these deficits materialize, they could place the City's plan in jeopardy. This is particularly so insofar as the Health and Hospitals Corporation is concerned. In the past, the City has substantially increased its operating subsidy to meet the Corporation's budgetary shortfalls, and our preliminary analysis of the most recent plan for the Corporation indicates that subsidy increases may be needed in future years as well—unless the Corporation's revenue collections improve over current levels. The resolution of the Transit Authority's financial woes is also being debated, and the City's Financial Plan does not contemplate that the solution will impact on its budgets.

The City's plan would also be adversely affected by the continued failure on the part of the City to resolve managerial shortcomings that must be eliminated in order that City operations be conducted in a climate which fosters fiscal responsibility. During the past four months my office has issued the first two in a series of reports that focus on various aspects of the City's management controls. These reports have been developed in special consultation with State Comptroller Regan, who has expressed his concern over the need for improvements in the management of City operations. The first of these reports, which focused on the City's implementation of its capital development plan, noted that the methods currently used by the City to formulate and manage its capital program are seriously inadequate, and proposed several major changes in the existing capital processes. The second report noted that the established City procedures for the review and implementation of outside recommendations aimed at improving City operations are not being followed. It is imperative that these recommendations be followed up if the City is to achieve maximum benefit from these efforts.
The largest and most immediate uncertainty relates to the upcoming labor settlements. If the settlements are greater than the amount currently provided for in the Financial Plan - an amount equal to the cost of the settlement that was negotiated in the 1978-80 period - the City's deficits will increase. For example, a 7 percent annual increase, in line with the original Federal guidelines, could increase the City's deficits for fiscal years 1981 and 1982 by approximately $200 million and $375 million, respectively. Each additional 1 percent annual increase would cost $50 million in fiscal 1981 and over $100 million in fiscal 1982.

These concerns, of course, have a material impact on any assessment of the City's near-term financial prospects, and will be considered in my office's review of the City's proposed Financial Plan submission. There is also a long-term concern that I would like to highlight. The City's projections for fiscal years 1983 and 1984 indicate potential gaps of $250 million in fiscal 1983 and $300 million in fiscal 1984. As noted in the City's submission, however, these gaps do not reflect any further labor cost increases beyond 1982. A 7 percent annual increase, for instance, could raise the 1984 gap to over one billion dollars. The possibility of such a large gap only two years after a presumed successful balancing of the City's budget in accordance with GAAP is due to a basic imbalance in the City's revenue and expenditure structure. Most of the City's expenditures can be expected to increase as a result of inflation (average salaries tend to increase in periodic leaps, based on the negotiated pattern). However, there are no assurances that two significant sources of City revenues, which together comprise more than half of the City's revenue stream, will perform similarly. One of these sources is the real estate tax. This tax, in recent years, has not exhibited significant growth despite continued inflation. The other revenue source - State and Federal aid - also does not necessarily increase with inflation.
While the City itself must deal with the sluggishness of real estate tax revenues, this Committee will have significant input into the availability of increased intergovernmental assistance to the City. In the last two years despite a substantial surge in inflation, Federal aid to the City available for budget balancing purposes has actually declined by several hundred million dollars. For one, the City lost countercyclical aid which totalled $140 million in fiscal year 1978. The amount of CETA funds that the City can use to fund municipal employees has also declined, resulting in the reduction of the City's CETA-funded work force by some 11,000 people in fiscal year 1980 as compared to the fiscal year 1978 levels. Moreover, at the same time that such aid has been declining, the Federal government has been mandating substantial increases in City expenditures as a result of new initiatives in special education, medical assistance, and environmental protection. You are all aware of the mandate to improve the quality of education for the handicapped. While the action may have social benefits, it has an adverse impact on the City's budget because the Federal government did not provide the funds to implement the increased services.

In a previous appearance before this Committee in April 1976, I urged that the Federal government revise its procedures for providing aid to local governments. I noted that the Federal government had in many instances imposed new mandates without providing the funds necessary for implementation. I recommended then, and I reiterate now, that the Federal government consider an "all or nothing" standard in setting local mandates, namely, that if it truly believes that a program is necessary, then it should provide full funding for it. Alternately, the institution of the program should be left to local discretion.
I further suggest that the funding provided by the Federal government should be made responsive to inflation, and that the Federal government be prepared to bear the responsibility for many of the costs now borne by local governments which result from national problems, and which should be addressed at a national level. These new initiatives are critical if the City's financial plan objectives are to be accomplished.
Mr. Chairman and distinguished members of the Committee. Thank you for providing me this opportunity to express my views regarding New York City's fiscal situation. I join with the Chairman of this Committee and the representatives of agencies charged with the responsibility for overseeing the City's financial condition in endorsing the direction chartered by the Mayor in his January 16th financial plan. In my various roles since the fiscal crisis in 1975 in monitoring the City's fiscal affairs, I have continually stressed the need for the City to avoid delaying difficult budgetary decisions which remain ultimately necessary for the City's successful re-entry into the public credit markets. Among other issues, I have expressed concern that the City balance its budgets through the use of recurring revenues or savings, recognize the costs of pensions on an accrual basis, institute management reform and, more recently, improve the capacity to control and direct its capital programs.

The Mayor's most recent Financial Plan begins the shift away from the pattern of the 1978, 1979, 1980 Financial Plans which avoided major retrenchment decisions and accelerates the difficult process of confronting the need to achieve and maintain a budget balanced according to Generally Accepted Accounting Principles. I would like to applaud the Mayor in this effort.
In endorsing the Mayor’s strategy, however, I must still express caution and reservation regarding many pieces of the new Plan and the methods by which the City hopes to achieve its goals. With the Mayor’s plan to move to a GAAP balanced budget just six months from now, which necessitates closing larger budget gaps in fiscal 1981 than originally planned, a number of uncertainties remain. The cost of upcoming labor settlements, while impossible to predict, remains a major uncertainty with regard to the City’s Plan. Labor increases in excess of that which is provided for in the current plan could require additional City actions not yet contemplated.

The Health and Hospitals Corporation (HHC) continues to overspend its budget and will require increasing City subsidies. Although the HHC may benefit during the current fiscal year from greater than anticipated State rate increases for Medicaid and possibly substantial rate appeal settlements, a $50 million budget gap in HHC for fiscal 1980 will have to be closed by an allocation from the City’s General Reserve Fund. While there have been some small improvements recently in the HHC’s baseline revenue collections, expenditures are projected to increase from 1981 through 1983 creating larger gaps to be closed in those years. A significant portion of the City’s plan to reduce future budget deficits in the HHC is contained in the Mayor’s Plan for hospital closings and reorganization which must be implemented in the near future in order for the Plan to have the required positive budgetary impact in fiscal 1981 and 1982.

The Board of Education (BE) also continues to cause concern. The new Financial Plan projects expenditure increases for the BE of almost $300 million from fiscal 1980 through 1983. These expenditure increases result largely from State and Federal mandates and Court orders with regard to the education and transportation of handicapped students. These growing costs are not projected
to be offset significantly by intergovernmental aid. In addition, the plan assumes increasing levels of State and Federal education grants from 1981 to 1983 which must be regarded with uncertainty in the current fiscal climate. A significant portion of the Mayor's Plan to eliminate City-wide budget gaps is dependent on large expenditure reductions in the Board of Education ($111 million in 1981) which almost certainly must involve school closings and teacher and other personnel layoffs. As a semiautonomous agency, under pressure to meet Federal mandates, the BE is not directly under the Mayor's control and the proposed cuts in the BE budget will, by their nature, be difficult to achieve.

Although the new Financial Plan begins a strategy which includes City-wide expenditure reductions, the City's Program to Eliminate the Gap in 1981 and 1982 includes the need for additional State and Federal actions of $170 million and $410 million, respectively. It is becoming increasingly evident that both the State and Federal governments are moving into a period of budgetary retrenchment. Even where additional aid appears to be forthcoming, the pattern seems to be a shift from general revenue sharing to categorical assistance, which will make the City's goals for additional intergovernmental budget balancing aid difficult to achieve. The current Financial Plan makes no provision for additional City actions, should this aid fail to materialize.

In order to move to a GAAP balanced budget in 1981, the Mayor has proposed a series of tax increases including a small increase in the property tax, excise tax on beer and liquor, revision of the financial corporation tax,
extension of taxes on gasoline and hotels, and a rate increase for water and sewer services among others. Most of these proposals will require legislative action and therefore must be regarded as uncertain at this time.

The City's Plan may also be negatively affected by national economic events. Although the City's Plan provides for the impact of a mild recession during 1980, it is possible that this recession may be deeper or more prolonged than anticipated. This situation could cause a reduction in revenues which could occur in the face of continued inflationary pressure or expenditures.

Another area of concern to me is in the City's management of its capital program. While it is clearly evident that the City's physical plant is rapidly deteriorating, the City has failed to fully utilize the resources made available to it in the four year plan for bricks and mortar. While the Mayor is correct in pointing out that recreating a viable capital program after three years (1976-1978) of forced inactivity takes time. Management improvements in the capital program have lagged more than those in other areas. The City is not yet at a point where it is meeting its capital needs and there has been a lack of major progress with regard to directing and controlling the capital budgeting and planning process. The ultimate economic viability and habitability of New York City is dependent upon a capacity to plan, finance, and execute restoration of its physical plant.

I will continue in my role in assisting the Municipal Assistance Corporation for the City of New York to monitor these and other areas of the City's fiscal situation with the clear goal of helping to ensure that the Mayor succeeds in a strategy that is on the right road to fiscal health of New York City.

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STATEMENT BY NEW YORK STATE COMPTROLLER EDWARD V. REGAN SUBMITTED TO THE U.S. SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS, JANUARY 29, 1980

Senator Proxmire and distinguished members of the Committee: this committee has indeed a most important responsibility to gather and assess information on the fiscal affairs of the City of New York and to inquire into the nature of the State's response to the needs of the City. My Special Deputy Comptroller for New York City, Sidney Schwartz, gave you his perspective on the City and as a part of his testimony he has discussed the program of the City to develop a balanced budget in accordance with Generally Accepted Accounting Principles (GAAP). I would like to give you an overview of New York State and our movement to provide for an integrated financial management system also based upon GAAP.

Last December 19, I presented to the Governor, the Legislature, the public and the media, a set of prototype financial statements for New York State prepared in accordance with generally accepted accounting principles for the fiscal year ended March 31, 1979. These statements included a comprehensive fund balance sheet showing the State's financial condition, similar in form to the type of report routinely prepared by a business corporation.

The balance sheet showed that New York State had an accumulated deficit of $2,001,834,000. Essentially, this deficit represents the net difference between the State's operating assets and its short-term operating liabilities at the statement date. Analysis shows that the major liability giving rise to the deficit is some $1.6 billion owed by the State to its school districts for education aid. This lag in payment is routinely paid in the first three months following the close of the State's fiscal year through the proceeds we receive from our annual spring borrowing. The background is that in the first three months of every fiscal year, the State's expenditures far exceed its revenues. In no small part this financial imbalance results from the past practices of "rolling over" payments from one fiscal year to the next. Although we meet our obligations routinely each year, the practice which we employ merely addresses the consequences of the problem without coming to grips with the problem itself.
What the State has been doing is well known to the financial community, members of this Committee and others interested in our financial operations. There has been open discussion and adequate disclosure of the whole subject. My predecessor prepared prototype statements for the previous fiscal year and in our most recent official statement the $2 billion deficit was acknowledged. Discussion and disclosure is not enough. Therefore, I have called for the State to shift its system of budgeting, accounting and reporting from a cash to an accrual basis and to budget, account for and report the State's financial activity in accordance with Generally Accepted Accounting Principles. I am pleased to report that the Governor in both his State of the State and Budget messages earlier this month endorsed this program and recommended its adoption. The State Senate has previously gone on record in support of accrued accounting and the State Assembly is seriously considering this proposal. Given this support, I see the conversion to GAAP being accomplished within the next two to three years.

Significantly, the Governor in his Executive Budget for 1980-81 proposes important steps to eliminate the accumulated deficit. The budget calls for the expenditure of $47 million to fully accrue new increases in aid to education. A modest beginning, to be sure, but an essential first effort to dispose of the practice of rollovers. Additionally the Governor has asked for $100 million to be included in the 1981-82 budget to begin the gradual acceleration of education aid payments to place these payments on a current basis. The current financing of new payments and an acceleration of the schedule of existing payments will eliminate the $1.6 billion liability of the major component of the deficit in about 16 years.

Like most other states, New York has kept its books on a cash basis. The lack of discipline under the cash basis leads to flexible financial management and historically Governors and legislatures have manipulated the system at will. How one should consider financial requirements became subordinate to how one could meet these requirements. Expenditures and revenues were routinely moved across fiscal years; tax consequences of new spending programs were routinely deferred and fiscal accountability essentially obscured. New York State's past excessive spending program demands and the attendant tax consequences of these programs were rooted in the loose and undisciplined cash accounting system.
Generally Accepted Accounting Principles extended to our budget, accounting and reporting system will alter these ill-conceived spending opportunities. Financial judgements will have to be made in a disciplined environment. The implications of these decisions will have to be measured against reliable and consistent financial reports. Liabilities will be known and recorded, revenues will be measured and their availability assured. In a word, fiscal accountability will work side by side with the financial management system.

We are taking this very progressive and far reaching step against a background of both misinformation and lack of information about our State finances. The State's economy and revenue base is now sound and stable, its spending has been running well below the rate of inflation and is now more in line with that of other States—yet a $2 billion accrued, accumulated deficit will now be formally discussed and dealt with. I am concerned that there is a potential for initial negative reaction by the financial community to the more accurate disclosure of this financial information. If this occurred, it would be ironic. I have met with the leaders of New York State on this program and I am prepared to meet with the nation's financial communities to explain what we are doing, to answer their questions, and as necessary to correct misimpressions.

What I have discussed here represents a very important set of actions to provide the basis for disciplined fiscal affairs in New York State. Since these actions have the endorsement of State officials, the financial community, the press, and the public, I think it is safe for me to conclude on a note of optimism. The need for fiscal reform by adopting GAAP is evident; there is a clear expression of the will to meet that need. These new initiatives are critical. I am committed to see them through.
TESTIMONY BY

FELIX G. ROHATYN, CHAIRMAN
MUNICIPAL ASSISTANCE CORPORATION FOR THE CITY OF NEW YORK

BEFORE
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNIVERSITY STATES SENATE

FEBRUARY 7, 1980
Mr. Chairman, Members of the Committee:

I would like to report on the status of the Four Year Debt Issuance Plan and MAC's participation in that financing package, as well as our view of the City's budget and our future prospects. We are reaching the halfway mark of this program which was constructed in 1978. The aggregate 4-year financing package amounting to $4.5 billion called on MAC to raise $2.8 billion through public and private sales of MAC bonds, for the City to sell $750 million in federally guaranteed bonds to union pension systems and New York City bonds in the amount of $950 million to be sold publicly in the last two years of the Plan. As backups for contingencies were $900 million of guarantees available under the law and significant additional economic capacity of MAC which I will come back to later in my testimony.

The financing plan is evolving on schedule. As called for in the timetable, MAC has so far issued a total of $1.8 billion of its bonds-- $901 million during fiscal year 1979 and $948 million to date during fiscal year 1980. The $1.8 billion has been raised from the following sources:

--$938 million from private placement to various financial institutions and City Pension Funds according to the terms of the November 1978 Agreement,
--$64 million from an exchange with the New York State Insurance Fund, and
--$847 MILLION FROM PUBLIC SALES

As a direct result of these financings, the City's seasonal borrowing requirements have been reduced from approximately $1.9 billion required in 1978, to approximately $650 million required during fiscal years 1979 and 1980. The short-term credit market viewed this development positively, enabling the City to sell publicly, for the first time since 1975, $275 million of its Notes to meet a portion of its 1979 seasonal financing requirements.

To date, during fiscal year 1980, the City has sold $350 million of its Notes publicly, and expects to meet the balance of its 1980 seasonal requirements from public sales.

A portion of the Corporation's issuances under the plan aggregating $642 million have been for refunding. The refundings have produced a more stable debt service structure which will assist MAC in meeting possible shortfalls in the City's own long-term financing program. They have also been accomplished so as to reduce MAC's average interest cost for the refunded debt by over 100 basis points at a time of an unprecedented climb in the level of interest rates. The refundings have also produced approximately $250 million of net budgetary savings for the City for the period 1980 to 1985, ahead of the schedule committed to at the time of the first Four Year Plan. During
The 1975-76 period, as you will surely remember, MAC had to refinance some $5 billion of City short-term Notes and to finance the City’s operating deficits and capital programs. This occurred during difficult markets and under conditions that were often chaotic. The resulting debt structure included many short-maturity, high interest series of bonds which created enormous budgetary pressures at the time of greatest fragility for the City. This is what we have been dealing with in our overall program to level out our maximum debt service at roughly the $650 million per annum level. Although we have not yet reached that level, it is noteworthy, that, with $6.18 billion in presently outstanding bonds, MAC’s maximum debt service in any future year is approximately $780 million while New York City, with about $6 billion in bonds outstanding has current debt service of about $1.1 billion per annum. Lowering our maximum debt service obviously gives MAC greater economic capacity to carry the City in times of need. Furthermore, as long as it remains obvious that inflationary expectations will remain at or near double digit rates, stretching out our debt instruments to 20-25 years at 8-9% interest rates seems to me to be a clear and simple duty. If current trends continue we may, in a few years, no longer have viable markets for long-term, fixed interest rate bonds in this country; we need only to look to Europe for examples.

With regard to the City’s budget, it has been the position of the Corporation for some time that the adoption of those
MEASURES WHICH ARE ULTIMATELY REQUIRED TO ACHIEVE BALANCE SHOULD NOT BE POSTPONED UNTIL THE FINAL YEAR OF THE PLAN. WE HAVE BEEN CONCERNED THAT GAPS NOT BE CLOSED PRIMARILY ON THE REVENUE SIDE OF THE BUDGET. A SERIES OF NONRECURRING REVENUES, AS WELL AS REVENUE INCREASES RESULTING FROM INFLATION, PROVIDE AN INSECURE FOUNDATION ON WHICH TO BUILD CREDIBLY BALANCED BUDGETS. THEREFORE, WE APPLAUD THE DECISION OF THE MAYOR TO SUBMIT A BUDGET BALANCED ACCORDING TO GENERALLY ACCEPTED ACCOUNTING PRINCIPLES ONE YEAR BEFORE IT IS REQUIRED. IT IS A SINGULARLY IMPORTANT STEP. IT IS AN ACTION FOR WHICH THE MAYOR SHOULD BE COMMENDED, FOR IT DEMONSTRATES CLEARLY A RECOGNITION BY THE CITY OF THE NEED TO ACT WITHOUT DELAY AND THE WILLINGNESS TO IMPLEMENT PAINFUL, BUT NECESSARY, BUDGET CUTS.

Further, the City has to date not succeeded in ministering to its own physical needs. The resources made available to it in this Four Year Financing Plan have not yet been fully applied to those deteriorating streets, sewers, bridges and parks which require immediate attention. The City, together with the State and its agencies, must develop the capacity to plan and execute the restoration of its physical plant. The City and State together must put greater focus on the job-creating, revenue-producing side of the economy that, in the long-run, is going to be the key to our success or failure.

The achievement by the City of a GAAP balanced budget now, and the prospects for repeated balanced budgets in the future, continue to be the single most important test for gaining entry into the credit markets. It is the mark of fiscal stability toward which the investment community has looked since the City's crisis began. While the City does not now have market access for its bonds, the adoption and implementation of a balanced budget for fiscal year 1981, and, the adoption in June 1981 of a balanced budget for fiscal year 1982 should encourage those agencies which rate municipal bonds to recognize the progress which the City has made and assign an investment-grade rating to long-term City securities.

It comes, however, as no great surprise that investment rating services such as Moody's would be more than normally skittish with respect to rating City bonds. The history of the City,
THE MASSIVE AMOUNTS INVOLVED, THE ECONOMIC TRENDS CLEARLY
ADVERSE TO THE NORTHEAST, THE CURRENT TRAVAILS OF CHICAGO,
CLEVELAND, PHILADELPHIA, ETC. ALL CONTRIBUTE TO THEIR RESERVE.
IN EARLIER TESTIMONY IN FRONT OF THIS COMMITTEE I STATED MY
VIEW THAT 2 OR 3 CONSECUTIVELY BALANCED BUDGETS UNDER GAAP
MIGHT BE REQUIRED TO PROVIDE FULL MARKET ACCESS TO THE CITY.
I BELIEVE MY PREDECESSOR, GEORGE GOULD, GAVE A SIMILAR VIEW
IN TESTIMONY LAST YEAR. ALTHOUGH THE FOUR YEAR PLAN CALLS
ON THE CITY TO SELL $300 AND $650 MILLION OF LONG-TERM BONDS IN
FISCAL 1981 AND 1982 RESPECTIVELY, IT WAS ALWAYS RECOGNIZED
THAT THIS MIGHT BE OPTIMISTIC AND THAT MAC SHOULD BE THERE AS
THE FIRST BACKUP, BEFORE THE AVAILABLE LOAN GUARANTEES. THIS IS
THE CASE, NOT ONLY THROUGH 1982 BUT, FROM AN ECONOMIC CAPACITY
POINT OF VIEW, INTO 1984 AND POSSIBLY BEYOND. DURING THIS
PERIOD OF TIME, THE MUNICIPAL ASSISTANCE CORPORATION IS
PREPARED BOTH TO FULFILL ITS OWN PART OF THE FOUR YEAR DEBT
ISSUANCE PLAN, AND TO ISSUE SUCH ADDITIONAL DEBT AS MAY BE
REQUIRED BY THE CITY'S CAPITAL PROGRAM, WHICH WAS TO BE MADE
UP OF CITY BONDS.

AS YOU ARE AWARE, MAC'S ABILITY TO ISSUE DEBT IS CONSTRAINED
ON SEVERAL LEVELS:

- THE ECONOMIC CAPACITY TO ISSUE AND SUPPORT
  DEBT IS LIMITED PRINCIPALLY BY TWO TESTS.
  THE CORPORATION HAS COVENANTED NOT TO ISSUE
  ADDITIONAL FIRST RESOLUTION BONDS IF THE
  MAXIMUM ANNUAL DEBT SERVICE PAYMENTS UNDER
that Resolution in any future year would exceed $425 million. MAC has further
convenanted not to issue additional Second Resolution Bonds unless available revenues
would cover maximum annual debt service payments under that Resolution in any
future year at least two times.

It is difficult to give you an exact estimate of MAC’s additional economic
capacity (as opposed to market acceptance) to carry debt. The obvious variables are
revenue assumptions on the one hand, and assumptions as to the type, maturity and
interest rates on our bonds on the others. It would be reasonable to assume at this
point, that by 1984, given continued satisfactory market acceptance, MAC could
comfortably support an aggregate in excess of $10 billion of outstanding long-term debt.

MAC’s statutory capacity to issue debt (exclusive of the bonds issued for refunding)
is $8.8 billion. To date, the Corporation has issued $6.8 billion.

The Bond Purchase Agreement (under which $2.8 billion of MAC bonds are to be sold as
part of the Four Year Debt Issuance Plan)
Also limited the level of outstanding bonds to $8.8 billion. That agreement further prohibits MAC from issuing other than First or Second Resolution Bonds until such time as the City has an investment-grade rating.

The capacity of the credit market to absorb new MAC debt limits the amount we can issue in any year. This is especially true in markets as irregular as the ones we are now experiencing. We are told by our managing underwriters that $600-$750 million of new debt is the maximum we should attempt to sell in one year.

Despite these constraints, MAC has the capacity to assist the City beyond the scope of the current Plan. The Corporation is already scheduled to place, pursuant to the Bond Purchase Agreement, $537 million of its Bonds in 1981 (of which $353 million is for capital purposes) and $324 million of its Bonds in 1982. It is our estimate that the City’s needs will require that MAC issue approximately $675 million in fiscal years 1981-82 over and above the Plan in order to fund both the City capital and the Corporation’s debt service reserve requirements, if the City fails to market its own securities. This would bring MAC to the end of the Four Year Plan with an aggregate $8.3 billion of debt issued.

Beyond 1982, we anticipate that the City’s capital needs will be in the range of $850-$900 million per year. If MAC were required to finance 100% of the City’s capital needs through
1984 on this schedule, our total issuance would rise to about $10.1 billion. I do not anticipate this happening. If the City continues on track, within a reasonable economic environment, the City capital funding requirements of 1983 and 1984 could be met through a combination of MAC issuances supplemented in ever-increasing amounts by the City's own debt. It is entirely plausible that the City, having implemented four consecutive GAAP balanced budgets and having successfully issued ever-larger amounts of debt for two years, would then be able to fully meet its own capital needs.

A scenario such as I have just outlined requires that MAC issue debt in 1981 and 1982 beyond that which is currently planned. We are prepared to do so. It also requires MAC to issue debt beyond its current statutory authorization. We are prepared to recommend to the Governor and to State Legislature that MAC's authority to issue debt be extended through fiscal 1984 and its ceiling raised by approximately $1.2 billion to $10 billion, thereby sustaining the City and its vital physical reconstruction activities without any additional Federal assistance.

Even though MAC carries the moral obligation of the State, I do not believe such an increase would adversely affect the State's credit. MAC is viewed by credit rating agencies and
INVESTORS AS ESSENTIALLY SECURED BY ITS REVENUE STREAM OF
SALES TAXES AND PER CAPITA STATE AID. THIS STREAM OF REVENUE
LAST FISCAL YEAR AMOUNTED TO $1.9 BILLION AS AGAINST MAXIMUM
DEBT SERVICE REQUIREMENTS IN 1989 OF $786 MILLION. MAC,
 THEREFORE, SHOULD NOT BE A BURDEN AGAINST THE STATE'S GENERAL
CREDIT. THE STATE'S GENERAL CREDIT SITUATION HOWEVER, DOES
AFFECT MAC. WE WERE CONCERNED RECENTLY, WHEN UNCERTAINTIES
WITH RESPECT TO THE STATE'S BUDGET CAUSED A SLIGHT DOWNGRADE IN
THE STATE'S GENERAL OBLIGATIONS BY STANDARD & POOR'S. THE
STATE'S CREDIT RATING, AS A PRACTICAL MATTER, CONSTITUTES A
CEILING AGAINST WHICH MAC HAS TO OPERATE. IT IS VITAL TO
MAC, AND TO THE FINANCING PLAN, THAT THE CREDIT AND BUDGETARY
POSTURE OF THE STATE REMAIN IMPECCABLE. I HAVE SO STATED TO
THE GOVERNOR IN THE STRONGEST POSSIBLE TERMS.

WE BELIEVE THIS PROGRAM SHOULD SEE THE CITY THROUGH. HOWEVER,
WE MUST REMEMBER THAT, BY NOW, MAC HAS BECOME THE LARGEST
ISSUER OF LONG-TERM MUNICIPAL BONDS IN THE COUNTRY, HAVING
PASSED THE STATE OF CALIFORNIA SOME TIME BACK AND WE DO NOT
REACH TO INFINITY.

A PERSUASIVE CASE CAN BE MADE FOR SUCH A SCENARIO AS I HAVE
JUST DESCRIBED; BUT, IN LIGHT OF SOME OF THE TESTIMONY MADE
TO THIS COMMITTEE ONLY LAST WEEK, WE MUST ALSO BE PREPARED
FOR SOME ALTERNATIVE SET OF EVENTS. THEY MIGHT INCLUDE THE
FOLLOWING:
- A SHARPLY DETERIORATING NATIONAL ECONOMIC AND INTERNATIONAL MONETARY ENVIRONMENT,

- REVENUE ASSUMPTIONS INCLUDED IN THE CITY’S BUDGET WHICH FAIL TO MATERIALIZE,

- EXPENDITURE REDUCTION TARGETS WHICH ARE NOT FULLY MET

- A SLOWER THAN ANTICIPATED PROCESS OF RESTORING INVESTMENT-GRADE RATINGS TO CITY BONDS, AND

- DEBT MARKETS SO TIGHT THAT CREDITS PERCEIVED AS WEAKER, SUCH AS NEW YORK CITY, ARE DENIED FULL ACCESS

IF SOME PATTERN OF EVENTS SIMILAR TO THESE WERE TO MATERIALIZE, THE NEED TO SUPPORT THE CITY’S CAPITAL SPENDING PROGRAM MIGHT EXTEND FOR A COUPLE OF ADDITIONAL YEARS. WHILE MAC MIGHT HAVE AMPLE ECONOMIC CAPACITY TO DO SO, THIS SHOULD NOT BE EQUATED WITH UNLIMITED MARKET ACCESS. IN SUCH A CASE, -- IN ORDER TO AVOID SEEKING ADDITIONAL FEDERAL ASSISTANCE BEYOND 1982 BY EXTENDING MAC’S ABILITY TO ASSIST THE CITY OVER A LONGER PERIOD -- IT MIGHT BECOME ADVISABLE TO UTILIZE SOME PORTION OF THOSE FEDERAL GUARANTEES WHICH ARE AVAILABLE IN 1982 UNDER THE CURRENT LAW. THESE GUARANTEES, IN SUPPLEMENT TO MAC’S ISSUING DEBT UNDER THE TWO RESOLUTIONS, AND POSSIBLY ISSUING PURSUANT TO A NEW RESOLUTION, COULD CARRY THE CITY EVEN UNDER THIS MORE SEVERE SET OF CIRCUMSTANCES, UNTIL SUCH TIME AS IT COULD SUPPORT ITSELF.
Under normal circumstances this should not be necessary. We live in unusual times, however, and while I do not anticipate the necessity to make use of the guarantees in 1982, I cannot rule out that this second set of circumstances might occur. However, regardless of which one materializes, given a combination of:

---Resolve on the part of elected City officials, to act decisively now, to bring the budget into balance,

---The cooperation of those governments which reside in Albany and Washington, and

---A viable economic environment for urban America

I do not anticipate that either the City, the State or MAC would turn to Washington after 1982 in search of additional financing assistance.
Senator Proxmire, Distinguished members of the Senate Banking Committee:

Five years ago this month, the first public awareness of the New York City fiscal crises surfaced.

In reviewing the tumultuous and historic events in the intervening years -- the almost daily brushes with bankruptcy, the creation of the Municipal Assistance Corporation and the Financial Control Board, the Federal Seasonal Loan guarantee and, most recently, the Federal guarantee of long-term debt -- even the most critical observer would be impressed by the tremendous progress that has been made in our common effort to enable the City to reenter the capital market on its own.

The City's sales...
The City's sales of short-term securities have been well received by the market place to date and a budget surplus has been generated in each of the past two years, albeit under the existing provisions of State law rather than in accordance with Generally Accepted Accounting Principals (GAAP).

During this same period the City has greatly accelerated its own timetable for market reentry.

Mayor Koch came before you last week with a plan to bring the City budget into balance according to GAAP by the end of City Fiscal Year 1981 -- one full year ahead of the current schedule.

While this is an ambitious plan and there are many uncertainties still to be dealt with, I believe that if the Congress and the Administration will join us, we can achieve the goal of a GAAP balanced City budget in 1981.
New York State assistance has been vital in enabling the City's budget to remain relatively stable in the face of inflation.

Even when measured in constant dollars, direct and indirect State assistance is expected to increase by over 30 percent from CFY 1975-76 through CFY 1980-81.

While we have made use of nonrecurring revenues and will continue to do so where appropriate, our long-range efforts have been directed toward developing a consistent base of support which the City can rely on both now and in the future.

This is especially true of State assumption of city financial burdens such as courts and City University.

Further, we have not limited ourselves to assistance in a strict accounting sense, because our ultimate goal extends beyond technical budget balance.

Essentially, our assistance...
Essentially, our assistance can be roughly divided into the following categories:

First, Direct Aid, including both unrestricted and categorical assistance.

In CFY 1980-81 it is projected that the city will receive approximately $3.6 billion in direct payments from the State's Local Assistance Fund.

Of particular importance to the City is the proposed increase of about $103 million in elementary and secondary education aid.

Second, State takeovers.

By the end of the Financial Plan period, the State will have assumed functions and/or costs which will be saving the City close to $300 million annually.

Included are certain...
Included are certain City court costs which will be 100 percent State funded by the end of the current State fiscal year, the local share of the Supplemental Security Income program -- already a State cost -- and the full assumption of City University Senior College operating costs and the related portion of the CUNY Construction Fund debt service.

Third, **administrative or discretionary assistance**. These include both one-time and recurring State actions which enable the City to increase revenues, and avoid or reduce costs, with an estimated value of approximately $160.0 million in CFY 1980.

Examples include savings generated by the State's Medicaid Management Information and Wage Reporting systems; intensified State personal income tax audits and revenues the City will obtain from the revised Food Stamp Claim when approved by the U.S. Department of Agriculture.

Some of these...
Some of these programs such as MMIS produce corollary savings for the Federal government as well.

Fourth, capital and financing assistance.

While Mr. Rohatyn will discuss MAC's role in more detail, it is worth noting that the City and MAC have reduced the City short-term credit needs from the estimated $4.5 billion in 1975-76 to roughly $600 million projected for CFY 1981.

At the same time, MAC -- aided in part by the Federal Loan Guarantee -- has provided the financing the City needs to repair and revitalize its capital plant.

Finally, support for a developing City economy.

This program includes a wide range of State actions which are not normally considered "aid."

For example, the State is providing one-half of the cost of the phaseout of the Stock Transfer Tax.

As the mayor indicated, the elimination of this tax was crucial to both the City and the State.

To date, the...
To date, the cost to the State is expected to total an estimated $280 million through SFY 1980-81.

In addition, the construction of a $53 million new home for the American Stock Exchange, made possible with State funding from the New York State Urban Development Corporation, will serve to anchor a revitalized lower west side.

That area will also benefit from the State's development of Battery Park City for which the relevant State authority has $200 million in outstanding bonds.

Other actions, such as the State's Accelerated Transit Program, will provide $805 million in improvements for transit and commuter rail in the metropolitan region.

This program is...
This program is being financed by the State and Federal governments without cost to the city. The totally State-financed construction of the new Convention Center, estimated to cost over $360 million, will enhance the City's already burgeoning tourist trade.

The State will also lease Riker's Island from the City at a total cost of approximately $200 million.

While most of the City's attention and that of its various monitors has been directed to the presence or absence of aid increments, State efforts as illustrated in this last category may well be the most meaningful assistance we provide.

These actions go beyond technical budget balance to the important long-range goal of strengthening the City's economy.

Obviously a strengthened...
Likewise, a strengthened City economy reflects favorably on the State's credit and that of MAC as well.

It is clear that New York State has met and exceeded our commitment to aid the City.

In 1979, for example, the State was able to provide $50 million over and above our original commitment of $200 million of assistance.

This additional support was made possible by the willingness of State and City officials to work together to develop a series of actions which benefitted the City while not requiring a dollar-for-dollar increase in State appropriations.

That capability and spirit are there today and will be there in 1980-81.

Thus, even though...
Thus, even though we may constrain the type of automatic, formula-driven expenditure growth experienced in the past, we will not constrain our willingness to provide assistance.

And while the type of aid may differ somewhat from that provided in prior years, our resolve to move the City toward market re-entry remains unchanged.

Yesterday, I met with Mayor Koch to discuss my Executive Budget for Fiscal Year 1980-81, my financial plan for the future and the effect of the plan on the City's ability to reach budgetary balance.

It is clear that the State's commitment for assistance in City Fiscal Year 1979-80 will be met.

For City Fiscal Year 1980-81, there are some differences between the Mayor's analysis and the estimates of my staff;

these differences total approximately $100 million.

We will continue...
We will continue to work with the City to reconcile our estimates.

But the State's commitment to the City's multi-year plan is clear.

Yet while our tax reductions and investments in the economic foundation of the City and the State have paid dividends with rising employment and a quickened pace of private sector investment, this occurred in the context of a growing and resilient national economy.

Now forecasters, including those of the Administration and the Congress, say that growth will end.

Our ability -- New York's and the entire Northeast and North Central part of this nation -- to maintain some semblance of economic well-being in the midst of a national recession is extremely limited.

Already the public...
Already the public sector in the Northeast is facing a host of "recession-related" problems.

Tax increases in New Jersey, budget deficits in Connecticut, local aid constraints in New York are not coincidental.

The same fundamental causes, soaring prices and a flagging economy, give rise to them all.

We in the Northeast recognize that the cure to inflation must be found, at least in part, in a reduction in the pace of economic growth.

What we find difficult to accept is that, while the Federal government expects an economic slowdown and knows from experience that the impact of that slowdown will be felt more directly in the Northeast, it is not willing to engage in any effective targeted countercyclical policies.

I am not referring to the recent actions of the House with respect to the targeted fiscal assistance program, nor even to the practice of saddling State and local governments with unfunded mandates such as special education.

I refer directly...
I refer directly to a fundamental unwillingness to come to grips with the basic economic and energy related problems of the Northeast.

The priorities in the proposed Budget -- for more defense spending, for synfuels, for basic research, to take the top three --- do next to nothing to alleviate our regional problems, both those which already exist and those arising from the scenario on which this budget rests.

We in the Northeast will not benefit from increased defense spending because the existing allocation network bypasses this region.

While we pay the higher and higher bills for the basic necessity of heating our homes, we receive little of the benefit of the windfall profits tax as passed either by the House or the Senate.

Clearly a response...
Clearly, a response to energy problems based on conservation through improved mass transit would be more in keeping with the needs of the Northeast and the interests of the country as a whole; clearly a defense procurement policy that began to redress the decades of inequitable patterns of spending would be a policy responsive to the requirements of both national security and regional wellbeing.

These Federal policies would more closely match budgetary spending priorities with the pain of a budget induced economic slowdown.

This Congress and this Administration will have the opportunity to redress the imbalance in Federal allocations which are a legacy from a time long past -- when New York and the Northeast were capable of fueling the restoration of the South and the development of the Sunbelt.

Decisions you will...
The decisions you make in the coming months on issues such as energy, mass transit funding and allocation of defense dollars are of crucial importance to New York -- not just because of the Federal Loan Guarantee agreement, but because they will decide in large measure the fate of this State and the entire region.

What we must face is the continued displacement of wealth from the Northeast which has ruinous economic consequences for the region.

I had the privilege of serving with the Chairman of this Committee when I served in Congress.

I would ask now that the Joint Economic Committee and this Committee study the problems that the exportation of capital from the Northeast could cause.

Given our dependence...
Given our dependence on imported energy supplies and increasing prices, the economic future of the region is dim.

As our economic future is weakened, so is our ability to sustain our present programs.

What is important to recognize today is that our work is not aimed simply at technical budget balance for the coming year.

The question is not the $100 million still under discussion between the State and the City.

Instead, we must realize that budgets are no better than the economy that supports them.

That is where our real problem lies.

Professor Roy Bahl of Syracuse University has shown that we still have fiscal balance problems.

In 1963, per capita spending in New York was 24 percent above the average level in the rest of the Nation.

By 1975, when...
By 1975, when I assumed office, that spending had increased to 54 percent over the national average; in 1978, New York had a per capita income, excluding transfer payments, two percent above the national average; yet it sustained a level of per capita expenditures 47 percent above the national average.

Indeed, among the ten largest states, New York ranks fifth in per capita income.

But if the burden of Federal, State and local taxes is deducted, New York plunges to last.

The future of this imbalance and our economic growth is not encouraging.

A model recently developed by the United States Department of Energy projected earnings by State, based on assumptions about energy resource availability, economic growth, and the price of imported oil.

This Federal study...
This Federal study, entitled State Earnings Analysis, shows that while all states will grow more slowly through 1985, New York's projected growth in earnings will be the lowest in the nation.

The future of our economy -- the City's, the State's, and the Northeast's -- is what ultimately will determine if the City can go to market.

Bond analysts will look at the economic projections and the economic strengths and weaknesses, not at promises made by a Governor before a Congressional Committee.

Thus, the larger question before the City, the State, this Committee, the Congress, and this Administration is not merely one of balanced budget.

It is the long range economic viability and future of the whole Northeast.

Thank you.