December 30, 1976

TO: Deputy Mayor John C. Burton
    Mr. Steve Clifford
    Mr. Jack Bigel

Here is a slightly revised version of our proposed memo.

Gene Keilin
TO: John C. Burton
    Stephen Clifford
    Eugene Keilin

FROM: John C. Burton

December 30, 1976

Since the recent Court of Appeals decision declaring the moratorium unconstitutional, we have been meeting with all of you as the representatives of the New York City financial institutions whose voluntary agreement on November 26, 1975 provided essential financial assistance to New York City. In our meetings, we have discussed what further commitments may be required of you, not only to deal with the current problem of moratorium notes, but also to deal with the longer-term budgetary and financing needs of the City, at this crucial time in the City's financial crisis.

As you know, the Municipal Assistance Corporation and The City of New York prepared a proposal to deal with the Court decision and communicated the proposal to counsel for the plaintiff in the case. In preparing this proposal, we took into consideration the City's ability to service debt and to finance a capital budget over the next ten years. In other words, our proposal is not merely a "moratorium solution", but rather it addresses the City's total capital and debt service picture.

The plaintiff's counsel has agreed to the timetable of our proposal - repayments of approximately 20 percent by February 1, 1977, another 30 percent by June 30, 1977 and the remaining 50 percent by November 19, 1977. We told him that our ability to meet this schedule of payments was conditioned on the acceptance of our proposal by the City's banks, pension funds, underwriters, and others and by various contingencies related to the City's cash flow. He has refused, however, to accept
these conditions as a limitation on the plaintiff's right to payment. Accordingly, he has submitted to the Court a proposed order unconditionally directing us to pay in accordance with this schedule. We have 30 days, ending January 17, 1977, to supply the Court with a response to the plaintiff's proposed order.

All of these matters have been discussed in detail with the President-Elect. As you know, Mr. Carter responded that bankruptcy was not a viable alternative for the City, and that the new Secretary of the Treasury will review the options for assuring market access and for Federal administrative actions that might be helpful to New York. He indicated that his legislative proposals would contain measures helpful to all urban areas. Mr. Carter also said that he was pleased with the City's progress toward achieving a balanced budget, that he expects this goal to be achieved on schedule, and that he also expects a prompt, local solution to the problem presented by the moratorium notes.

In response to the President-Elect's expectation of a prompt, local solution, and to prepare our submission to the Court of Appeals, we are forced to seek the following commitments from you by January 1, 1977.

1. A voluntary deferral to February 1, 1982, of the initial principal repayment on the MAC Bonds held by you as listed in the schedules delivered pursuant to the agreement dated November 26, 1975. Such deferral must be substantially implemented before the first principal payment on such Bonds now due on February 1, 1977, or we will be unable to achieve the $206 million of savings in MAC debt service funding requirements in the current fiscal year. These are the savings which our proposal contemplates will be made available to the moratorium note holders by February 1, as a 20 per cent partial
payment of their moratorium notes.
The resultant savings in MAC debt service funding requirements are:

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Funding Reductions ($million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1977</td>
<td>$205.8</td>
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</tr>
</tbody>
</table>

These funding reductions result from the deferral by you of only $137 million in payments each year.
We may also ask that you accept as a refunding of your outstanding MAC Bonds, new MAC securities with no capital reserve fund requirement.

2. We assume that the banks will continue their role among MAC's underwriters, whether as related to public offerings contemplated by our present proposal or otherwise. Our proposal contemplates a public offering of approximately $300 million of MAC securities underwritten by MAC's commercial and investment bank underwriters. We contemplate approximately 15 year securities with no principal amortization for the first five years, similar to several MAC Bonds publicly offered in the past. We are attempting to structure a MAC security to be used for these purposes that could be serviced by the City real estate tax as well as by State sales and stock transfer taxes; we are also considering a security that would not require a capital reserve fund. As you know, the current market for municipal securities in general and MAC securities in particular is strong and encouraging. We believe the climate was strengthened still further by the meeting with President-Elect Carter and his expressions concerning the City.
3. Investment by the pension systems collectively, and by the commercial banks collectively, each of an additional $100 million in MAC securities. We are considering a MAC security that would be exchanged for a City Bond, or converted into the kind of MAC security mentioned in Item 2 above, upon the fulfillment of certain conditions. We expect that the MAC security purchased by the institutions would not have a capital reserve fund requirement. The proposed time schedule would call for completion of the institutional sale by June 30, 1977.

4. Reaffirmation of your voluntary agreement, incorporated in the November 26 Agreement, to defer payment of principal on your holdings of City notes. Alternatively, we may ask you to defer such payment beyond the terms of the Agreement. In such event, we would ask you to exchange these notes for other City securities or for MAC securities similar to those referred to in Item 2 above.

5. Unanimous agreement to rescind the provision of the November 26 Agreement that prohibits MAC for using debt service savings resulting from that Agreement in the issuance of new securities. This prohibition, if not withdrawn, would severely limit MAC's ability to produce rational debt service schedules.

6. On July 1, 1978, all present arrangements for the City's necessary seasonal and long-term capital financing will lapse. Therefore, we would like you to consider the conditions under which the banks would be willing to resume their traditional roles as lenders and underwriters to the City, and under which the pension funds would be willing at a minimum to reinvest some portion of their City holdings as such holdings mature after June 30, 1978.
In consideration for the above, we are prepared to do the following:

A. To negotiate a new rate of interest for those MAC securities on which principal is deferred, pursuant to Item 1, above.

B. In exchange for the deferral requested above, to provide a short maturity (1978-82) for the new MAC securities sold to you as described in Item 3 above.

C. If the City notes referred to in Item 4 are exchanged by you for MAC or City securities of longer maturity than currently provided in the November 26 Agreement, to negotiate an interest rate appropriately related to the new maturities.

D. We believe that it is possible to accomplish all of the above, to finance at least $1 billion of annual capital spending in fiscal year 1979 and thereafter and to keep the real estate tax essentially constant, assuming assessed values do not fall and equalization rates do not rise. Such an end to a decade of rapid rises in the real estate tax would mean more than the prospect of tax relief for residents and businesses. In addition, it should indicate to you as lenders and underwriters the possibility that the City can obtain and pay for the borrowing it requires, now and in the future, with a stable tax and without a significant impact on the City's budgets. The achievement of this result assumes balanced City budgets in fiscal year 1978 and thereafter and the kind of sensible, medium-term debt maturities which our proposal contemplates. We will use our best efforts to achieve this orderly structure of financing and taxing.
E. We will continue to undertake other measures relating to the City's economic development and to seek appropriate State and Federal action which recognizes and rewards the City's own efforts toward austerity and reform.

F. We have been asked about the status of the legal action known as Flushing I, which, among other things, concerns the constitutionality of the State legislation which makes available to MAC the revenue stream from the State sales and stock transfer taxes. As you know, bond counsel has issued an opinion that such legislation is constitutional, and the motion made by MAC for summary judgement was granted by the Supreme Court. If you so request, we will consider what action may be taken to expedite final resolution of this litigation.

G. In connection with your consideration of the conditions necessary for the City's return to the capital markets, we are prepared to provide assurances of continuation of the financial and budgetary reforms that will be implemented prior to June 30, 1978 and, should you think it desirable, to consider appropriate debt covenants relating to such reforms. We remind you that the MAC statute requires, among other things, an annual audit of the City's financial statements beginning with the 1978 fiscal year and requires the City to adopt and maintain a balanced budget for 1978 and for each succeeding fiscal year for at least so long as MAC has its own bonds outstanding (currently, until 1995). In addition, the MAC statute requires MAC to receive and review proposed expense budgets for each year, proposed expenditure plans for each upcoming quarter and and expenditure reports for each completed quarter, and to
determine whether each such budget, as proposed, as reviewed quarterly, and as audited, is and will be balanced.
TO:

FROM:

Since the recent Court of Appeals decision declaring the moratorium unconstitutional we have been meeting with all of you as the representatives of the New York City financial institutions whose voluntary agreement on November 26, 1975 provided essential financial assistance to New York City. In our meetings, we have discussed what further commitments may be required of you, not only to deal with the current problem of moratorium notes, but also to deal with the longer-term budgetary and financing needs of the City.

As you know, the Municipal Assistance Corporation and the City of New York prepared a proposal to deal with the Court decision and communicated the proposal to counsel for the plaintiff in the case. In preparing this proposal, we took into consideration the City's ability to service debt and to finance a capital budget over the next ten years. In other words, our proposal is not merely a "moratorium solution", but rather it addresses the City's total capital and debt service picture.

The plaintiff's counsel has agreed to the timetable of our proposal -- repayments of approximately 20 per cent by February 1, 1977, another 30 per cent by June 30, 1977, and
the remaining 50 per cent by November 19, 1977. We told him that our ability to meet this schedule of payments was conditioned on the acceptance of our proposal by the City's banks, pension funds, underwriters, and others and by various contingencies related to the City's cash flow. He has refused, however, to accept these conditions as a limitation on the plaintiff's right to payment. Accordingly, he has submitted to the Court a proposed order unconditionally directing us to pay in accordance with this schedule. We have 30 days, ending January --, 1977, to supply the Court with a response to the plaintiff's proposed order.

All of these matters have been discussed in detail with the President-Elect. As you know, Mr. Carter responded that bankruptcy was not a viable alternative for the City, and that the new Secretary of the Treasury will review the options for assuring market access and for Federal administrative actions that might be helpful to New York. He indicated that his legislative proposals would contain measures helpful to all urban areas. Mr. Carter also said that he was pleased with the City's progress toward achieving a balanced budget, that he expects this goal to be achieved on schedule, and that he also expects a prompt, local solution to the problem presented by the moratorium notes.
So that we may prepare our submission to the Court of Appeals and respond to the need for a prompt solution, we will seek the following commitments from you by January __, 1977:

1. A voluntary deferral to February 1, 1982, of the initial principal repayments on the MAC Bonds held by you as listed in the schedules delivered pursuant to the agreement dated November 26, 1975, (the November 26 Agreement). Such deferral must be substantially implemented before the first principal payment on such Bonds now due on February 1, 1977, or we will be unable to achieve the $206 million of savings in MAC debt service funding requirements in the current fiscal year. These are the savings which our proposal contemplates will be made available to the moratorium note holders by February 1, as a 20 per cent partial payment of their moratorium notes.

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As you know, the current market for municipal securities in general and MAC securities in particular is strong and encouraging. We believe the climate was strengthened still further by the meeting with President-Elect Carter and his expressions concerning the City.

3. Investment by the pension systems collectively, and by the commercial banks collectively, each of an additional $100 million in MAC securities. We are considering a MAC security that would be exchanged for a City Bond, or converted into the kind of MAC security mentioned in Item 2 above, upon the happening of certain conditions. We expect that the MAC security purchased by the institutions would not have a capital reserve fund requirement. We expect to complete the institutional sale by June 30, 1977.
4. Reaffirmation of your voluntary agreement incorporated in the November 26 Agreement, to defer payment of principal on your holdings of City notes. Alternatively, we may ask you to defer further such payment. In such event, we would ask you to exchange these notes for other City securities or for MAC securities similar to those referred to in Item 2 above.

5. Unanimous agreement to rescind the provision of the November 26 Agreement that prohibits MAC from using debt service savings resulting from that 1975 agreement in the issuance of new securities. This prohibition, if not withdrawn, would severely limit MAC's ability to produce rational debt service schedules.

6. On July 1, 1978, all present arrangements for the City's necessary seasonal and long-term capital financing will lapse. Therefore, we would like you to consider the conditions under which the banks would be willing to resume their traditional role as lenders and underwriters to the City, and under which the pension funds would be willing at a minimum to reinvest some portion of the City holdings as they mature after June 30, 1978.

In consideration for the above, we are prepared to do the following:

A. To negotiate a new rate of interest for those MAC securities on which principal is deferred, pursuant to Item 1 above.

B. In exchange for the deferral requested above, to provide a short maturity (1979-82) for the new MAC securities sold to you as described in Item 3 above.
C. If the City notes referred to in Item 4 are exchanged by you for MAC or City securities of longer maturity than currently provided in the November 26 Agreement, to negotiate an interest rate appropriately related to the new maturities.

D. We believe that it is possible to accomplish all of the above, to finance at least $1 billion of annual capital spending in fiscal year 1979 and thereafter and to keep the real estate tax essentially constant, assuming assessed values do not fall and equalization rates do not rise. Such an end to a decade of rapid rises in the real estate tax would mean more than the prospect of tax relief for residents and businesses.

In addition, it should indicate to you as lenders and underwriters the possibility that the City can obtain and pay for the borrowing it requires, now and in the future, with a stable tax and without a significant impact on the City's budgets. The achievement of this result assumes balanced City budgets in fiscal year 1978 and thereafter and the kind of sensible, medium-term debt maturities which our proposal contemplates. We will use our best efforts to achieve this orderly structure of financing and taxing.

E. We will continue to seek appropriate tax relief in other areas and appropriate State and Federal action which recognizes and rewards the City's own efforts towards austerity and reform.
F. We have been asked about the status of the legal action known as Flushing I, which, among other things, concerns the constitutionality of the State legislation which makes available to MAC the revenue stream from the State sales and stock transfer taxes. As you know, bond counsel has issued an opinion that such legislation is constitutional, and the motion made by MAC for summary judgment was granted by the Supreme Court. If you so request, we will consider what action may be taken to expedite final resolution of this litigation.

G. In connection with your consideration of the conditions necessary for the City's return to the capital markets, we are prepared to take steps to assure a continuation of the financial and budgetary reforms that will be implemented prior to June 30, 1978. We remind you that the MAC statute requires, among other things, an annual audit of the City's financial statements beginning with the 1978 fiscal year and requires the City to adopt and maintain a balanced budget for 1978 and each succeeding fiscal year. In addition, for so long as MAC has its own bonds outstanding (currently, until 1995), the MAC statute requires MAC to receive and review proposed expense budgets for each year, proposed expenditure plans for each upcoming quarter and expenditure reports for each completed quarter, and to determine whether each such budget is and will be balanced. Should you think it desirable, the City will determine whether it is authorized
to make a contractual commitment to adopt balanced budgets in future years, and will consider ways to establish a special fund into which tax revenues intended for debt service will be placed during each fiscal year.

EJK/lsd

29 December 1976
FLUSHING NATIONAL BANK, on behalf of itself and all other holders of notes of the City of New York maturing on or before June 30, 1976,

Plaintiff-Appellant,

against

MUNICIPAL ASSISTANCE CORPORATION FOR THE CITY OF NEW YORK; NEW YORK STATE EMERGENCY FINANCIAL CONTROL BOARD; THE CITY OF NEW YORK; and HARRISON J. GOLDIN, Comptroller of the City of New York,

Defendants-Respondents.

SIRS:

PLEASE TAKE NOTICE that the Remittitur, of which the within is a true copy, will be presented for settlement and signature to the Court at the office of the Clerk of the Court, at the courthouse, Albany, New York, on the 17th day of January, 1977, at 10:00 o'clock in the forenoon of that day.

Dated: New York, New York
December 16, 1976.

Yours, etc.

RICHENTHAL, ABRAMS & MOSS
Attorneys for Appellant Flushing National Bank
Office and P. O. Address
122 East 42nd Street
New York, New York 10017
Telephone: (212) 687-8360
TO:

PAUL, WEISS, RIFKIND, WHARTON & GARRISON
Attorneys for Defendant-Respondent Municipal Assistance Corporation for the City of New York
345 Park Avenue
New York, New York 10022

W. BERNARD RICHLAND, Corporation Counsel
Attorney for Defendants-Respondents The City of New York and Harrison J. Goldin, Comptroller of the City of New York
Municipal Building
New York, New York 10007

LOUIS J. LEPKOWITZ, Esq.
Attorney General of the State of New York
Attorney for Defendant New York State Emergency Financial Control Board
Two World Trade Center
New York, New York 10047
REMITTITUR

COURT OF APPEALS
STATE OF NEW YORK

The Hon. Charles D. Breitel, Chief Judge, Presiding

No. 391

FLUSHING NATIONAL BANK, on behalf of itself and all other holders of notes of the City of New York maturing on or before June 30, 1976,

Plaintiff-Appellant,

—against—

MUNICIPAL ASSISTANCE CORPORATION FOR THE CITY OF NEW YORK; NEW YORK STATE EMERGENCY FINANCIAL CONTROL BOARD; THE CITY OF NEW YORK; and HARRISON J. GOLDB, Comptroller of the City of New York,

Defendants-Respondents.

The appellant in the above entitled appeal appeared by Richenthal, Abrams & Moss (Arthur Richenthal, of counsel), New York City; the respondent Municipal Assistance Corporation for the City of New York, by Paul, Weiss, Rifkind, Wharton & Garrison (Simon H. Rifkind, Robert L. Laufer and Howard S. Veisz, of counsel), New York City; the respondents The City of New York and Harrison J. Goldin, Comptroller of the City of New York, by W. Bernard Richland, New York City Corporation Counsel (James G. Greilsher, L. Kevin Sheridan, Leonard Koerner, and James Griffin, of counsel); and the respondent New York State Emergency Financial Control Board, by Louis J. Lefkowitz, Attorney General for the State of New York (Shirley Adelson Siegel and Samuel A. Hirshowitz, of counsel).
The Court, after due deliberation, and upon application by Richenthal, Abrams & Moss, attorneys for appellant,

ORDERS AND ADJUDGES, that the order of the Appellate Division of the Supreme Court, First Judicial Department, entered in the Office of the Clerk of said Appellate Division on May 4, 1976, affirming the judgment of the Supreme Court, New York County, entered in the Office of the Clerk of the County of New York on December 24, 1975, granting respondents' motions for summary judgment dismissing the amended complaint and denying appellant's cross-motion for summary judgment, is reversed, with costs to appellant, and said judgment entered on December 24, 1975, is vacated; and

FURTHER ORDERS AND ADJUDGES, that appellant is entitled on its motion for summary judgment to a judgment declaring that the New York State Emergency Moratorium Act for the City of New York (L. 1975, ch. 874, as amd. by L. 1975, ch. 875) violates the "faith and credit" provision of the Constitution of the State of New York, Article VIII, § 2; and is therefore unconstitutional under the Constitution of the State of New York; and

FURTHER ORDERS AND ADJUDGES; that appellant is entitled to a judgment directing the City of New York to perform its constitutional duty to make payment in full of principal and interest, in lawful money of the United States of America, in accordance with the schedule of payments set forth in the next
ordering paragraph, of all Revenue Anticipation Notes ("RANS") and Bond Anticipation Notes ("BANS") issued by the City of New York, more particularly described below, the holder of which has not exchanged such note for an obligation of the Municipal Assistance Corporation for the City of New York, and excluding such notes held by the Municipal Assistance Corporation for the City of New York ("MAC") and by the banks, pension funds and sinking funds that are parties to the Amended and Restated Agreement dated November 26, 1975 with MAC:

<table>
<thead>
<tr>
<th>Date of Issue</th>
<th>Specified Maturity Date</th>
<th>Stated Annual Interest Rate</th>
<th>Type</th>
</tr>
</thead>
<tbody>
<tr>
<td>12/13/74</td>
<td>12/11/75</td>
<td>9.50%</td>
<td>RANS</td>
</tr>
<tr>
<td>1/13/75</td>
<td>1/12/76</td>
<td>9.40%</td>
<td>RANS</td>
</tr>
<tr>
<td>2/14/75</td>
<td>2/13/76</td>
<td>7.55%</td>
<td>RANS</td>
</tr>
<tr>
<td>3/14/75</td>
<td>3/17/76</td>
<td>8.75%</td>
<td>BANS</td>
</tr>
</tbody>
</table>

upon presentation of such note for payment; and

FURTHER ORDERS AND ADJUDGES, that the schedule of payments referred to in the preceding ordering paragraph shall be as follows:

Twenty (20%) per cent of the original principal amount of each such note shall be paid on or before February 1, 1977;

Thirty (30%) per cent of the original principal amount of each such note shall be paid on or before June 30, 1977; and

The entire unpaid principal amount of each such note shall be paid on or before November 19, 1977.

Together with each such payment of principal, the City of New York shall pay to the holder of such note, interest at the
interest rate per annum stated in the note certificate, on the
unpaid principal amount of such note, from its stated original
maturity date to the scheduled date(s) of payment of principal,
less any interest payment heretofore made by the City of New York
on such note for any period after the stated original maturity
date of such note; and

FURTHER ORDERS AND ADJUDGES, that the Court retains
jurisdiction in matters arising from implementing and enforcing
this remittitur or the judgments to be entered in accordance with
this remittitur.

The Court—FURTHER ORDERS that the papers required to
be filed and this record of the proceedings in this Court be
remitted to the Clerk, Supreme Court, New York County, there to
be proceeded upon according to law.

I certify that the preceding contains a correct
record of the proceedings in this appeal in the Court of Appeals
and that the papers required to be filed are attached.

Joseph W. Bellacosa, Clerk of the Court

COURT OF APPEALS
STATE OF NEW YORK

No. 391

FLUSHING NATIONAL BANK, etc.,

Plaintiff-Appellant,

—against—

MUNICIPAL ASSISTANCE CORPORATION, etc., et al,

Defendants-Respondents.

NOTICE OF SETTLEMENT
OF REMITTITUR

LAW OFFICES
OF
RICHENTHAL, ABRAMS & MOSS

Attorneys for Plaintiff-Appellant
122 EAST 42nd STREET
NEW YORK CITY
637-9360

DUE SERVICE OF WITHIN PAPER IS HEREBY
ADMITTED
December 10, 1976

MEMORANDUM

RE: Alternate City funding source.

In light of the difficult situation faced directly by the City as a result of the court decision voiding the Note Moratorium, and indirectly by the banks and pension funds faced with additional pressure for credit, alternate means of securing money for the City from its own resources have been considered. The following is a proposal with some degree of feasibility:

It is proposed that the City of New York place tolls on the East River approaches to Manhattan which are now free.* Furthermore, it is recommended that the newly tolled facilities (the Brooklyn, Queensboro, Manhattan, Williamsburg and several other smaller bridges) be merged into the facilities pledged to the revenue stream of the Triborough Bridge and Tunnel Authority (TBTA).

The City could then sell title to all TBTA-run facilities to the TBTA. The proceeds of the sale would enable the City to redeem all, or substantially all of its outstanding publicly held short-term notes. Such sale could be arranged through a financing which would: 1) refund all outstanding TBTA debt, thereby defeasing all prior bondholder liens and indentures, and 2) allow the sale of traditional toll revenue bonds secured by System cash flows as determined by a traffic consultant to provide ample bondholder protection.

The above financing would affect a current arrangement whereby surplus TBTA receipts are used to support the Metropolitan Transportation Authority (MTA) and New York City Transit Authority (TA) as an operating subsidy (such subsidy was $81.0 million in 1975). However, the additional revenues from the East River approach facilities should allow a continuation of some form of subsidy arrangement, with any loss in subsidy theoretically provided from reduced New York City General Fund expenditures for bridge maintenance on the East River approaches, and/or increased Federal Assistance for TA/MTA subsidies. In addition, since the City would apply sale moneys generated to retire the $1 billion Note debt, freed up interest on such debt of $60 million per year could be applied to the TA/MTA subsidy. Conceivably the TA/MTA subsidy could increase over 1975 levels as a result of appropriation of interest on the City notes to TA/MTA subsidy.

*Note: It has been determined that there are two obstacles to tolling the East River approaches: 1) the political intransigence of the Mayor and City Controller who are, by policy, opposed, and 2) U. S. Department of Transportation regulations which prohibit tolling of the Hamilton, Washington and Williamsburg bridges, or the west-bound lane of the Manhattan Bridge, all of which have been built or repaired with Federal funds and declared "free bridges". Should there be no hope of overcoming these obstacles, the refunding and sale of existing TBTA facilities would still be feasible and provide a great deal of capital for the City.
Of $260,910,000 total TBTA bonded debt to be outstanding at 3/2/77, $185,910,000 could be called immediately at par and refunded. $75,000,000, the balance, could be callable 3/1/79 at 100 1/2%. Interest, at 6 1/4%, principal and the 1/2% call premium, would be provided from investment of $75 million of new bond proceeds in U. S. government obligations until the first available call date. After the effect of investment, the $75 million bonds would be almost self-supporting, based upon the yield on two-year Treasury paper.

The following numbers indicate a very rough work-up of the estimated revenues of TBTA which would be available for debt service, with and without East River toll revenue:

<table>
<thead>
<tr>
<th></th>
<th>With East River Tolls</th>
<th>Without East River Tolls</th>
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<tbody>
<tr>
<td>1976 Gross Revenues¹</td>
<td>$200,500,000</td>
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</tr>
<tr>
<td>East River Crossing Revenues²</td>
<td>70,000,000</td>
<td>---</td>
</tr>
<tr>
<td>Less: Personnel Costs²</td>
<td>(32,000,000)</td>
<td>(25,500,000)</td>
</tr>
<tr>
<td>O&amp;M²</td>
<td>(20,000,000)</td>
<td>(14,900,000)</td>
</tr>
<tr>
<td>Repair and Replacement Reserve²</td>
<td>(20,000,000)</td>
<td>(15,000,000)</td>
</tr>
<tr>
<td>Net Available for Debt Service</td>
<td>$198,500,000</td>
<td>$145,100,000</td>
</tr>
<tr>
<td>To be used for Debt Service</td>
<td>$150,000,000</td>
<td>$120,000,000</td>
</tr>
<tr>
<td>Available Surplus for MTA³</td>
<td>$48,500,000</td>
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</tr>
</tbody>
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¹From TBTA February, 1976 Official Statement.
²Internal estimate based on current TBTA costs of operation.
³The available surplus, together with $60 million in interest, to be saved by payout of the City's $1 billion notes, will provide $108,500,000 or $80,000,000, respectively, for TA/MTA subsidy.

$150,000,000 per year, at 8% interest cost would fund approximately $1.5 billion in principal over a 20-year period on a level annual debt service basis, with net revenue coverage of maximum annual debt service, before application of surplus to TA/MTA, over 1.30 times. $120,000,000 per year, on the same basis, would provide $1.2 billion. The net proceeds to the City would be $1.34 billion, or $940 million, respectively, after the effect of refunding existing TBTA debt.

It is felt that the political cost of tolling the East River approaches would be outweighed by the economic advantages to be provided from toll plaza construction employment, the rehiring of laid off City personnel for toll collection and bridge maintenance, and a reduced drain on the City's General Fund, while providing for full cash payment, from a new source, of the City's note debt. It is felt that a well-secured revenue bond can be sold and that the City must look to its own resources to solve its problems and not apply further pressure upon the banks and pension funds to purchase additional MAC or City debt.
ART. VII, § 3.4

CONSTRUCTION

The effect of the constitutional provision of this part of this chapter and the provisions of this part of this chapter, including their interpretation and construction, shall be construed in accordance with the purposes of the Constitution and the laws of the State and shall be so construed as to give effect to the constitutional provision of this part of this chapter and the provisions of this part of this chapter, including their interpretation and construction, and as to give effect to the constitutional provision of this part of this chapter and the provisions of this part of this chapter, including their interpretation and construction, as a whole, in such a manner as to accord with the legislative intent. In case of any conflict, the provisions of this part of this chapter shall prevail over the provisions of this part of this chapter, including their interpretation and construction. In case of any conflict, the provisions of this part of this chapter shall prevail over the provisions of this part of this chapter, including their interpretation and construction. In case of any conflict, the provisions of this part of this chapter shall prevail over the provisions of this part of this chapter, including their interpretation and construction. In case of any conflict, the provisions of this part of this chapter shall prevail over the provisions of this part of this chapter, including their interpretation and construction.
December 7, 1976

Dear Gene:

Over the last several days I have received a number of calls from Sally Farrell of Carter, Ledyard & Milburn, counsel to the United States Trust Company, and from Sandy Altman of the City with respect to the interest rate which should be paid on short-term notes of the City ("City Notes"), which are still outstanding in the hands of the public, the Clearinghouse Banks and the City Pension Funds, and City Notes which were exchanged for MAC Bonds in connection with MAC's exchange offers for its 1976 Series 5 and Series 6 Bonds. You will recall that under the Moratorium Act, it was contemplated that holders of City Notes who did not exchange their City Notes for MAC Bonds would be paid one year's interest at the rate of 6% on the anniversary of the scheduled maturity date of their City Notes, and that holders of City Notes who exchanged their Notes for MAC Bonds in the exchange offers referred to above would receive interest on their City Notes from the original scheduled maturity date of their City Notes through June 21, 1976 at the rate of 6%.

As we discussed last week, although the primary responsibility for determining the amount and manner of payment of such interest is obviously the City's, it would seem appropriate that MAC should have some input into this decision because of MAC's involvement in the exchange offers, as well as in other aspects of City finance, including the development of a plan to repay City Notes held by the public.
There would appear to be at least four alternatives available to the City with respect to such interest payments:

1. The City could pay interest on all City Notes at the rate of 6%. We believe that the City continues to have the authority to pay such interest based on the provisions of the Moratorium Act, which are still effective until a remittitum has been settled by the parties and a formal court order has been issued. In our judgment, the main argument in favor of paying 6% is that a payment at such rate is necessary in order to fulfill one of the conditions of the Amended and Restated Agreement of the obligation of the Banks and the Pension Funds to defer until 1986 payment in full of the City Notes held by them. Such condition clearly provides that the City timely pay interest at least annually at the rate of 6% a year on all short-term notes of the City, including those held by the public and those which were exchanged for MAC Bonds. As you know, we have taken the position that the Flushing II decision does not release the Banks and the Pension Funds from fulfilling such obligation. In order for us to continue to maintain this position, the City will have to fulfill this condition by paying interest at the rate of 6% until the court issues its order in the Flushing II case.

2. The City could pay interest on all City Notes at a rate of 3%. The City Corporation Counsel has taken the view that the City is authorized to pay such rate by the provisions of Section 3-a of the General Municipal Law, which provides that interest accrues on "any judgment or accrued claim" at the rate of not greater than 3%. I have attached, for your information, a copy of the statute.

3. The City could pay no interest at the present time pending the issuance of an order by the court with respect to the payment of all City Notes. Such an order could be drafted to provide the appropriate rate of interest payable on all City Notes.

4. The City could choose one of the above three alternatives with respect to Notes still outstanding in the hands of the public, the Banks and the Pension Funds, while choosing another of the alternatives with respect to the City Notes which were exchanged for MAC Bonds.

There are at least two reasons why the City might choose to treat City Notes in one class different
from City Notes in the other class. The first reason is that, in the event of any payment at a rate above that which might be ultimately ordered by a court, the City would probably "recapture" any overpayment with respect to City Notes held by the public, the Banks and the Pension Funds by offsetting such overpayment against amounts payable in the future, but the City could probably not "recapture" any amounts paid to holders of City Notes who had exchanged their City Notes for MAC Bonds because this payment is a one time only payment. A second reason why the City might choose to treat the two classes of City Notes differently is that it might be felt that holders of City Notes who exchanged their City Notes for MAC Bonds should be entitled to receive interest at a rate of 6% because they may have assumed that in making their exchange, the 6% rate was part of the package which they accepted. The MAC Official Statement and the related documents that were used in connection with the exchange offer stated that the City would pay interest on the exchanged City Notes at the rate of 6% or such other rate as may be determined by applicable law. There is, therefore, no requirement that the City pay interest to such former holders at the rate of 6%, although, as a policy matter, there may be some desire to give the persons who exchanged their City Notes the benefit of the 6% rate, even if the court ultimately determined that a rate lower than 6% could legally be paid.

We believe that, as a legal matter, the City is not required to choose any particular one of these four alternatives, but, rather, is permitted to choose any one of such alternatives. The question is, therefore, a policy question with respect to which we believe your advice would be useful to the City. It would seem to us that the preservation of our legal position under the Amended and Restated Agreement, as explained under alternative 1, is a factor which should be accorded great weight.

The City will have to make some decision this week as to the method it proposes to adopt, because the anniversary of the first of the series of affected City Notes occurs on Saturday, December 11, 1976, and it was originally anticipated that interest checks would be mailed by United States Trust Company on behalf of the City on or about December 10, 1976. Sally Farrell has informed me that United States Trust Company had intended to enclose the interest checks payable to former holders of City Notes who exchanged such Notes a brief explanation of such interest. I have enclosed a copy of such explanation, which obviously may have to be altered depending upon the City's determination of the amount of the interest payment. In addition, Sally has requested that United States
Trust Company be provided as much lead time as possible in order to provide for the printing of any explanation which would accompany any interest checks which would be sent on December 10, 1976.

Allen or I will be happy to discuss in greater detail any of the matters set forth in this letter.

Best regards.

Sincerely,

Frederick R. Cummings, Jr.

FRC: cq
Encls.
GENERAL MUNICIPAL LAW

§ 3-a. Rate of interest on judgments and accrued claims against
municipal corporations.

1. Except as provided in subdivision two of this section, the rate of
interest to be paid by a municipal corporation upon any judgment or
accrued claim against the municipal corporation shall not exceed three
per centum per annum.

2. The rate of interest to be paid upon any judgment or accrued
claim against the municipal corporation arising out of condemnation pro-
ceedings shall not exceed six per centum per annum.

3. The term "municipal corporation" as used in this section shall
mean and include a city, county, town, school district, fire district,
and special or public district organized for the purpose of financing the
or retirement system support costs of public improvements or a pension
system in whole or in part by any such city, county, town, school
district, or special or public district.


6. L.1969 inserted references to a fire district.

Supplementary Index to Notes
Claims against retirement system 16
Interest payable by municipalities 15
Property leased by municipality 14

1. Constitutionality

This section limiting interest payable to condemned property owners to 4 per cent was not unconstitutional on ground that it deprived landowners of just compensation. In re Real Properties on Long Island, supra, 35 Misc.2d 409, 301 N.Y.S.2d 925.

2. Where State Finance Law § 16 provided for payment of 6% maximum interest in condemnations, provisions for payment of only 4% upon condemnation of land by town was unconstitutional, and provisions of this section insofar as rate of interest was concerned were unconstitutional, and award for condemnation by town must bear interest at rate of 0% from date of State Finance Law § 16, providing for payment of 0% by State. In re Town of Hempstead, supra, 35 Misc.2d 134, 294 N.Y.S.2d 398.

3. With other laws

When award is rendered against municipality, this section, with its prescribed rate of interest, should be read and applied in pari materia with provisions of CPLR art 301, et seq., relating to awards of interest. Aeme Building Inc. v. Nassau County, 1971.

Accrued claims

Whether judgments against municipal corporations are also subject to the interest that may be awarded in a suit for breach of contract from corporations' assessments of value.

§ 3-a. Rate of interest on judgments and accrued claims against municip

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December 7, 1976

BY HAND

Eugene J. Keilin, Esq.
Executive Director
Municipal Assistance Corporation
For The City of New York
Two World Trade Center
New York, New York 10047

Dear Gene:

Over the last several days I have received a number of calls from Sally Farrell of Carter, Ledyard & Milburn, counsel to the United States Trust Company, and from Sandy Altman of the City with respect to the interest rate which should be paid on short-term notes of the City ("City Notes"), which are still outstanding in the hands of the public, the Clearinghouse Banks and the City Pension Funds, and City Notes which were exchanged for MAC Bonds in connection with MAC’s exchange offers for its 1976 Series 5 and Series 6 Bonds. You will recall that under the Moratorium Act, it was contemplated that holders of City Notes who did not exchange their City Notes for MAC Bonds would be paid one year’s interest at the rate of 6% on the anniversary of the scheduled maturity date of their City Notes, and that holders of City Notes who exchanged their Notes for MAC Bonds in the exchange offers referred to above would receive interest on their City Notes from the original scheduled maturity date of their City Notes through June 21, 1976 at the rate of 6%.

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Allen or I will be happy to discuss in greater detail any of the matters set forth in this letter.

Best regards.

Sincerely,

Frederick R. Cummings, Jr.

FRC: cq
Encls.
GENERAL MUNICIPAL LAW
§ 3-a. Rate of interest on judgments and accrued claims against municipal corporations.
1. Except as provided in subdivision two of this section, the rate of interest to be paid by a municipal corporation upon any judgment or accrued claim against the municipal corporation shall not exceed three per centum per annum.
2. The rate of interest to be paid upon any judgment or accrued claim against the municipal corporation arising out of condemnation proceedings of any governmental entity, including a city, county, village, town, school district, fire district, or any combination thereof, shall be paid at the rate of six per centum per annum.
3. The term "municipal corporation" included in this section shall mean and include a city, county, village, town, school district, fire district, or any combination thereof, including, in whole or in part, any such city, county, village, town, school district, or special or public district.
L.1969 substituted "six" for "four" per centum.
Supplementary Index to Notes
Claims against retirement system 16 Interest payable by municipalities 15 Property leased by municipality 14
1. Constitutionality
This section limiting interest payable to four per cent did not require compensation to local governments. In re Real Property. (1966), 58 Misc.2d 400, 295 N.Y.S.2d 909, the State of New York v. Mayor of the City of Amsterdam, 58 Misc.2d 400, 295 N.Y.S.2d 909, held that the provisions of this section were not unconstitutional.
Where State Finance Law § 16 provided for payment of 6% maximum interest in condemnation cases, the provisions of this section were not unconstitutional. In re State Finance Law § 16, providing for payment of 6% of state and city taxes, held to be constitutional. In re Town of Hempstead, Lido Beach, Nassau County, 1968, 38 Misc.2d 314, 294 N.Y.S.2d 589.
2. Generally
This section providing that interest on judgments and accrued claims against municipal corporations shall not exceed three per centum on account of benefit and performance of local governments and their taxpayers, and its benefits may not be waived by municipal officers. New York v. Long Island Rail Ro. Co. v. City of New York, 8 Report, 1965, 49 Misc.2d 606, 277 N.Y.S.2d 737.
3. Power of court
Only mortgage lien is affected by condemnation, and even after condemnation of mortgaged property, holder of note may assert his rights against mortgagee on note and not be barred by non-purchase by compulsion or purchase by condemnation. Barten v. South Point Marine, Inc., 1966, 17 N.Y.2d 291, 270 N.Y.S.2d 500, 217 N.E.2d 671.
4. Accrued claims
Whether judgments against municipal corporation are based on damages from corporation's overassessment of...
United States Trust Company
of New York
45 Wall Street New York, N.Y. 10005
212-425-4500

To the original holders of Revenue Anticipation Notes
for the City of New York, formerly 9.50% due December 11,
1975 tendered pursuant to the MAC Exchange Offer

The enclosed check represents 6% interest payable through June 21,
1976 on the exchanged notes at the rate of $31.5616 per $1,000 of notes.
This rate was calculated for 192 days on the basis of a 365 day year from
the original maturity date of the notes: December 11, 1975.
United States Trust Company
of New York
45 Wall Street New York, N.Y. 10005
212-425-4500

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6 December 1976

Arthur Richenthal, Esquire
Richenthal, Abrams and Moss
122 East 42nd Street
New York, New York 10017

Re: Flushing National Bank vs. Municipal Assistance Corporation
For The City of New York, et al.

Dear Mr. Richenthal:

In accordance with your recent Request for Documents, dated November 29, 1976, the Municipal Assistance Corporation is furnishing, with this letter, four copies each (except as noted) of the following documents:


Request Item 9: Debt Service Payment Schedules for First General Bond Resolution Bonds of the Municipal Assistance Corporation For The City of New York, with original holders indicated; Debt Service Schedule for Second General Bond Resolution Bonds of the Municipal Assistance Corporation For The City of New York;
See also Exhibit 1, Notes to Financial Statements, 1976 Annual Report, Municipal Assistance Corporation For The City of New York, page 33.

The documents requested in the remaining items on your list are being furnished to you separately by The City of New York.

Sincerely,

[Signature]

Stephen J. Weinstein
Deputy Executive Director

Enclosures (25)

cc: Allen L. Thomas, Esquire
    Paul, Weiss, Rifkind, Wharton and Garrison

SJW/mp

bcc: Mr. James Brigham
     Office of Deputy Mayor For Finance

    Mr. Sol Lewis
    Third Deputy Comptroller

    Mr. Jeffrey Heintz
    Office of Management and Budget
Request for Documents (4 copies of each)


2. Same for State of New York (July or August 1976).


4. Certified copy of City's last complete Official Statement actually delivered to the purchasers of bonds or notes of the City and any supplement necessary to update material to December 5, 1976.

5. Same for MAC and State of New York.


7. Most recent Certified Debt Statement with respect to 105 General N.Y.S. Const. Debt Limit (Art. 8).

8. Maturity and P. & I. Schedule for City Bonds Outstanding, Long Form, with each year shown separately.

   (P. & I. = Principal and Interest.)

9. Same for MAC; list purchasers (public as group) and present holders of each Series (public, pension funds, bank, etc.)

10. Short-term Notes Outstanding of the City and MAC, by type, date of issue and maturity, rate of interest, principal and interest due at maturity, a list of taxes or revenues uncollected on December 1, 1976, against which such notes were originally issued; amount, if any, segregated for repayment of the notes, and percent of estimated specific taxes and revenues actually received and collected in last three fiscal years. Purchasers and present holders of the notes (Federal Government, pensions, banks, MAC, public).

11. Agreements with banks and pension funds for extension of City notes; agreement with Federal Government on Seasonal Loans.
12. List of all taxes imposed by the City of New York within the incorporated area of the City in the last three years, and the rates of collection thereof in the same year and in each subsequent year until collected.

13. Schedule of loans (or "first instance appropriations") made by State to City over the last three years and the dates of repayments thereon.
FLUSHING NATIONAL BANK, on behalf of itself and all other holders of notes of the City of New York maturing on or before June 30, 1976,

Plaintiffs,

against

MUNICIPAL ASSISTANCE CORPORATION FOR THE CITY OF NEW YORK; NEW YORK STATE EMERGENCY FINANCIAL CONTROL BOARD; THE CITY OF NEW YORK; and HARRISON J. GOLDBIN, Comptroller of the City of New York,

Defendants.

NOTICE OF MOTION
FOR
CONSOLIDATION
and
CLASS ACTION
AUTHORIZATION

PYRAMID SERVICE CO., on behalf of itself and all other holders of unpaid short term obligations of the City of New York matured between December 11, 1975 through March 12, 1976,

Plaintiff,

against

THE CITY OF NEW YORK,

Defendant.

Index No. 08578/76
(Altion No. 2)
S I R S:

PLEASE TAKE NOTICE that upon the determination of the Court of Appeals of the State of New York dated 19 November 1976 whereby, in Action No. 1 herein, the New York State Emergency Moratorium Act of 1975 for the City of New York was declared unconstitutional, and upon the Remittitur issued by the said Court in said Action No. 1 on 8 February 1977, and upon the pleadings in Action No. 2 herein, the undersigned will move this Court at a Special Term thereof to be held by Hon. James Gibson, Justice, at the Courthouse located at No. 60 Centre Street, New York, New York, on the 25th day of February 1977 at 9:30AM or as soon thereafter as counsel can be heard, for an order:

(a) pursuant to CPLR §602(a) consolidating the above entitled actions, upon the grounds that said actions share common questions of law and of fact; that consolidation will expedite disposition of both actions; and that the Remittitur issued by the Court of Appeals in Action No. 1 authorizes and contemplates such consolidation; and

(b) pursuant to CPLR §902, 903 and 904 determining that
Action No. 2 may be maintained as a class action, describing the class as set forth in the Amended and Supplemental Complaint in said Action No. 2 herein, and determining that notice of the pendency of Action No. 2 need not be given to the members of the said class, upon the respective grounds that:

(i) the prerequisites of CPLR §901 have been met,

(ii) notice to the members of the class is not necessary to protect the interests of the represented parties,

(iii) the individual members of the class are so numerous, widely dispersed and unidentifiable that notice to them cannot be reasonably or effectively given,

(iv) the cost of any attempted notice will prevent the action from going forward, and

(v) the grant of class action status constitutes a salutary and substantive remedy invoked as part of the relief sought by the plaintiff class

And for such other, further and different relief as the Court may deem proper.

Dated: Bethpage, New York
15 February 1977

WILLIAM I. NILES
Attorney for Plaintiff
(Action No. 2)
4250 Hempstead Tpke.
Bethpage, N. Y. 11714
(516) 796-7000
To:-

W. BERNARD RICHLAND,
Corporation Counsel
Attorney for Defendant
    (Action No. 2)
Municipal Building
New York, N. Y. 10007.

RICHTHAL, ABRAMS & MOSS, ESQS.
Attorneys for Plaintiff
    (Action No. 1)
122 East 42nd Street
New York, N. Y. 10017

PAUL, WEISS, RIFFKIND, WHARTON & GARRISON, ESQS.
Attorneys for Defendant,
    Municipal Assistance Corporation (Action No. 1)
345 Park Avenue
New York, N. Y. 10022

LOUIS J. LEFKOWITZ,
Attorney General of the State of New York
Attorney for Defendant,
    NYS Emergency Financial Control Board (Action No. 1)
Two World Trade Center
New York, N. Y. 10047
SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

FLUSHING NATIONAL BANK, on behalf of itself and all other holders of notes of the City of New York maturing on or before June 30, 1976,

Plaintiffs,

-against-

MUNICIPAL ASSISTANCE CORPORATION FOR THE CITY OF NEW YORK; NEW YORK STATE EMERGENCY FINANCIAL CONTROL BOARD; THE CITY OF NEW YORK; and HARRISON J. COLDIN, Comptroller of the City of New York,

Defendants.

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

PYRAMID SERVICE CO., on behalf of itself and all other holders of unpaid short term obligations of the City of New York matured between December 11, 1975 through March 12, 1976

Plaintiff,

-against-

THE CITY OF NEW YORK,

Defendant.

Index No. 20245/75
(Action No. 1)

AFFIRMATION

Index No. 08578/76
(Action No. 2)
STATE OF NEW YORK

COUNTY OF NASSAU

William I. Niles, an attorney licensed to practice law in the State of New York, affirms under penalties of perjury:

1. I am the attorney for plaintiff in Action No. 2 and am fully familiar with all the facts and circumstances in said cause heretofore.

2. Action No. 1 was commenced by Flushing National Bank in the latter part of 1975, alleging: (1) that the Emergency Moratorium Act impairs contracts between the City and its note holders, thus violating Article I § 10 of the United States Constitution; (2) violates Article 8 of the State Constitution by refusal to adhere to the restrictions therein on borrowing and securing the City notes; (3) violates the same Article 8 of the State Constitution with respect to the limited time for redemption of City notes; (4) alleges that the Emergency Moratorium Act is in conflict with the Federal Bankruptcy Law in that it binds non-consenting creditors to a composition plan; (5) vio-
lates the Equal Protection Clause of the Fourteenth Amendment of the United States Constitution as it applies to City notes and not to City bonds; and for injunctive relief pending determination of the constitutionality of the Emergency Moratorium Act.

3. On 19 November 1976 the Court of Appeals of the State of New York declared the Emergency Moratorium Act unconstitutional, and on 8 February 1977 issued its Remittitum to this Court for further proceedings.

4. That by said Remittitum, this Court was directed, among other things, "to hear and determine with dispatch!"

"3. Whether, in any orders or judgment entered, the payment of interest on the principal of the municipal notes shall be directed at the face rate prior to maturity and at the rate of six percent as provided in Chapters 874 and 875 of the Laws of 1975 from the date of maturity to the date of payment."

"c. To entertain motions to intervene in or to consolidate into, and to accept referral motions to consolidate into this action any other proceeding or action heretofore or hereafter brought to enforce the payment of the municipal notes or for which provision is made in Paras. B(1) and B(2)."
5. That on 10 December 1976 the Amended and Supplemental Complaint in Action No. 2 was duly served upon the defendant in said action; a true copy of said pleading is hereto annexed as Exhibit "A" hereof.

6. That on 28 December 1976 defendant in Action No. 2 duly served its answer to said Amended and Supplemental Complaint; a true copy of said pleading is hereto annexed as Exhibit "B" hereof.

7. Action No. 2 was brought to procure judgment declaring that plaintiff therein, the holder of unpaid short term obligations of the City of New York, is entitled to earn interest thereon from their respective original maturity dates, at a rate or rates of interest determined in compliance with the "just compensation" and "due process" clauses of the Constitutions of the United States and of the State of New York; and that the Court hear and determine what interest rate or rates shall constitute such just compensation by the procedures mandated as constituting due process; and that the power and authority conferred upon the Court by CPLR § 907(5) be invoked to
substantively implement plaintiff's interests by its decree of installment payments to be made by defendant, in accordance with its financial capacity.

8. The thrust of Action No. 2 is directed at the same issue of the determination of interest rate as the attention of this Court is directed to by that portion of the Remittitur set forth at Paragraph 4 of this affirmation, and the questions of law and fact which shall be considered by the Court in effectuating the directions of the Remittitur are shared in common with the issues of Action No. 2. Thereby, it is respectfully submitted that consolidation is appropriate to avoid the injustice and anomaly that might arise from divergent determinations were Action No. 2 dealt with separately.

9. This motion is also directed to procure the Court's determination that it may be accorded class action status, and this motion is brought within the time prescribed therefor by CPLR §902. Affirmant believes that Action No. 1 has not been accorded class action status, and further believes that no motion therefor has been made by plaintiff in that action, and that the time statutorily limited for such motion has expired.
10. The persons constituting the class described in the Amended and Supplemental Complaint are the holders of approximately one billion dollars of short term obligations of the City of New York which matured between 11 December 1975 and 12 March 1976; they are numerous, are dispersed nationwide (if not world-wide) and their individual identities as holders of unregistered, negotiable securities, are not ascertainable. The consequence of the foregoing is that a requirement of notice to the members of the class, can require such expense as would render it impossible for a class action to proceed. A genuinely effective effort at notice to the class members, under the circumstances that prevail herein, would frustrate the effort to procure the benefits of class action status to the members of the said class.

11. There are questions of law and fact common to the class members which predominate over any question affecting only individual members of the class, in that all such class members have rejected exchange of their respective City notes for MAC
bonds, and were invalidly restrained by the Emergency Moratorium Act from the enforcement by lawful means, of payment of the principal obligations of their City notes on and after their respective due dates. All such City note holders, as a class, are similarly situated with respect to their right to earn interest from the maturity dates of their respective City notes in accordance with the "just compensation" clauses of the federal and state Constitutions and ascertained by procedure mandated by the "due process" clauses thereof. All such City note holders are similarly situated as a class, in the necessity that the collectibility of their City notes be preserved by reasonable accommodation to the defendant's ability to pay the increment of interest herein sought in their behalf, lest any precipitous requirement for the payment thereof, in addition to the principal, shall result in municipal disruption and impact detrimentally upon the collectibility of said City notes. The order of magnitude of the claim contemplated in procuring such "just compensation" for the note holders will be $10,000,000 per year for each one percent of additional interest which shall be held mandated as just compen-
sation to the note holders. Inasmuch a City obligations were yielding returns in the order of 15% per annum during the period of the moratorium, the interest increment over the 6% rate which the City has been paying on the notes, could mount to a sum of the order of $90,000,000 for each year since maturity of the notes in question.

Unique relief for the distress of the holders of the City notes, as a class, is available to them by declaration that this action may be conducted as a class action, and the invocation of the Court's powers pursuant to CPLR Rule 907(5), which such class action status would authorize. Consequently, the interest of individual class members in class action status is doubly significant, in that each note holder is injured in the same manner and seeks to vindicate the same right to just compensation while also benefitting from the substantive character of the relief from harsh economic and social consequences which class action status affords. The interest of the individual class members is not in any manner to be distinguished from plaintiff's own int-
erest in the outcome of the litigation.

12. The claim of the plaintiff in Action No. 2 herein is that the Emergency Moratorium Act invalidly restrained the plaintiff and the other note holders from access to legal redress for non-payment of the obligations, which imposition has effectuated both a deprivation to plaintiff of the use of its money, and an appropriation thereof to public use for the further municipal purposes of the City of New York; by virtue of which circumstances the federal and state Constitutions mandate that plaintiff be accorded just compensation for the appropriation and application of its funds, to be ascertained in accordance with plaintiff's constitutional right to due process and to equal protection under the law.

13. The plaintiff will fairly and adequately protect the interests of the class inasmuch a plaintiff has such a plain, direct and substantial interest in the outcome of this controversy identical to that of all the members of the class as to assure the adequacy of presentation of the issues involved.

14. A class action is superior to other methods for
the fair and efficient adjudication of the controversy set forth in the Amended and Supplemental Complaint in Action No. 2 herein, in that:

(a) the constitutional issues raised by the litigation will apply uniformly to all members of the class.

(b) The instant litigation is founded upon legal premises which are consistent with holding and Remittitur of the Court of Appeals in Action No. 1.

(c) any judicial review generated in the course of this litigation may be expeditiously pursued to conclusion.

(d) the Court shall thereby enjoy unique dominion to specify terms for payment of any judgment in accordance with the financial capacity of the defendant so as to avoid harsh economic and social consequences.

(e) the interests of smaller members of the proposed class shall be vindicated inasmuch as it would be impractical, inefficient and prohibitively expensive for such smaller class members to individually pursue their legal recourse herein.

(f) there is no instrumentality of government which will seek to redress the claims of members of the class.
15. Action No. 2 is not a mere duplication of any aspect of Action No. 1. While the amended complaint in Action No. 1 is framed as a class action, no motion has been made for authority that such action be prosecuted as a class action. Insofar as Action No. 1 adverts to the issue of the interest rate to be paid after the respective maturity dates of the notes, only paragraph "EIGHTEENTH" alleges any inadequacy as to interest, as follows:

"The City Note Moratorium Law is also unconstitutional under the impairment of obligations clause of the United States Constitution because it permits a reduction to 6% per annum the interest payable on the City notes during the approximate Three-year moratorium period, whereas, on information and belief, all the plaintiffs' City notes maturing on or before June 30, 1976 carry interest rates in excess of 6% and up to 9.50% per annum."

The foregoing allegation concerns itself with the provisions of the federal Constitution, Art. I § 10, Cl. 1 prohibiting any state from passing any law impairing the obligation of contracts. Inasmuch as the Court of Appeals, in declaring the invalidity of the Emergency Moratorium Law, did not invoke any federal constitutional principle, this Court is left to consider any and all applicable rules of law to the issue of interest rate.
While Action No. 1 appears to seek extrapolation of the applicability of the stated interest rate on each note to the period of time following its maturity, Action No. 2 seeks evaluation by judicial process of that interest rate which renders constitutional "just compensation" to the note holders. The rate or rates of interest thus to be ascertained may well be higher or lower than the rates specified on the face of the applicable notes. But popular knowledge of the state of the open market with respect to City securities during the recent crisis period, suggests that a substantial increment of interest is properly payable to the note holders, even in excess of the rates specified on the face of their respective notes. It is to vindicate that potential entitlement of the note holders for which Action No. 2 is brought.

16. It is respectfully submitted that consolidation of Action No. 2 with Action No. 1, as elsewhere in this motion sought, does not, pursuant to CPLR §906(1), impair its qualification for class action status; and the declaratory nature of the relief requested in Action No. 2 relieves the notice requirement of CPLR §904.
17. The claim of the plaintiff in Action No. 2 has particular relevance to the remaining issues of Action No. 1. The mandate of the Remittitur in Action No. 1:

(a) distinguishes the circumstances of "other holders of municipal notes, except institutional or corporate holders, purportedly subjected to the moratorium under Chapters 874 and 875 of the Laws of 1975 who were holders for value on Nov. 14, 1975, the effective date of the statute."

and,

(b) directs hearing and determination whether the payment of interest shall be directed "at the rate of six percent as provided in Chapters 874 and 875 of the Laws of 1975 from the date of maturity to the date of payment."

Plaintiff's claim in Action No. 2, it is respectfully submitted, lies within the parameters of this Court's considerations as directed by the Remittitur, inasmuch as:

(a) distinct recognition of the holders for value on the effective date of the moratorium statute, is consistent and compatible with the thrust of Action No. 2 that the funds of such holders were taken for public use by virtue of the denial to them of legal redress imposed by the moratorium statute, in consequence of which restraint the city was free to and did refuse to pay.
(b) this Court is directed to explore and determine what interest rate shall be payable after the original maturity dates of the notes.

The Court of Appeals has expressly recognized in its Remittitur that there are note holders whose rights are not dealt with therein. That posture is wholly consistent with recognition accorded to the concept that the enactment of the invalid moratorium statute constituted a taking of private property for public use, at least as against those who were note holders for value on the effective date of the statute.

For the foregoing reasons, affirnant respectfully urges that plaintiff's motion for consolidation and declaration of class action status for Action No. 2, be granted together with such other, further and different relief as the Court may deem proper in the premises.

Dated: Bethpage, New York
15 February 1977

William I. Niles
SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

PYRAMID SERVICE CO., on behalf of itself and all other holders of unpaid short term obligations of the City of New York matured between December 11, 1975 through March 12, 1976,

Plaintiffs,

-against-

THE CITY OF NEW YORK,

Defendant.

The plaintiff above named, by its attorney, William I. Niles, for its amended and supplemental complaint, alleges for itself and on behalf of all others similarly situated, as follows:

FOR A FIRST CAUSE OF ACTION

1. That plaintiff is and at all times hereinafter mentioned was a partnership existing under and by virtue of the laws of the State of Florida, having an office in that state in the County of Broward.

2. That at all times hereinafter mentioned, the

EXHIBIT "A"
defendant and still is a municipal corporation organized and existing pursuant to the laws of the State of New York.

3. That plaintiff is the owner and holder of certain short-term obligations issued by defendant which matured respectively between the 11th day of December, 1975 and the 12th day of March, 1976 which remain unpaid except as to the interest accrued to their respective maturity dates ("Notes").

4. That plaintiff has not voluntarily extended the due dates of its said Notes and has neither consented to, nor intends to consent to extension of the due dates of its said Notes.

5. That plaintiff brings this action on behalf of itself and all other holders of such unpaid Notes ("Holders").

6. That plaintiff intends to move this Court for an appropriate order pursuant to §902 C.P.L.R.

7. That heretofore the Legislature of the State of New York invalidly enacted the New York State Emergency Moratorium Act for the City of New York (L. 1975, Ch. 874 as amended, L. 1975, Ch. 875) ("Moratorium Act").

8. That the Moratorium Act, among other things, in-
validly imposed upon plaintiff and upon the Holders, restraint against their enforcement by lawful means, of payment of the principal obligations of said Notes on and after their respective due dates.

9. That each such Note was made upon the full faith and credit of the defendant, constituting its pledge to make full payment of principal and interest due on said Notes on the dates of their respective maturities.

10. That in consequence of the restraint so imposed upon plaintiff and the Holders, defendant thereupon availed itself of the opportunity thus afforded it by not paying the said Notes when due.

11. That by defendant's failure to make full and timely payment of the obligations of the said Notes, defendant thereby appropriated the funds due thereon to the plaintiff and to the Holders to its own municipal purposes.

12. That by virtue of the foregoing, the funds due to plaintiff and to the Holders, as aforesaid, was appropriated to further public use during the period commencing upon the respective due dates of said Notes and continuing through the
present to such future date when the sums owing on said Notes shall actually be paid ("Appropriation Period").

13. That the Constitutions of the State of New York and of the United States mandate payment of interest on the said Notes during the Appropriation Period at a rate determined in compliance with the "just compensation" and "due process" provisions thereof.

14. That neither the interest rates respectively provided upon the face of the respective Notes, nor legal interest, necessarily constitute such just compensation to the plaintiff and to the Holders during the Appropriation Period.

15. That it is properly and lawfully a judicial function, and is incumbent upon this Court, to:

   a) declare that payment of interest to the plaintiff and to the Holders constituting just compensation during the Appropriation Period, is mandated by the Constitutions of the State of New York and of the United States.

   b) ascertain by due process the rate or rates of interest which shall constitute such just compensation.
c) mandate payment of the consequent interest so determined to be due to plaintiff and the Holders.

FOR A SECOND CAUSE OF ACTION

16. Plaintiff repeats and realleges each and every allegation contained in the paragraphs of this complaint numbered '1', '2', '3', '4', '5', '6', '7', '8', '9', '10', '11' and '12' with the same force and effect as if herein fully set forth.

17. That defendant has failed and neglected to make provision as mandated by the Constitutions of the State of New York and of the United States, for the ascertainment and payment to plaintiff and to the Holders, of just compensation determined by due process for their property so appropriated; that the plaintiff and the Holders are entitled to relief from the failure and neglect of defendant as aforesaid.

18. That defendant has an enormous municipal debt, which if honored as portions thereof become due, exceeds the defendant's capacity to pay; any precipitous attempt to make such payment of principal will result in municipal disruption
and detrimentally impact upon defendant's ability to pay the Notes, and thereby upon the value of the Notes.

19. That the general public knowledge of such detrimental impact as aforesaid, and the prevailing uncertainty surrounding the prospective time and means for payment of the Notes, and the consequent prospect that defendant may resort to relief under the applicable Federal Bankruptcy statute, all aggregate to further undermine the value of the said Notes.

20. That the plaintiff and the Holders are entitled to be afforded remedy for their distress in the premises, whereby they shall be meaningfully benefitted in their right to payment allowing defendant no greater leeway than constitutional decency permits.

21. That it is in the best interests of the plaintiff and the Holders, that recourse be had in their behalf to the authority conferred upon this Court by R 907 C.P.L.R., to render judgment in favor of the plaintiff and of the Holders for all sums due them, including principal and interest as constitutionally mandated, and that payment thereof be made in in-
stalments in accordance with the financial capacity therefor of defendant, so as to avoid such harsh economic and social consequences upon defendant as would impact to the detriment of the ability and expectation of plaintiff and the Holders to receive full payment of sums due them.

22. That plaintiff and the Holders invoke the provisions of R 907 C.P.L.R. herein not as a mere adjective convenience to their redress, but as a substantive available remedy to the distress herein complained of; that judicial pronouncement of the right of plaintiff and of the Holders to be relieved of the restraint invalidly sought to be imposed by the Moratorium Act, does not serve to create the means for payment where it otherwise does not exist.

23. That further strenuous and valiant efforts by the defendant, and any prospective participation therein by the state and/or federal governments is speculative and conjectural, and subject to considerable delay in its implementation, all to the further prejudice of the interests of the plaintiff and of the Holders.

WHEREFORE, plaintiff demands judgment as follows:
A) As to the first cause of action:

i) Declaring first that during the Appropriation Period, plaintiff and the Holders shall be entitled to earn interest on the Notes sufficient to constitute just compensation as mandated by the Constitutions of the State of New York and of the United States, and

ii) Declaring that the Court shall hear, determine and adjudge the rate or rates of interest which shall afford plaintiff and the Holders such just compensation, and

iii) That the Court then duly hear, determine and adjudge the rate or rates of interest Thus due to the plaintiff and to the Holders, and

iv) That the plaintiff and the Holders then have judgment for the sums of money so determined to be due them.

B) As to the second cause of action:

i) Awarding to the plaintiff and to the Holders all sums due them under the Notes, including principal and interest as constitutionally mandated, and

ii) That the Court thereupon duly hear, determine and adjudge the manner and extent of installment payments to be made by defendant, in accordance with the financial capac-
ity therefor of defendant, so as to avoid such harsh economic and social consequences on defendant to the extent that such determination serves the best interests of the plaintiff and of the Holders, and judgment herein be rendered accordingly, and

C) As to both causes of action-

i) That the Court make such other and further declaration of the legal rights, relations and duties of the parties to this action, and grant such other and further relief as shall be necessary and proper in the premises, and

ii) That the plaintiff be awarded the costs and disbursements of this action, together with reasonable attorney's fees.

Dated: Bethpage, New York
December 3rd, 1976

WILLIAM I. NILES
Attorney for Plaintiff
4250 Hempstead Tpke,
Bethpage, N.Y. 11714
(516) 796-7000

To:- W. BERNARD RICHLAND
Corporation Counsel
Attorney for Defendant
Municipal Bldg.,
N. Y. C. 10007
SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

- - - - - - - - - - - - - - - - - - -

PYRAMID SERVICE CO., on behalf of itself and all other holders of unpaid short term obligations of The City of New York matured between December 11, 1975 through March 12, 1976, Plaintiff,

-against-

THE CITY OF NEW YORK,

Defendant.

- - - - - - - - - - - - - - - - - - -

Defendant, The City of New York, by its attorney, W. Bernard Richland, Corporation Counsel of the City of New York, for its answer to the amended and supplemental complaint (hereafter the "complaint") herein:

ANSWERING THE FIRST ALLEGED CAUSE OF ACTION

1. Denies that it has knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraphs 1, 3, 4, and 6 of the complaint.

2. Denies each and every allegation contained in paragraph 5 of the complaint except admits that plaintiff purports to bring this action on behalf of itself and certain other holders of City notes.

EXHIBIT "B"
3. Denies each and every allegation contained in paragraphs 7, 8, 9 and 10 of the complaint and refers the Court to the decision of the Court of Appeals of November 19, 1976 in Flushing National Bank v. Municipal Assistance Corporation et al., (N.Y.L.J., November 23, 1976, p. 5).

4. Denies each and every allegation contained in paragraphs 11, 12, 13, 14 and 15 of the complaint.

ANSWERING THE SECOND ALLEGED CAUSE OF ACTION

5. With respect to paragraph 16 of the complaint, repeats and reiterates, with the same force and effect as if fully repeated herein, its answers to paragraphs 1 through 12 of the complaint.

6. Denies each and every allegation contained in paragraphs 17 and 23 of the complaint.

7. Denies that it has knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 19 of the complaint.

8. Denies each and every allegation contained in paragraphs 20 and 21 of the complaint and refers the Court to the decision of the Court of Appeals in Flushing, supra and the proposed remittitur to be submitted by the City of New York in that case.
9. Denies each and every allegation contained in paragraph 22 of the complaint except admits that plaintiff purports to invoke the provisions of §907, CPLR.

FIRST DEFENSE

10. The complaint fails to state a claim upon which relief can be granted.

SECOND DEFENSE

11. The action may not be maintained as a class action pursuant to §§901, et seq., CPLR, Justice Fraiman having denied plaintiff's motion for class action status with respect to the original complaint herein in a decision reported in the New York Law Journal on November 4, 1976 at p. 4, cols. 2-3.

WHEREFORE, defendant The City of New York respectfully requests judgment dismissing the complaint and granting defendant the costs and disbursements of this action and such other and further relief as the Court deems just and proper.


Respectfully submitted,

W. BERNARD RICHLAND
Corporate Counsel
Attorney for Defendant
The City of New York
Office and P.O. Address
Municipal Building - Rm. 1656
New York, New York 10007
Tel. 566-5500
October 27, 1976

Eugene Keilin
Municipal Assistance Corporation
For The City of New York
Municipal Building
Room 4540
New York, New York

Dear Gene:

I enclose our first draft, as yet unreviewed by Judge Rifkind, of our "what happens if" memorandum on the consequences and possible courses of action following an adverse decision in the Flushing T case.

Please let me have your thoughts on this memo as soon as you and your colleagues have had an opportunity to review it.

Best regards.

Sincerely,

Allen L. Thomas

ALT: ps
Enclosure

HAND DELIVERY
MEMORANDUM

To Messrs. Felix G. Rohatyn
George D. Gould
Eugene Keilin

From Paul, Weiss, Rifkind, Wharton & Garrison

Subject: Possible Courses of Action in the Event of an Adverse Decision in Flushing II

You have asked us to outline the possible courses of action available to the Municipal Assistance Corporation For The City of New York (the "Corporation") and The City of New York (the "City") in the event the New York Court of Appeals renders a decision in Flushing National Bank v. The City of New York, et al. ("Flushing II") declaring the Moratorium Act unconstitutional. In addition, you have asked us to outline the effects of such a decision on the City's current financing arrangements.

I. Possible Adverse Decisions by the Court of Appeals

An adverse decision by the Court of Appeals declaring the Moratorium Act unconstitutional under the New York State Constitution could assume several forms, principally the following:

#1. an injunctive decree ordering immediate repayment of the outstanding short-term notes of the City subject to the Moratorium Act (the "City Notes");

We assume that any adverse decision by the Court of Appeals would be based, at least in part, on the State Constitution and would not be based solely upon the Federal Constitution.
#2. an injunctive decree setting forth an extended schedule for repayment of the City Notes;

#3. a remand to the State Supreme Court with instructions to fashion an appropriate schedule for the payment of the City Notes; or

#4. a decree purporting to compel payment, pursuant to Article 8, Section 2, ¶ 4 of the New York State Constitution, after five years from the issuance of the City Notes.

The likelihood of the Court of Appeals issuing an injunctive decree ordering immediate repayment of the City Notes (#1) is, in our view, remote. If there were no Moratorium Act, the vehicle for enforcement of the rights of holders of the City's obligations would have been a mandamus proceeding to compel payment. Historically, mandamus proceedings for the enforcement of municipal obligations have been controlled by equitable principles, involving consideration of the debtor's ability to pay and the needs of other persons dependent on the continuation of government services. The City and its citizens would have the right in such a proceeding to present evidence bearing on the condition of the City's Treasury and the repercussions that various payment schedules would entail. There is no apparent reason why invalidation of the Moratorium Act should leave the City in a worse position
than it would have been in had normal legal remedies prevailed from the start. Invalidation should mean no more than that the judiciary, rather than legislature, is the branch of government to be entrusted with the development of the appropriate remedy when a city is unable to pay its debt obligations when due.

The likelihood of the Court of Appeals issuing an injunctive decree setting forth an extended repayment schedule for the City Notes (#2) is also remote. Nothing in the record on appeal, as it now stands, would enable the Court of Appeals to balance the competing interests referred to above and fashion a repayment schedule for the City Notes in an informed manner.

The more likely possibility, in our view, is that the Court of Appeals would remand the case to the State Supreme Court with instructions to take evidence concerning the competing factors referred to above and to establish an appropriate repayment schedule for the City Notes, after taking into consideration such factors (#3).

It is also possible, but not probable, that the Court of Appeals would uphold the Moratorium Act under the State Constitution, but nevertheless state that the City Notes must be paid, pursuant to Article 8, Section 2, ¶ 4, within five years from their issuance (#4).

II. Possible Courses of Action

#1. If the Court of Appeals were to compel
immediate repayment of the City Notes, the following avenues would be open to the Corporation and the City:

a) There would be a period of 90 days in which to petition the Court of Appeals for reargument. Any such petition could be accompanied by a motion for a stay of all further proceedings pending reargument. Subject to a review of the actual opinion, we recommend that such a petition for reargument and motion for stay be filed promptly after the issuance of such an adverse opinion. We will prepare drafts of such papers to be ready in advance.

b) Under Article II, Title 6-A, of the Local Finance Law ("Title 6-A"), no proceeding to enforce the judgment could commence until appropriate notice was served upon the City Comptroller and 30 days expired thereafter without payment of the debt. During that 30 day period, the City, or the Emergency Financial Control Board, would have the perogative to petition the State Supreme Court for a further stay of proceedings. Under Title 6-A, such a petition would be predicated on a showing of the City's continued inability to pay its debts as they mature, and a statement of intent to file a

*/ However, in order to avoid an immediate event of default under the Federal Credit Agreement, such stay must be granted within 10 days after the date of the decision (see Section III of this Memorandum).
"repayment plan." Such a petition would automatically commence an additional 90 day stay, subject to statutory provisions for extension or curtailment by court order, and to judicial rulings on the constitutionality of Title 6-A. Should the constitutionality of Title 6-A be upheld -- which may be unlikely if the Moratorium Act fails to pass constitutional muster -- and a repayment plan approved by the courts, the stay then in effect could be extended for the time necessary to carry out the terms of such repayment plan. Despite the substantial adverse consequences of a Title 6-A proceeding on the City's current financing arrangements (see Section III of this Memorandum), we recommend that a Title 6-A proceeding be commenced if the Court of Appeals orders immediate payment and either denies a petition for reargument or reaffirms the original decision after reargument.

c) Were the usefulness of Title 6-A to cease, because of either the expiration of a stay period or an adjudication of unconstitutionality, recourse could be had only to Chapter IX of the Federal Bankruptcy Act (the "Bankruptcy Act"). A petition under the Bankruptcy Act, like Title 6-A, would
stay all proceedings to enforce the Court of Appeals judgment as well as the underlying obligations. Again, as with the use of Title 6-A, despite the substantial adverse consequences of a bankruptcy proceeding on the City's current financing arrangements (see Section III of this Memorandum), we recommend that such a proceeding be commenced if the Court of Appeals orders immediate payment and the usefulness of Title 6-A ceases.

d) Finally, if immediate payment of the City Notes were ordered, the City or the Corporation could seek Federal financial assistance, and might have to seek Federal assistance if any of the City's currently projected cash sources evaporated as a result of the utilization by the City of Title 6-A or the Bankruptcy Act (see Section III of this Memorandum).

#2. If the Court of Appeals were to establish a repayment schedule which was unsatisfactory to the City, the procedures set forth in Section II, #1 above could be utilized by the City to defer implementation of such an unsatisfactory repayment schedule.

#3. If the Court of Appeals were to remand the suit to the State Supreme Court to fashion an appro
priate payment schedule, no immediate action would be required. In such case the State Supreme Court would provide an adequate forum for the presentation of the City's case. A mandamus-like proceeding in the State Supreme Court, pursuant to such a judgment, could conceivably result in an acceptable schedule for the retirement of the City Notes. If the State Supreme Court were, however, to fashion an unacceptable repayment schedule, opportunities for appellate review would follow.

#4. In the event the Court of Appeals upheld the constitutionality of the Moratorium Act, but stated that the City Notes must be paid within five years from their date of issuance pursuant to Article 8, Section 2, ¶ 4 of the State Constitution, nothing need be done immediately. In such a case, however, no future exchange offers would be likely to be successful and, accordingly, alternative sources of financing the remaining City Notes subject to the Moratorium Act would have to be found.

III. Effects of an Adverse Decision on City Financing Arrangements

The most serious effects on the City's financing arrangements of a decision holding the Moratorium Act unconstitutional would be on the Federal Credit Agreement (the "Credit Agreement") and the Amended and Restated Agreement of November 26, 1975 (the "Amended and Restated Agreement") by and among certain New York Clearing House Banks (the "Banks"), City Pension Funds (the "Pension Funds") and City Sinking Funds.
1. The Credit Agreement. Under the Credit Agreement, the Secretary of the Treasury is authorized to lend the City up to $2.3 billion within each of the 1976-77 and 1977-78 fiscal years. Such loans are subject to conditions, chief of which is that the Secretary must determine "that there is a reasonable prospect of repayment of the loan in accordance with its terms and conditions."

If the Moratorium Act were declared unconstitutional, the Secretary would be far less likely to make the determination of a "reasonable prospect of repayment" and the Secretary, might, therefore, refuse to make additional loans. Furthermore, if the Moratorium Act were to be declared unconstitutional and such decision were not vacated, set aside or stayed within 10 days from the date thereof, an "event of default" under the Credit Agreement would occur. If an event of default occurs, the Secretary may, but is not required to, demand immediate and full repayment on all loans outstanding under the Credit Agreement. If a long-term repayment schedule were to be adopted by the lower court on remand from the Court of Appeals, the Secretary might waive the event of default (which he has the statutory power to do) and determine that there was still a "reasonable prospect of repayment" so that the federal seasonal loan program could continue.

In addition, the filing of a petition under Title 6-A or the Bankruptcy Act also constitute events of default.
Whether the Secretary would waive such an event of default and make the required determination would obviously depend on the facts surrounding the use of Title 6-A or the Bankruptcy Act.

Failure to repay any federal seasonal loan, or any interest thereon, is also an event of default and one that the Secretary probably would not or could not waive.

2. The Amended and Restated Agreement. The Banks and Pension Funds hold approximately $819 million of City Notes. Pursuant to the Amended and Restated Agreement, the Banks and Pension Funds have agreed to defer the payment in full of such City Notes until 1986, subject to equal annual reductions of outstanding principal from the "end of the moratorium period" to 1986 if, among other things, the City pays 6% interest on such City Notes. Under the Amended and Restated Agreement, if the City filed a petition under Title 6-A or the Bankruptcy Act, or failed to pay the required 6% interest on the City Notes following a declaration that the Moratorium Act was unconstitutional, the Banks and Pension Funds will be released from their obligations to defer payment on such City Notes and the Bank and Pension Fund held City Notes would be payable on the same basis as the publicly held City Notes.

Even if, as a result of a declaration that the Moratorium Act is unconstitutional, the City does not file Title 6-A or Bankruptcy Act petitions, it appears from
several clauses in the Amended and Restated Agreement (which may be subject to various interpretations) that the Banks and Pension Funds might be released from their obligations under the Amended and Restated Agreement to "roll-over" or keep outstanding until 1986 their City Notes.

Under the Amended and Restated Agreement, the Pension Funds are required to purchase $2.53 billion (of which $1.625 billion remains to be purchased) of the City's or the Corporation's bonds through the end of the 1977-78 fiscal year. If, after any declaration that the Moratorium Act is unconstitutional, the City filed a Title 6-A or Bankruptcy Act petition, or failed to pay the required 6% interest on City Notes, or failed to make further contributions to the Pension Funds as required, or failed to pay interest on outstanding City bonds, the Pension Funds would be released from their obligations under the Amended and Restated Agreement to make additional purchases of the City's or the Corporation's bonds. Finally, should an adverse ruling in Flushing II render the City unable to deliver to the Pension Funds an official statement regarding the City's financial position which is satisfactory to the Trustees of such Pension Funds, a strong argument could be made that the Pension Funds would be released from further obligations under the Amended and Restated Agreement.

P.W.R.W. & G.
MEMORANDUM

To Messrs. Felix G. Rohatyn
George D. Gould
Eugene Keilin

From Paul, Weiss, Rifkind, Wharton & Garrison

Subject
Possible Courses of Action in the Event of an Adverse Decision in Flushing II

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We assume that any adverse decision by the Court of Appeals would be based, at least in part, on the State Constitution and would not be based solely upon the Federal Constitution.
#2. an injunctive decree setting forth an extended schedule for repayment of the City Notes;

#3. a remand to the State Supreme Court with instructions to fashion an appropriate schedule for the payment of the City Notes; or

#4. a decree purporting to compel payment, pursuant to Article 8, Section 2, ¶ 4 of the New York State Constitution, after five years from the issuance of the City Notes.

The likelihood of the Court of Appeals issuing an injunctive decree ordering immediate repayment of the City Notes (#1) is, in our view, remote. If there were no Moratorium Act, the vehicle for enforcement of the rights of holders of the City's obligations would have been a mandamus proceeding to compel payment. Historically, mandamus proceedings for the enforcement of municipal obligations have been controlled by equitable principles, involving consideration of the debtor's ability to pay and the needs of other persons dependent on the continuation of government services. The City and its citizens would have the right in such a proceeding to present evidence bearing on the condition of the City's Treasury and the repercussions that various payment schedules would entail. There is no apparent reason why invalidation of the Moratorium Act should leave the City in a worse position
than it would have been in had normal legal remedies prevailed from the start. Invalidation should mean no more than that the judiciary, rather than legislature, is the branch of government to be entrusted with the development of the appropriate remedy when a city is unable to pay its debt obligations when due.

The likelihood of the Court of Appeals issuing an injunctive decree setting forth an extended repayment schedule for the City Notes (#2) is also remote. Nothing in the record on appeal, as it now stands, would enable the Court of Appeals to balance the competing interests referred to above and fashion a repayment schedule for the City Notes in an informed manner.

In our view, the more likely possibility in the event of an adverse decision, is that the Court of Appeals would remand the case to the State Supreme Court with instructions to take evidence concerning the competing factors referred to above and to establish an appropriate repayment schedule for the City Notes, after taking into consideration such factors (#3).

It is also possible, but not probable, that the Court of Appeals would uphold the Moratorium Act under the State Constitution, but nevertheless state that the City Notes must be paid, pursuant to Article 8, Section 2, ¶ 4, within five years from their issuance (#4).

II. Possible Courses of Action

#1. If the Court of Appeals were to compel
immediate repayment of the City Notes, the following avenues would be open to the Corporation and the City:

a) There would be a period of 90 days in which to petition the Court of Appeals for reargument. Any such petition could be accompanied by a motion for a stay of all further proceedings pending reargument. Subject to a review of the actual opinion, we recommend that such a petition for reargument and motion for stay be filed promptly after the issuance of such an adverse opinion. We will prepare drafts of such papers to be ready in advance.

b) Under Article II, Title 6-A, of the Local Finance Law ("Title 6-A"), no proceeding to enforce the judgment could commence until appropriate notice was served upon the City Comptroller and 30 days expired thereafter without payment of the debt. During that 30 day period, the City, or the Emergency Financial Control Board, would have the prerogative to petition the State Supreme Court for a further stay of proceedings. Under Title 6-A, such a petition would be predicated on a showing of the City's continued inability to pay its debts as they mature, and a statement of intent to file a

*// However, in order to avoid an immediate event of default under the Federal Credit Agreement, such stay must be granted within 10 days after the date of the decision (see Section III of this Memorandum).
"repayment plan." Such a petition would automatically commence an additional 90 day stay, subject to statutory provisions for extension or curtailment by court order, and to judicial rulings on the constitutionality of Title 6-A. Should the constitutionality of Title 6-A be upheld -- which may be unlikely if the Moratorium Act fails to pass constitutional muster -- and a repayment plan approved by the courts, the stay then in effect could be extended for the time necessary to carry out the terms of such repayment plan. Despite the substantial adverse consequences of a Title 6-A proceeding on the City's current financing arrangements (see Section III of this Memorandum), we recommend that a Title 6-A proceeding be commenced if the Court of Appeals orders immediate payment and either denies a petition for reargument or reaffirms the original decision after reargument.

c) Were the usefulness of Title 6-A to cease, because of either the expiration of a stay period or an adjudication of unconstitutionality, recourse could be had only to Chapter IX of the Federal Bankruptcy Act (the "Bankruptcy Act"). A petition under the Bankruptcy Act, like Title 6-A, would
stay all proceedings to enforce the Court of Appeals judgment as well as the underlying obligations. Again, as with the use of Title 6-A, despite the substantial adverse consequences of a bankruptcy proceeding on the City's current financing arrangements (see Section III of this Memorandum), we recommend that such a proceeding be commenced if the Court of Appeals orders immediate payment and the usefulness of Title 6-A ceases.

d) Finally, if immediate payment of the City Notes were ordered, the City or the Corporation could seek Federal financial assistance, and might have to seek Federal assistance if any of the City's currently projected cash sources evaporated as a result of the utilization by the City of Title 6-A or the Bankruptcy Act (see Section III of this Memorandum).

#2. If the Court of Appeals were to establish a repayment schedule which was unsatisfactory to the City, the procedures set forth in Section II, #1 above could be utilized by the City to defer implementation of such an unsatisfactory repayment schedule.

#3. If the Court of Appeals were to remand the suit to the State Supreme Court to fashion an appro-
priate payment schedule, no immediate action would be required. In such case the State Supreme Court would provide an adequate forum for the presentation of the City's case. A mandamus-like proceeding in the State Supreme Court, pursuant to such a judgment, could conceivably result in an acceptable schedule for the retirement of the City Notes. If the State Supreme Court were, however, to fashion an unacceptable repayment schedule, opportunities for appellate review would follow.

#4. In the event the Court of Appeals upheld the constitutionality of the Moratorium Act, but stated that the City Notes must be paid within five years from their date of issuance pursuant to Article 8, Section 2, ¶ 4 of the State Constitution, nothing need be done immediately. In such a case, however, no future exchange offers would be likely to be successful and, accordingly, alternative sources of financing the remaining City Notes subject to the Moratorium Act would have to be found.

III. Effects of an Adverse Decision on City Financing Arrangements

The most serious effects on the City's financing arrangements of a decision holding the Moratorium Act unconstitutional would be on the Federal Credit Agreement (the "Credit Agreement") and the Amended and Restated Agreement of November 26, 1975 (the "Amended and Restated Agreement") by and among certain New York Clearing House Banks (the "Banks"), City Pension Funds (the "Pension Funds") and City Sinking Funds.
1. **The Credit Agreement.** Under the Credit Agreement, the Secretary of the Treasury is authorized to lend the City up to $2.3 billion within each of the 1976-77 and 1977-78 fiscal years. Such loans are subject to conditions, chief of which is that the Secretary must determine "that there is a reasonable prospect of repayment of the loan in accordance with its terms and conditions." If the Moratorium Act were declared unconstitutional, the Secretary would be far less likely to make the determination of a "reasonable prospect of repayment" and the Secretary, might, therefore, refuse to make additional loans. Furthermore, if the Moratorium Act were to be declared unconstitutional and such decision were not vacated, set aside or stayed within 10 days from the date thereof, an "event of default" under the Credit Agreement would occur. If an event of default occurs, the Secretary may, but is not required to, demand immediate and full repayment on all loans outstanding under the Credit Agreement. If a long-term repayment schedule were to be adopted by the lower court on remand from the Court of Appeals, the Secretary might waive the event of default (which he has the statutory power to do) and determine that there was still a "reasonable prospect of repayment" so that the federal seasonal loan program could continue.

In addition, the filing of a petition under Title 6-A or the Bankruptcy Act also constitute events of default.
Mr. Felix G. Rohatyn  
Lazard, Freres & Co.  
1 Rockefeller Plaza  
New York, New York

Dear Felix:

As you have requested, I enclose our memorandum on the courses of action that might be followed in the event of an adverse decision by the Court of Appeals in the Moratorium case.

A draft of the memorandum has been reviewed and approved by Judge Rifkind and Gene Keilin.

I would appreciate your thoughts on this memorandum, which I will be happy to discuss with you.

Best regards.

Sincerely,

[Signature]

Alton L. Thomas

ALT:mp
Enclosure

BY HAND

cc: George D. Gould  
Eugene J. Keilin  

w/enclosure  
By Hand
Melvin L. Heineman, Esq.
Lazard, Freres & Co.
1 Rockefeller Plaza
New York, New York

Dear Mel:

As I mentioned to you over the telephone, I enclose the first draft, as yet unreviewed by Rifkind, Laufer or Thomas, of a response to Flushing's Post-Argument Submission in the Flushing II case.

We will be meeting to review and revise this draft beginning at about 10:00 o'clock tomorrow morning here in our office.

Best regards.

Sincerely,

Allen L. Thomas

ALT:mp
Enclosure
BY HAND

cc: Eugene J. Keilin, Esq./w/enclosure
By Hand
COURT OF APPEALS  
STATE OF NEW YORK  

FLUSHING NATIONAL BANK, etc.  

Plaintiffs-Appellants,  

against  

MUNICIPAL ASSISTANCE CORPORATION,  
et al.,  

Defendants-Respondents.  


ANSWERING SUBMISSION OF  
DEFENDANT-RESPONDENT FOR  
THE CITY OF NEW YORK  

Preliminary Statement

Appellant's "Post Argument Submission" reiterates the contention, first voiced in oral argument before this Court, that the Constitutionality of the Moratorium is not simply to be measured by rights accorded noteholders, as all parties had heretofore assumed, but that the notes in issue should be elevated to the status of municipal bonds, and accorded rights under Article VIII Section 2, which the Constitution expressly reserves for holders of such long-term obligations.

Appellant's submission is not only untimely, but is inconsistent with earlier positions taken by appellant in this very case. Thus, for example, at page 22 of
of its brief before the Appellate Division, appellant acknowledged that "the fourth paragraph of Section 2 of Article 8" - the same paragraph relied on here - "merely gives bondholders an additional remedy against the Comptroller if payment of their principal is not appropriated in the budget," and has no application to the instant case. (Emphasis supplied)

There and elsewhere (See, e.g., Appellant's Appellate Division Reply Br. at 45, Appellant's original Court of Appeals Br. at 60), appellant rightfully conceded, not only that this provision is inapplicable to City noteholders, but that it is a remedial clause of limited applicability, and not the "self-executing constitutional mandate", alleged in appellant's cover letter to Court of Appeals, dated September 13, 1976.*

The radically different position on which appellant now places its primary reliance is unsupported by constitution, case law, or constitutional convention records. It is a position which appellant attempts to justify solely on the basis of assumptions, plucked from the air, as to the intent of the

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* "Self-executing" mandate is one of a number of inappropriate labels applied by appellant to confuse and camouflage the true issues in this case. While Section 2 provides that the comptroller "shall" make certain appropriations, the imposition of a first lien, in the event of his failure, is left to the discretion of the Courts. As shown herein, application to the Court for the drastic relief permitted by Section 2 cannot be made for a period of five years from the date that notes, such as those issued, are issued. At that point should it be reached, it will be for the courts to weigh the extent of any continuing emergency and fashion an appropriate remedy. Such remedy, as Section 2 states, "may include a diversion of incoming revenues."
Constitution's draftsman. Scant attempt is made to reconcile appellant's assumptions with their finished product.

We return here to the Constitution itself, and first principles of Constitutional interpretation.

Article VIII Section 2 states that

Provision shall be made annually by appropriation by every . . . city, . . . for the payment of interest on all indebtedness and for the amounts required for (a) the amortization and redemption of term bonds, sinking fund bonds and serial bonds, (b) the redemption of certificates or other evidence of indebtedness (except those issued in anticipation of the collection of taxes or other revenues, or renewals thereof, and which are described in paragraph A of section five of this article and those issued in anticipation of the receipt of the proceeds of the sale of bonds theretofore authorized) contracted to be paid in such year out of the tax levy or other revenues applicable to a reduction thereof, and (c) the redemption of certificates or other evidence of indebtedness issued in anticipation of the collection of taxes or other revenues, or renewals thereof, which are not retired within five years after their date of original issue. If at any time the respective appropriating authorities shall fail to make such appropriations, a sufficient sum shall be set apart from the first revenues thereafter received and shall be applied to such purposes. The fiscal officer of any county, city, town, village or school district may be required to set apart and apply such revenues as aforesaid at the suit of any holder of obligations issued for any such indebtedness. (Emphasis supplied)

Section 5, pertaining to debt limit exclusions states that
"In ascertaining the power of a county, city, town or village to contract indebtedness, there shall be excluded:

A. Certificates or other evidences of indebtedness . . . issued for purposes other than the financing of capital improvements and contracted to be redeemed in one of the two fiscal years immediately succeeding the year of their issue, and certificates or other evidences of indebtedness issued in any fiscal year in anticipation of (a) the collection of taxes on real estate for amounts theretofore actually levied and uncollected or to be levied in such year and payable out of such taxes, (b) moneys receivable from the state which have theretofore been apportioned by the state or which are to be so apportioned within one year after their issue and (c) the collection of any other taxes due and payable or to become due and payable within one year or of other revenues to be received within one year after their issue; excepting any such certificates or other evidences of indebtedness or renewals thereof which are not retired within five years after their date of original issue.

Appellant does not ask the court to grant relief because of the "literal language" of these sections, but "despite" it. (App. Br. 8) This Court, we submit, should hesitate to extend the Constitution for the express purpose of dismantling an emergency legislative program.

I

NOTEHOLDERS COVERED BY THE MORATORIUM CONTRACTED FOR ANTICIPATION NOTES AND FOR NO OTHER OBLIGATION

Appellant suggests, inter alia, that the notes here in issue do not fall within the "anticipation note" exclusion of paragraph 4 because, in appellant's opinion, they were not issued in advance of "authentically anticipated"
income. No basis is offered for this contention which, at least as to the revenue and bond anticipation notes here in issue, cannot blindly be assumed. There is absolutely no evidence in the record that the City, at the time these notes were sold, did not anticipate a continued market for its bonds, or the receipt of state and federal aid, and other pertinent revenues, in excess of $1.2 billion, the principal amount of revenue anticipation notes covered by the Moratorium. Whatever the merits of appellants' assumption, however, its right to the requested relief does not logically follow as a matter of course.

Appellant, and members of its purported class, contracted to purchase nothing other than city notes, with the rights and limitations attendant thereto. They are entitled neither to more nor less than what they bargained for. If, as appellant maintains, the City overstated its anticipated income in connection with the sale of these notes, appellants' theory may well have justified injunctive relief barring their issuance. This was the question addressed by the Court of Appeals in Wein v. State of New York, 39 N.Y.2d 136 (1976). Conceivably, an action for damages based upon appellant's allegations, could be instituted today. But never, either in the commercial or government context, have purchasers of securities, alleged to have been issued fraudulently or ultra vires, been granted relief in the nature of conversion to other more senior obligations of the issuer. That such relief should be granted here, where
the inevitable effect would be to impair the security granted
bondholders, and the protection granted taxpayers, by Article VII
of the Constitution, simply does not follow from any authority
cited by appellant.

The thrust of appellant's argument fails on yet another ground. Even if sale of the notes in issue was a palpable abuse of constitutional restraints on borrowing, the constitution does not mandate a judicial resolution or penalty. To the contrary, the Constitution expressly states, in Article VIII, Section 12, that:

"It shall be the duty of the legislature, subject to the provisions of this constitution, to restrict the power of taxation, assessment, borrowing money, contracting indebtedness, and loaning the credit of counties, cities, towns and villages, so as to prevent abuses in taxation and assessments and in contracting of indebtedness by them." (Emphasis supplied)

This the legislature has done in the series of enactments of which the Moratorium Act is a part. Tight reins on taxation, spending and borrowing, imposed by the legislature, not only preclude the improper issuance of new debt, but afford current creditors the prospect of repayment in the shortest possible time. Dismantling this program by striking down its cornerstone can serve no constitutional goal.
NOTES WITHIN THE MORATORIUM RETAIN THEIR STATUS FOR THE CONSTITUTIONALLY PRESCRIBED FIVE-YEAR PERIOD

Appellant makes the further argument that the notes in issue automatically converted to the status of bonds, requiring an immediate appropriation, upon the alleged receipt of anticipated income, for the fiscal year of issuance. Again, nothing in Article VII supports the conclusion drawn from the alleged facts. To the contrary, the argument is wholly inconsistent with the language and history of Section 2.

Section 2 in specific and controlling terms, states that provision shall be made by appropriation for:

"(c) the redemption of certificates or other evidence of indebtedness issued in anticipation of the collection of taxes or other revenues, or renewals thereof, which are not retired within five years after their date of original issue. (Emphasis supplied)"

The five-year adjustment period permitted by the Constitution is absolute, and in no way dependent on the occurrence or continuation of tax delinquencies.

Nothing in the parenthetical exclusion of clause (b), or in Section 5A of Article VIII, alters this result, or could arguably have been intended to. As appellant correctly points out at page 10 of its submission, the five-year provision quoted above was a part of Section 2 before the parenthetical clause
of subdivision (b), or any reference to Section 5A, was inserted therein. Appellant goes on to state that the parenthetical clause in subdivision (b) "was merely a technical amendment which was not intended to make any substantive change" in Section 2.

If this is true, then the specific five-year provision of clause (c) must control, and appellant's argument, as applied to revenue anticipation notes, is at an end. Whether or not labeled a technical amendment, however, the inclusion of the parenthetical certainly gives appellant no greater rights than were previously awarded. The parenthetical provides in clear and simple terms that appropriation shall not be required for the redemption of notes:

"issued in anticipation of the collection of taxes or other revenues, or renewals thereof, and which are described in paragraph A of section five of this article and those issued in anticipation of the receipt of the proceeds of the sale of bonds theretofore authorized"

Standards set out in Section 5A, including allusions to uncollected taxes or revenues, are to be applied prospectively at the time of issuance. Nothing in the parenthetical indicates an intent to override clause (c), and, therefore, authorize a premature diversion of "first revenues", if anticipated income short of that required to preserve essential government services, is received within the five-year period. For such period at
least, the legislature may impose a solution which takes cognizance not only of the rights of creditors, but of the needs of those who depend on the allocation of scarce funds for their health, safety and welfare. Therefore, the equities are left to the courts.

Appellant attempts to escape the text of the Constitution by finding alleged flaws in its literal format. The flaws, however, reside in appellant's argument. We deal here with the major underlying fallacies.

1. Appellant contends that our interpretation of Section 2 would leave revenue anticipation notes without constitutional pledge of punctual payment, and would leave bond anticipation notes, "without any constitutional protection whatever." (Appellant's Submission at 2). This, of course, ignores the existence of other pertinent provisions of the state and federal constitutions, notably the federal contract clause. Every debt instrument, including revenue and bond anticipation notes, carries with it a contractual pledge of punctual payment, subject only to the implicit reservation of the emergency police power of the state. Clearly, this pledge is not subject to impairment, any more than other contractual obligations, in the "discretion of the state legislature." Section 2 paragraph 4 is not, therefore, the exclusive remedy of any creditor. It is, as appellant previously stated, an "additional remedy" for bondholders.*

* That such interpretation is consistent with the overall constitutional scheme is further demonstrated by reference to Article VII Section 16, the corresponding State Finance section from which Article VIII Section 2 was derived. Not only does Section 16 exclude notes issued in anticipation of taxes, revenues or bonds from its ambit, but it does so permanently, without any five year limitation. Despite this, investor confidence in the State of New York, based upon other constitutional guarantees, has long and consistently been attested to.
2. Appellant further contends that the parenthetical exclusion of Section 2, and presumably clause (c) as well, was intended to do no more than avert the necessity for a double appropriation of uncollected income -- one to meet obligations anticipated in the year of issuance, and a second to repay noteholders whose loans are applied to satisfy such obligations as they arise. Appellant's theory, based upon the tenuous assumption of a balanced budget, is that meeting ordinary obligations from the use of note proceeds will free a corresponding amount of income for repayment of the debt. Appellant then asserts that if such debt is carried over to the following year, with no commensurate carry-over of anticipated income, a new appropriation will be required to retire the debt. From this, through a leap of faith, appellant concludes that an appropriation must be made immediately, and that anticipation notes become "the functional equivalent of long term debt," as soon as the original anticipated income is consumed. (Submission at 6) The argument is plagued with two non sequiturs: (a) the assumption that because an appropriation must be made, it must be made immediately; and (b) the assumption that because deferred notes acquire, to a limited extent, the deferred payment aspect of bonds, they become the "functional" and constitutional equivalent of bonds in all respects. Neither assumption bears scrutiny.

Appellant's argument demonstrates no more than that an appropriation must ultimately be made, and sufficient taxes levied, to retire the debt. It does not establish that either
must be done as a matter of constitutional mandate in the fiscal year immediately following maturity. The omission to include such a requirement in the constitution is not mere oversight. With it would go the risk, evident here, of overwhelming a municipality with a sudden and unexpected burden, unlimited as to amount by any counterpart to the protective long term debt ceiling. The constitution thus recognizes the need to allow municipalities a reasonable time in which to adjust expenditures and restore its credit, as reflected in Section 2, paragraph 4, clauses b and c. That the interim effect may be to require satisfaction of the debt from a future year's tax levy or other income, affords no compelling reason for eliminating the five year adjustment period.

The correctness of our interpretation is supported by Levy v. McClellan, 196 N.Y. 178, 195 (1909), paradoxically cited by appellant at page 7 of its submission. There the issue was whether the City of New York could incur additional long term debt, or whether it had reached the constitutional ceiling. This turned on whether "revenue bonds" issued to meet expenses in 1908, and intended to be paid from taxes to be levied in the following fiscal year, had to be included in the computation. The Court of Appeals there ruled that those notes were constitutionally and logically indistinguishable from any other anticipation note. In the words of the Court:

* [Footnote, p. 12]
"They do not differ, in their temporary character, from other revenue bonds. They are issued in emergencies and provisionally. Instead of being in anticipation of the revenue for the year, in which issued, they are redeemable in the ensuing year under a special appropriation to be made. They should not be included in the computation. (Emphasis supplied)

Just as the one year deferral in Levy was not critical to classification of the note, the maximum postponement permitted by the Moratorium here does not trigger a constitutional reclassification. The constitution draws the line, plainly, at five years.

None of the remaining authorities cited by appellant, consisting of inapposite case law, disjointed historical references, and opinions of the Attorney General as to the meaning of unique state finance provisions in effect prior to the 1938 constitution revision, come closer to advancing appellant's cause.

In short, not only is it non "obvious" that the notes in issue should be deemed the equivalent of bonds for purposes of applying Article VII, Sections 2 and 5A, but, in fact, the opposite result appears to be the proper one.

The term "Revenue bonds" as appears in the opinion above was the predecessor of the term "revenue anticipation note" and does not imply long term bonded debt in the current parlance.
CONCLUSION

For all the reasons stated above, and in our main brief, the order of the Appellate Division, First Department, should be affirmed.

Dated: September 19, 1976

Respectfully submitted,

PAUL, WEISS, RIFKIND, WHARTON & GARRISON
Attorneys for Defendant-Respondent
Municipal Assistance Corporation
for the City of New York

Of Counsel:

Simon H. Rifkind
Robert L. Laufer
Howard S. Veisz
MEMORANDUM

To Herbert Elish

From Frederick R. Cummings
George S. Balis

Subject Municipal Assistance Corporation - Aid to Needy Holders of City Notes

You have asked us to outline our tentative conclusions with respect to the legal implications of a program by which MAC would make available some financial relief to needy holders of (1) publicly held short-term obligations of the City now subject to the Moratorium ("City Notes") and (2) MAC bonds issued in exchange for City Notes in one or both of the exchange offers.

Although there are various legal and practical problems inherent in the "Mercy MAC" program outlined in this memorandum, it is our tentative conclusion that MAC may legally carry out a program along the lines described below.

I. Proposed Program.

A Mercy MAC program might take one of many forms and many variables exist within any such program for determination, as a matter of policy, by the MAC Board. However, a program along the following lines, previously discussed with you and members of your staff, seems to raise the fewest legal and practical problems. The proposed program can be outlined as follows:

A. Summary.

MAC would offer to exchange its Bonds, which would have certain favorable terms, for City Notes or MAC Bonds held
by needy persons meeting certain predetermined criteria. The special "Mercy MAC Bonds" would be issued under the Second General Bond Resolution\(^1\) and would be Serial Bonds in the aggregate principal amount of the City Notes or MAC Bonds accepted in exchange. The Serial Bonds would be in relatively small denominations scheduled to mature semi-annually. An overall limit of $25,000,000 or $50,000,000 would be placed on the entire program. In addition, a limit would be placed on the aggregate amount of City Notes or MAC Bonds that could be exchanged by any one person. Financial tests would be established to determine eligibility for the exchange program and a mechanism to police eligibility would be put in place.

B. Source of Funding.

1. A source of funds must be identified from which MAC may pay Mercy MAC Bonds as they mature. For example, if the program is limited to $25,000,000 of Serial Bonds maturing semi-annually in equal amounts over five years, then, in addition to interest, MAC will need $2.5 million every six months over the life of the program. (Interest requirements, at 8% would be

\(^1\) By issuing Mercy MAC Bonds under the Second General Bond Resolution, the Corporation would make such Bonds basically similar to those issued in the Exchange Offers. We see no legal impediment, however, to issuing such Bonds under the First General Bond Resolution.
$1,000,000 for the first semi-annual payment and would reduce thereafter as principal is paid.) 2/ MAC may certify for these funds from its normal revenue stream, but this would reduce the amount of cash flowing to the City.

2. Two possible alternative sources of funds have been identified. First, proceeds of a "Mini-MAC" offering could be used, presumably with a back-up commitment from the Clearing House Banks to purchase the balance of the offering not purchased by the public. Second, proceeds of a sale of long-term MAC Bonds directly to the Clearing House Banks (and perhaps investment banks) could be used. Direct sales to the Banks would be committed to in advance, but would be coordinated with the maturity dates of the Mercy MAC Bonds. The Banks should have an interest in providing relief to unsophisticated, needy holders of City Notes, because in many cases they played an important role in marketing such City Notes at the time of their original issuance and, therefore, they should be willing to participate in the program.

3. On balance, we believe that direct Bank funding is preferable to Mini-MAC funding. Although MAC is committed to do Mini-MAC, MAC has suggested that this might not be an appropriate time for implementation of that program. Furthermore, it does not seem entirely appropriate to suggest that small investors fund what may be considered a "bail-out" of other small investors.

2/ The City is now paying interest on City Notes at the rate of 6% a year. Therefore, the only additional interest cost is the cost to the City of a higher interest rate on Mercy MAC Bonds.
Finally, certain of the legal arguments in support of the program may be strengthened by the argument that the funds for Mercy MAC are not available for any other purpose, as would be the case, presumably, if such funds came from the Banks. The Banks have indicated that they would purchase no new MAC Bonds, but might be willing to purchase these special purpose Bonds to fund Mercy MAC.

C. Terms of the Bonds.

1. A basic theme of the proposed program is that no person should receive cash immediately for the entire amount of his holdings. Rather, cash should be made available in limited amounts over a period of years to provide required living expenses. Accordingly, Serial Bonds would have to be issued in relatively small denominations. Term Bonds would require by-lot sinking funds which would not insure that any individual would receive cash (other than interest) at any specific time prior to ultimate maturity and would insure that some individuals would be paid off completely prior to ultimate maturity. Each is equally antithetical to the purpose of the program. We propose, therefore, that Serial Bonds be exchanged for a like principal amount of City Notes or MAC Bonds and that the Bonds so exchanged mature (serially) in equal amounts over the course of five years. Accordingly, someone exchanging a $10,000 City Note would receive MAC Bonds maturing $2,000 a year in each of five years. As an additional aid to the needy, maturities should be set semi-annually so that, in the above example, the person would receive $1,000 every six months.
2. We propose that the interest rate on the Mercy MAC Bonds be fixed at 8%, which is greater than the 6% Moratorium rate but equal to the interest on Exchange Offer Bonds.

3. We question whether Mercy MAC Bonds should be made non-transferable. We are not in a position to predict how the market would react to Bonds with terms such as those outlined. If such Bonds were to trade at or above par or at any price higher than first and second Exchange Offer Bonds, Mercy MAC Bondholders might be thought to have gained even more of an advantage over holders of MAC Exchange Offer Bonds than MAC intended to give them. Non-transferability would eliminate any such unintended advantage, but would add a complication which the Board might consider unnecessary or undesirable as a matter of policy.

D. Limitation on Amount.

1. Outstanding City Notes are in either $10,000 minimum denominations or $25,000 minimum denominations. (We understand, but have not yet confirmed, that only the BANs scheduled to mature on March 12, 1976 were issued in $10,000 denominations.)

2. We suggest, therefore, that a maximum amount of City Notes or MAC Bonds exchangeable by any one person be set at $25,000. Accordingly, one City Note issued in a minimum denomination of $25,000, two City Notes issued in minimum denominations of $10,000, or five MAC Bonds issued in minimum denominations
of $5,000, could be exchanged by any one person pursuant to the program.

E. Financial Tests.

1. Although we believe that strict financial tests should be established for eligibility for participation in the Mercy MAC program, e.g., maximum net worth, maximum annual income, maximum aggregate assets, we are not in a position to suggest what limits should be set. Constitutional requirements of due process and equal protection will mandate, however, that whatever standards are chosen be based on reasonable distinctions and designed to fairly accomplish the legitimate goals of the Mercy MAC program.

2. In addition, it will have to be decided whether the financial tests must be applied without exception or whether some group should be constituted to grant exceptions. Furthermore, it is possible that general rather than specific tests could be adopted and a group appointed to apply those standards on a case-by-case basis. If such a group is to be constituted, there will be a serious problem as to the delegability of the power to make such distinctions. This question is discussed elsewhere in this memorandum.

F. Acquisition Date Limitation.

In order to exclude speculators, even if they are needy, and to prevent transfers designed to take improper advantage of the program, we suggest that no one be eligible to exchange
unless he acquired his City Notes prior to an arbitrary chosen date. June 10, 1975, the date of MAC's creation, might be a reasonable cut-off date.

G. Application of Criteria.

Even if flexible criteria are not developed and no exceptions from specific criteria are to be permitted, somebody will have to be designated to determine whether the specific criteria are met. In addition, affidavits will have to be developed pursuant to which eligibility will be determined and documentation, such as original confirmation slips, cancelled checks, or whatever, will have to be made available to support such affidavits.

II. Legal Considerations.

A. Equitable Considerations.

1. General equitable principles require that in situations in which there is a doubt as to whether a municipality will be able to repay all of its obligations when due, it must apply any limited resources available for such a repayment pro rata to all holders of such obligations and may not prefer one holder to another. Thus, in Bankers Life Co. v. City of Little Field, Tex. 93 F.2d 152, 153, (5th Cir. 1937), Justice Holmes, sitting as Circuit Judge stated:
"It has been an invariable rule based upon equitable principles, that all persons in the same status, entitled to share in the distribution of a fund, are on a parity, entitled to a pro rata share of such funds as their interests may appear and no more . . . Equity knows no other basis."

Similarly, in Rising v. Hoffman, 116 Col.63, 179 Pac. 2d 430 (1947), the court held, under equitable principles, that upon insolvency of any funds available for the retirement of bonds must be held in trust for all bondholders:

". . . After the maturity date of the bond issue, all unpaid bonds are on a basis of equality, and, as to them, no priority or preference exists; but where the district is insolvent and thereby the funds on hand are insufficient to pay all of the outstanding matured bonds, then it becomes the duty of the town treasurer as a statutory trustee to pro rate the funds among all of the owners of the outstanding bonds." 179 Pac. 2d at 436.

We have not found any New York cases discussing the principal of pro rata distribution of available funds by a municipality when there are insufficient funds to pay all outstanding obligations. Our research indicates, however, that there are no States which have decided this question otherwise. For a further example of cases in which this principle is stated, see 171 ALR 1033 (1947). See also, 15 McQuillin, Municipal Corporations, § 43.127 (1970, Supp. 1975). We have no reason to

3/ Although the City is not insolvent, its position may be deemed comparable, to the extent that outstanding short-term notes have passed their stated maturity date and holders of short-term notes are not currently receiving payment of their principal.
believe that New York would adopt a contrary rule in a similar case.

2. This is not, however, such a case and, accordingly, it is our tentative conclusion that the equitable principles discussed above should not be applicable to the Mercy MAC program outlined herein. The distinguishing features of the Mercy MAC program are as follows:

(i) MAC is not the City or a City agency; it is a State agency. It will be MAC and not the City which will make non-pro rata distributions to holders of City Notes and MAC Bonds. Although moneys flowing to MAC from tax and per capita aid sources ultimately flow to the City if not used by MAC, the taxes are now State taxes and the per capita aid has been dedicated to MAC by State legislation. Accordingly, even to the extent that MAC uses its revenue sources ultimately to pay debt service on the Mercy MAC Bonds (or on bonds issued to the Banks to fund Mercy MAC sinking fund payments), it will be using State and not City revenue sources.

(ii) Under the program outlined herein, MAC would not be making any cash immediately available. The form of the transaction will be a bond-for-note exchange rather than cash payment for outstanding notes. The exchanged City Notes will remain outstanding in the hands of MAC.
(iii) No cash is "available" for pro rata payment to holders of outstanding City Notes. It is assumed that the Banks will be willing to buy MAC Bonds only if and to the extent that the proceeds of such sales are used to fund sinking fund obligations on Mercy MAC Bonds pursuant to this program. Accordingly, the equitable principle that "available" funds must be distributed pro rata is simply not applicable.

(iv) There is a reasonable and rational basis for the distinction between needy holders and other holders. This is substantially different from an arbitrary distinction based on date of issuance or serial number of the notes, which were the kinds of distinctions made in the equity cases described above.

3. Equitable principles can be superseded by legislation. Accordingly, a specific statute authorizing and directing MAC, as a State agency, to implement the Mercy MAC program would erase any lingering doubt as to the applicability of the equitable principle of pro rata distribution. Although it is our tentative conclusion that such legislation is not, as a matter of law, necessary, it may be appropriate as a political matter to seek legislation. If such legislation were forthcoming, it would, of course, strengthen the defense against a legal attack on the Mercy MAC program.
B. Constitutional Considerations.

Because MAC is a State agency, its actions in adopting and implementing a Mercy MAC program will have to pass the Constitutional tests of equal protection and due process.

1. The traditional equal protection test is whether the proposed discrimination or distinction is rationally related to a legitimate state concern. See, e.g., Railway Express Agency v. New York, 336 U.S. 106 (1949), in which a law forbidding all advertising on motor vehicles, except advertising of the owner's products, was upheld against Constitutional attack.

In recent years, a "new" equal protection test has developed in two types of cases: (i) those in which the basis of the distinction drawn by the State is "inherently suspect" either because of its tendency to disadvantage persons of a discernible and stigmatized status (e.g., classifications based on race, religion, alienage, legitimacy) or persons who are exercising federally protected rights (e.g., interstate travel); and (ii) those in which the effect of the distinction is to impair a "fundamental right" (e.g., procreation, voting, personal liberty). A State classification which either rests upon grounds "inherently suspect" or impairs a "fundamental right" will be sustained only if demonstrably necessary to promote a compelling State interest. The State bears a heavy burden of justification in such cases.
2. Against this legal background, the Mercy MAC program should be judged by the traditional test. The program will not impair any recognized equal protection "fundamental right." Although it is true that the Mercy MAC proposal involves a poverty/wealth distinction, poverty and wealth have been held not to constitute a "suspect classification." James v. Valtierra, 402 U.S. 137 (1971).

No rigid formula has been developed under the traditional test to determine whether a distinction is rationally related to a legitimate State concern. Many laws and State actions are in some respect unequal in form or in application. It is only arbitrary or invidious discrimination that the traditional equal protection clause prohibits.

Here, it is beyond question that the Mercy MAC program is aimed directly at a legitimate State concern: providing a modicum of financial relief, by using State funds, to a financially troubled group. If any authority for this proposition is required, it is notable that protective legislation based wholly upon age, economic need and the prevention of severe economic hardship has been sustained in city rent increase exemption laws, public assistance, social security, real estate tax subsidies and federal and state income tax
exemptions. See, e.g., Parrino v. Lindsay, 323 N.Y.S.2d 689, 692 (1971).

3. The guidelines for eligibility to participate in the Mercy MAC program must, however, reflect a rational attempt to draw a distinction between needy holders and other holders. Of course there will be some difficult line drawing, but so long as the criteria perform the function of identifying the needy bondholders, the Mercy MAC program will not be violative of equal protection principles.

4. The considerations that establish that the Mercy MAC proposal will not violate equal protection principles are equally applicable to the question whether the Mercy MAC proposal violates due process.

C. Delegation

1. A question may be raised as to whether MAC, without specific authorization by the State Legislature, has the power as a matter of Constitutional and administrative law to distinguish between "needy" and other holders of City Notes and MAC Bonds for the purpose of making available favorable Mercy MAC treatment. New York courts have traditionally sanctioned legislative programs which have entrusted significant responsibility to State boards, commissions and authorities. Indeed, it has been stated that constitutionally to confer discretion does not mean that:
"a precise or specific formula must be furnished in a field where flexibility and the adaptation of the legislative policy to infinitely variable conditions constitute the essence of the program..." Martin v. State Liquor Authority, 43 Misc. 2d 682, 686 (Sup. Ct. 1964), aff'd. 15 N.Y. 2d 707 (1965); See Gaynor v. Marohn, 268 N.Y. 417, 424 (1935).

Although fundamental questions of policy are not subject to delegation, broad agency discretion has been upheld where guided by relatively general legislative standards. As one court has stated:

"It is enough if the Legislature lays down 'an intelligible principle'..." Utica v. Water Pollution Control Board, 5 N.Y. 2d 164, 169 (1959).

2. Under these tests, MAC should have the authority to implement the Mercy MAC proposal without further State legislation. By legislative mandate, MAC is specifically empowered to assist the City to "[meet] its obligation to the holders of its outstanding securities." Section 3010 of the New York State Municipal Assistance Corporation Act (the "Act"). One specific means available to MAC is to exchange MAC bonds for City Notes, so long as the Board determines that the rights of the other note holders are not prejudiced by such exchange. (See Section 3035 of the Act.) This is a determination which, as discussed elsewhere herein, appears reasonable.

3. It would appear that the MAC Board has a significant degree of flexibility in determining how to administer the Mercy MAC program. In order to accomplish its legislative mandate of "assisting the municipality... [to meet] its obligations to the
holders of its outstanding securities." MAC is specifically authorized

"to do any act and all things necessary or convenient to carry out its purposes and exercise the powers expressly given and granted in this article or in the special act creating such municipal assistance corporation." Section 3010 of the Act.

4. The above analysis indicates that the MAC Board may itself, with whatever advice it chooses to acquire, develop and adopt specific eligibility guidelines for the program and may instruct its staff or others to perform the ministerial acts of implementation. If the MAC Board were to wish to delegate to another body the task of adopting guidelines or the power to grant significant exceptions to such guidelines, separate legislation to so empower such a body would probably be required.

D. Statutory Considerations.

1. A question might be raised regarding the power of MAC to use the proceeds of a sale of Bonds to Banks to pay principal and interest when due on Mercy MAC Bonds. Section 3012(1)(a) of the Act specifically empowers all municipal assistance corporations to issue bonds to provide sufficient funds for achieving
their corporate purposes. The exchange of Mercy MAC Bonds for City Notes pursuant to the Mercy MAC program is clearly within MAC's corporate purposes. This program can be instituted, however, only if funds are made available to finance the Mercy MAC debt service. The proceeds of the sale of Bonds to the Banks will provide that funding and, accordingly, will serve to insure the effectiveness of the Mercy MAC program. It is true that Section 3012(1)(a) states that "corporate purposes" includes making payments of interest on its notes and bonds, and that it does not list the making of payments on principal. But it is obvious from the language, however, that the list of certain purposes is by no means an exclusive one.

The First and Second General Bond Resolutions provide that the Corporation shall apply the proceeds derived from the sale of each series of Bonds as shall be specified in the Series Resolution authorizing such series. Assuming the Series Resolution authorizing the issuance of Bonds to the Banks will authorize that the proceeds of such sale be applied to the Mercy MAC debt service, there would be no legal obstacle to such application of the proceeds.

2. Section 3035(3)(b) of the Act requires that the Board of Directors of MAC shall determine that the terms of any proposed exchange of MAC Bonds for outstanding City Notes
"will not prejudice the rights of holders of other bonds and notes of the [C]ity."

The rights of the other noteholders should not be deemed to be affected, because the exchange will have no impact on the payment of principal of and interest on their notes. No funds otherwise available for payments to other noteholders are to be used in the Mercy MAC program described herein. The rights of the City bondholders would not be prejudiced, because the City is current in the payment of the principal of and interest on its outstanding bonds.
III. Applicability to Needy Holders of MAC Exchange Bonds.

A. Legal Analysis.

1. The power of MAC to exchange Mercy MAC Bonds for currently outstanding MAC Bonds held by Bondholders who are otherwise eligible for Mercy MAC participation is contained in Section 3012 of the Act. This section provides that MAC has the power "to refund any bonds by the issuance of new Bonds whether or not the bonds to be refunded have or have not matured." Under the proposal, this refunding would be accomplished by the issuance to the eligible MAC Bondholders of new Mercy MAC Bonds, pursuant to a new Series Resolution adopted pursuant to the Second General Bond Resolution.

2. Each of the Series 1 through 6 Resolutions provides that a fixed dollar amount must be applied to the retirement of outstanding Bonds (if not previously repurchased) in order to fulfill the sinking fund requirement in each year in which a sinking fund installment must be paid. The Bonds received by MAC in exchange from eligible Bondholders will not be deemed "outstanding" for purposes of the sinking fund call. Accordingly, the pool of Bonds against which such fixed dollar amounts may be

---

4/ The Second General Bond Resolution also contains provisions for the "refunding" of bonds by the issuance of new bonds. The type of "refunding" contemplated by the Resolution, however, would be either difficult or impossible to effectuate in the context of the Mercy MAC proposal.
applied will be reduced and the chance that a Bond held by a non-eligible Bondholder will be selected in the sinking fund lottery will be increased.

B. Conclusion.

1. Although we continue to consult with Bond Counsel to MAC on this point, we find no legal impediment to making the Mercy MAC program equally applicable to holders of MAC Bonds received in the first or second exchange offers if such holders otherwise meet the Mercy MAC eligibility standards.

2. In the second exchange offer Official Statement, which was issued after the Mercy MAC concept was first discussed by the press, after describing the concept in general terms, MAC stated:

"The Corporation has determined, however, that if it implements any such proposal, such proposal will be equally applicable to persons who have theretofore exchanged City Notes for bonds of the Corporation pursuant to this Exchange Offer, so that no person will be denied such an opportunity to be paid in cash by reason of such person's tender of City Notes pursuant to this Exchange Offer."

At the time, we thought that it would be legally impossible to make a Mercy MAC program available to holders of first Exchange Offer Bonds. Subsequent analysis and refinement of the proposed terms of the program have led us to the contrary conclusion.

*  *  *

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We will inform you promptly if our continuing research or consultations with Bond Counsel alters any of the conclusions expressed in this memorandum.

Please call us if you have any further questions or would like to discuss this memorandum with us.

ALT
FRC
GSB
PERSONAL AND UNOFFICIAL

Mr. Francis J. Barry
President
Circle Line Yachts, Inc.
Foot of West 43d Street
New York, New York 10036

Re: Flushing National Bank, etc.
v. Municipal Assistance Corp., etc.

Dear Frank:

I thought you might be interested in reading the enclosed opinion in the above-entitled matter.

Do you agree with the conclusion?

Best wishes to Marian and you.

Sincerely,

[Signature]

Myles J. Lane

Enclosure
SUPREME COURT, APPELLATE DIVISION
First Department, March 1976

Arthur Markewich, J.P.,
Vincent A. Lupiano,
Harold Birns,
Louis J. Capozzoli,
Myles J. Lane, JJ.

Flushing National Bank, on behalf of itself and all other holders of notes of the City of New York maturing on or before June 30, 1976,

Plaintiffs-Appellants,

against

Municipal Assistance Corporation for the City of New York; New York State Emergency Financial Control Board; The City of New York and Harrison J. Goldin, Comptroller of the City of New York,

Defendants-Respondents,

and

State of New York,

Defendant

Appeal from a judgment of the Supreme Court, New York County (Baer, J.), entered December 24, 1975, granting defendants' motion for summary judgment and denying plaintiffs' motion for a preliminary injunction.

Simon H. Rifkind of counsel (Robert L. Laufer, Dean B. Allison, Howard S. Veisz and Jonathan Siegfried with him on the brief; Paul, Weiss, Rifkind, Wharton & Garrison, attorneys) for respondent Municipal Assistance Corporation for the City of New York

Arthur Richenthal of counsel (Richenthal, Abrams & Moss, attorneys) for plaintiffs-appellants

W. Bernard Richland (James G. Grielsheimer, L. Kevin Sheridan, Leonard Koerner and James Griffin with him on the brief), Corporation Counsel for Municipal defendants-respondents

Shirley Adelson Siegel of counsel (Samuel A. Hirshowitz with her on the brief; Louis J. Lefkowitz, Attorney General) for defendant-respondent New York State Emergency Financial Control Board
No. 2127 -- Flushing National Bank v. Municipal Assistance Corp.

LANE, J.:

This action was brought, inter alia, to declare the invalidity of the "New York State Emergency Moratorium Act for the City of New York" (Chapters 874 and 875 of the Laws of 1975). The further injunctive relief sought has since been rendered academic and is not the subject of this appeal.

The Emergency Moratorium Act (EMA) provides for a conditional three-year moratorium on enforcement of outstanding short-term obligations of the City of New York. The short-term City obligations involved tax anticipation notes, bond anticipation notes, revenue anticipation notes, budget notes, and urban renewal notes.

The moratorium is conditioned upon an offer having been made to exchange the short-term obligations with a replacement obligation* having a date of maturity no more than 20 years after the date of maturity of the short-term obligation.

Should a short-term noteholder decline to accept the exchange offer, then payment on principal is to be suspended for a three-year period. Payment of interest thereon is provided at the rate stated in the obligation to the date of its maturity and thereafter at a rate of not

* Defined as "a bond, note or other evidence of indebtedness of the municipal assistance corporation for the city of New York . . ." (Ch. 874, § 2[4]).
less than 6% per annum. Interest payments are to be made at least annually. The City is not precluded from issuing other evidence of indebtedness to consenting shareholders in payment, renewal, or refunding of the short-term obligations.

The EMA legislation is alleged to be infirm in that it violates the Federal and State Constitutions. The plaintiff, Flushing National Bank, further urges that the 6% interest rate paid after maturity of the notes is confiscatory* and that the EMA violates the Federal Bankruptcy Act.

We must note at the outset that the EMA was not enacted by the Legislature arbitrarily or in a vacuum but is the latest in a series of legislative efforts to restore the City's financial integrity.

The first such special legislation, in June 1975, involved the creation of the Municipal Assistance Corporation (Laws of 1975, Chapter 168), which corporation was authorized to issue and sell its own bonds and notes and thereby to aid the City by purchasing City obligations or making direct payments to it.

This was followed by enactment of the New York State Financial Emergency Act in September 1975 (Laws of 1975, Chapters 868-870), which created a board to review, control and supervise the financial management of the City.

The present EMA (Laws of 1975, Chapters 874-875), enacted in November 1975, is the latest of such legislation.

* Flushing bases this claim on a comparison with interest paid on other short-term obligations of subdivisions of New York State.
In passing each item of legislation, there was a finding that the City was in need of assistance in order to maintain its essential services and financial stability, the failure of which would have grave impact Citywide and the ripples of which would be felt Statewide, and even nationwide.

The sense of urgency in these findings has become intensified as the fullness of the dimensions of the financial crisis made its impact on the Legislature.

The City's difficulties were first characterized as "cause [for] concern" (Laws of 1975, Chapter 168, § 3002), then resulted in the finding of "a financial emergency and an emergency period" (Laws of 1975, Chapter 868, § 1), and ripened into a finding that "the grave public emergency . . . has dramatically worsened" (Laws of 1975, Chapter 874, Section 1, Legislative Findings).

Each piece of remedial legislation enacted received great consideration, and the legislative findings published at the head of each act reveal that all involved were mindful of the dire consequences attendant upon a failure to ameliorate a fast deteriorating fiscal condition. The Legislature was similarly concerned with maintaining investor receptivity and respect for the pledge of the faith and credit of the City to payment of its obligations. Keeping this perspective in mind, it would appear that the EMA is not a "... Law impairing the Obligation of Contracts" violative of the United States Constitution (Art. 1, § 10).

Nothing in the EMA articulates an intent not to honor the obligation evidenced by the short-term obligations of the City, but it rather establishes a revised schedule
for payment of these obligations. Traditionally, there has been a distinction drawn between the obligation of a contract and the remedies available to enforce that obligation. Modification of a remedy can obtain without impairing the obligation of a contract (Sturges v. Crowninshield, 17 U.S. [4 Wheat.], 122, 200). It has also been noted that:

"It is competent for the States to change the form of the remedy, or to modify it otherwise, as they may see fit, provided no substantial right secured by the contract is thereby impaired. No attempt has been made to fix definitely the line between alterations of the remedy, which are to be deemed legitimate, and those which, under the form of modifying the remedy, impair substantial rights. Every case must be determined upon its own circumstances" (Von Hoffman v. City of Quincy, 71 U.S. [4 Wall.], 535, 553).

The reasonableness of the modification of the remedy must be left to the judgment and discretion of the Legislature, which discretion should not be disturbed absent palpable error (Antoni v. Greenhow, 107 U.S. 769, 775; East New York Savings Bank v. Hahn, 326 U.S. 230, 230-233).

The case at bar is dealing neither with a modification of remedy which gives no immediate payment to the creditor (W. B. Worthen Co. v. Thoman, 292 U.S. 426), nor with holders of obligations with a divesting of property rights (Wood v. Lovett, 313 U.S. 362) but, rather, with a mere extension of time to make full payment.

The EMA legislation has not rendered the short-term notes invalid, nor has it released or extinguished them. What it has done in the present financial emergency is afford a reason for the State's exercise of its inherent powers, which include the right to police and modify remedial

Absent such State powers, reasonably exercised, the viability of contracts, public or private, would be most tenuous. To deny a State a method of affording a modified remedy (e.g., via extension of time to pay) and simultaneously to allow rigid enforcement of those outstanding obligations would be to espouse a concept of every man for himself, which would be destructive of potential public resources and inimical to the survival of the State.

As Chief Justice Hughes so aptly stated in this regard:

"The policy of protecting contracts against impairment presupposes the maintenance of a government by virtue of which contractual relations are worth while,—a government which retains adequate authority to secure the peace and good order of society" (Home Bldg. & L. Assn. v. Blaisdell, 290 U.S. 398, 435).

The principles enunciated apply with equal vigor to both private and public obligations. With regard to the latter, it has been recognized that the principal asset of a governmental authority is its taxing power. As Justice Frankfurter so cogently noted in Faitoute Co. v. Asbury Park (316 U.S. 502, 509):

"An unsecured municipal security is . . . merely a draft on the good faith of a municipality in exercising its taxing power. The notion that a city has unlimited taxing power is, of course,
an illusion. A city cannot be taken over and operated for the benefit of its creditors, nor can its creditors take over the taxing power. Indeed, so far as the Federal Constitution is concerned, the taxing power of a municipality is not even within its own control -- it is wholly subordinate to the unrestrained power of the State over political subdivisions of its own creation. "A municipal corporation ... is a representative not only of the State, but is a portion of its governmental power ... The State may withdraw these local powers of government at pleasure, and may, through its legislature or other appointed channels, govern the local territory as it governs the State at large. It may enlarge or contract its powers or destroy its existence." United States v. Railroad Company, 17 Wall. 322, 329. And see Hunter v. Pittsburgh, 207 U.S. 161.

"In effect, therefore, the practical value of an unsecured claim against the city is inseparable from reliance upon the effectiveness of the city's taxing power."

He further noted:

"Impairment of an obligation means refusal to pay an honest debt; it does not mean contriving ways and means for paying it. The necessity compelled by unexpected financial conditions to modify an original arrangement for discharging a city's debt is implied in every such obligation for the very reason that thereby the obligation is discharged, not impaired."

The conclusion articulated in the Ashbury Park case is inescapable; namely:

"[S]tate intervention, carefully devised, worked out with scrupulous detail and with due regard to the interests of all the creditors, and scrutinized to that end by the state judiciary with the result that that which was a most depreciated claim of little value has, by the very scheme complained of, been saved and transmuted into substantial value. To call a law so beneficent in its consequences on behalf of the creditor who, having had so much restored to him, now insists on standing on the paper rights that were merely paper before this
resuscitating scheme, an impairment of the obligation of contract is indeed to make of the Constitution a code of lifeless forms instead of an enduring framework of government for a dynamic society."

As to the alleged violation of our New York State Constitution (Art. VIII, §§ 2, 10, 12), we merely note that the mandate of these sections has not been violated by the EMA legislation. The City has pledged its faith and credit for payment of its obligations and the City has not violated the strictures of §§ 10 and 12 relating to the City's power to levy real estate taxes.

As to the claim that the interest rate of 6% offered on matured notes is inadequate and confiscatory, it must be noted that this amount is double that available on any other judgment or accrued claim against the City (General Municipal Law, § 3-a). Furthermore, it must be remembered that the rate paid is for matured notes, while the comparisons made by Flushing are with interest rates offered on unmatured notes. As to the alleged violation of the Bankruptcy Act, it must merely be noted that we are dealing here with an extension of the time for payment of an indebtedness and not the "composition of indebtedness" encompassed by the Federal Bankruptcy Act.

In sum, we are concerned with that which Justice Frankfurter in a similar case described as

". . . the empiric process of legislation at its fairest: frequent reconsideration, intensive study of the consequences of what has been done, readjustment to changing conditions, and safeguarding the future on the basis of responsible forecasts" (East New York Savings Bank v. Hahn, 326 U.S. 230, 234-235).

Accordingly, the judgment of the Supreme Court, New York County, entered December 24, 1975, declaring Chapters 874 and 875 of the Laws of 1975 to be valid, should be affirmed without costs.

All concur

7
February 23, 1976

Dear Shirley and Jim:

Enclosed is the first draft of our proposed brief to the Appellate Division in the above matter. I welcome your comments as soon as possible.

As you will see, the brief is presently over 50 pages. We will make an attempt to cut it down, but may have to request the Court to permit us to serve an oversized brief.

I look forward to receiving drafts of your proposed briefs.

Sincerely,

Robert L. Laufer

Enclosure

cc: Daniel Goldberg, Esq.
To be argued by:

Simon H. Rifkind, Esq.

NEW YORK SUPREME COURT

Appellate Division - First Department

FLUSHING NATIONAL BANK, on behalf of itself and all other holders of notes of the City of New York maturing on or before June 30, 1976,

Plaintiff-Appellant,

-against-

MUNICIPAL ASSISTANCE CORPORATION FOR THE CITY OF NEW YORK; NEW YORK STATE EMERGENCY FINANCIAL CONTROL BOARD FOR THE CITY OF NEW YORK; THE CITY OF NEW YORK and HARRISON J. GOLDIN, Comptroller of the City of New York,

Defendants-Respondents,

-and-

STATE OF NEW YORK,

Defendant.

BRIEF OF RESPONDENT MUNICIPAL ASSISTANCE CORPORATION FOR THE CITY OF NEW YORK

PAUL, WEISS, RIFKIND, WHARTON & GARRISON
ATTORNEYS AND COUNSELLORS AT LAW
345 PARK AVENUE, NEW YORK, N.Y. 10022
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NEW YORK SUPREME COURT
Appellate Division - First Department

FLUSHING NATIONAL BANK, on behalf of itself and all other holders of notes of the City of New York maturing on or before June 30, 1976,

Plaintiff-Appellant,

-against-

MUNICIPAL ASSISTANCE CORPORATION FOR THE CITY OF NEW YORK; NEW YORK STATE EMERGENCY FINANCIAL CONTROL BOARD FOR THE CITY OF NEW YORK; THE CITY OF NEW YORK and HARRISON J. GOLDIN, Comptroller of the City of New York,

Defendants-Respondents,

-and-

STATE OF NEW YORK,

Defendant.

BRIEF OF RESPONDENT MUNICIPAL ASSISTANCE CORPORATION FOR THE CITY OF NEW YORK

Preliminary Statement

This is an appeal by plaintiff-appellant from a judgment of the Supreme Court of the State of New York, County of New York (Baer, J.), entered in the Office of the Clerk of the County of New York on December 24, 1975, granting summary judgment in favor of defendants-respondents and holding the New York State Emergency Moratorium Act for the City of New York (Chapter 874, as amended by Ch. 875, of the Laws of 1975) ("Moratorium Act") to be constitutional and not in violation of the United States Constitution, the New York State Constitution or the Federal Bankruptcy Act.
Question Presented

The sole question presented on this appeal is whether the Moratorium Act is a constitutional exercise of the inherent police power of the State to deal with the financial emergency facing the City and State of New York or whether, as claimed by appellant, the Act violates certain provisions of the United States Constitution, the New York State Constitution and the Federal Bankruptcy Act.

The Court below, in a lengthy and learned opinion, held the Moratorium Act to be constitutional.

Statement of the Case

This case involves an emergency exercise of the State's inherent police power, undertaken at an Extraordinary Session of the Legislature, in order to avert the financial collapse of New York City. Seeking to invalidate the Legislature's response to this crisis, appellant relies upon strident rhetoric, reckless and erroneous speculation about the City's future financial condition and theories of public finance and political science that bear little resemblance to reality. But no constitutional provision, State or Federal, no statute and no case law requires, as appellant suggests, that the State must let its greatest city die. To the contrary, all of the relevant authorities recognize the State's power to enact the Moratorium Act in order to save the City.

The Moratorium Act, far from being invalidated by the Federal or State Constitutions, statutes or case law, is all the more strengthened by them. For, as we shall show, the law as announced by every controlling Federal and State case dealing with
the issues presented here, and as summarized in the reasoned decision of the Court below, fully supports the view that the Moratorium Act is a valid exercise of the State's traditional police power, a measure well within the alternatives available to the Legislature to extricate the City of New York from its current financial crisis.

The City's Financial Crisis

Appellant fails to comprehend the simple proposition that, while an "emergency does not create power" on the part of the State, it "may furnish the occasion for the exercise" of existing power.* This is the case here.

The financial crisis presently facing New York City is one of unprecedented proportions. The problems of the City have been the subject of almost daily attention by municipal, State and Federal governmental leaders, and have made front-page news around the world. The record here is replete with evidence of the City's predicament -- massive lay-offs, wage freezes, closings of schools, hospitals, libraries, firehouses and police stations, cancellation of new construction, spiralling unemployment, Federal and State budgets which will further reduce cash flow to the City. (A149-66; RA16-17, 22, 33-58).**

Such diverse persons and entities as the Republican President of the United States, the Democratic-controlled Congress, Demo-

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**References to "A" are to pages of appellant's appendix. References to "RA" are to pages of respondents' joint appendix. References to "App. Br." are to pages of appellant's brief on this appeal.
ocratic and Republican State legislators, the New York City Council and the Democratic Mayor of the City of New York -- who rarely, if ever, concur on any issue -- all agree as to the existence and the colossal dimensions of the financial crisis in the City. Only appellant believes that no emergency exists, or at least not enough of an emergency to justify the exercise of the State's police power. Appellant's factual premises, we submit, are as erroneous as its legal analysis.

Previous Legislative Efforts

On two occasions prior to the passage of the Moratorium Act, the Legislature enacted special legislation intended to alleviate the dire situation in New York City. Unfortunately, neither of these early measures proved sufficient to deal with the problem.

First, on June 10, 1975, the Legislature enacted The Municipal Assistance Corporation for the City of New York Act. (L. 1975, ch. 196.) That legislation created the respondent Municipal Assistance Corporation for the City of New York ("MAC") and empowered it, among other things, to issue and sell its own bonds and notes and to render financial assistance to the City by purchasing City obligations or by making direct payments to the City to defray its expenses. (Pub. Auth. Law, §§ 3035, 3037.) However, the MAC legislation and MAC's subsequent efforts on the City's behalf were not alone a sufficient antidote for the City's financial distress. (A150-51, A157-58)

Secondly, therefore, on September 9, 1975, the Legislature met in Extraordinary Session and enacted the immediate predecessor to the Moratorium Act, the New York State Financial Emergency Act
for the City of New York ("Emergency Act"). (L. 1975, chs. 868, 869, 870.) The principal features of the Emergency Act were (1) the creation of a State controlled board -- the New York State Emergency Financial Control Board -- to review, control and supervise the financial management of the City (Emergency Act, § 5), and (2) a provision for the formulation by that Board, in cooperation with the City, of a three-year Financial Plan for the City, on the basis of which the City might balance its budget and return to sound financial condition. (Id., § 8.) The Legislature expressly found that the Emergency Act was necessary, because

"... a financial emergency ... exists in the City of New York [and] the city is unable to obtain the funds needed by the city to continue to provide essential services to its inhabitants or to meet its obligations to the holders of outstanding securities." (L. 1975, ch. 868, § 1.)

Thus, the Emergency Act was adopted

"... to bring the emergency under control ... to insure the continuity of governmental operations in the city and to provide the means by which the present emergency can in time be overcome [and] the city restored to financial health. ..." (Ibid.)

Once again, however, the Legislature's efforts, while a step in the right direction, were not enough to overcome the City's financial problems. Indeed, only two months after the passage of the Emergency Act, in November 1975, the Legislature found that the "grave public emergency" existing with respect to New York City "has dramatically worsened in the last two months." (A47)

It was in these circumstances that, on November 15, 1975, the Legislature, again in Extraordinary Session, enacted the Moratorium Act. In so doing, the Legislature found that there was

"... an imminent danger that the city of New York will be unable to pay its outstanding short-term indebtedness and even to provide those basic services essential to the
health, safety and welfare of its inhabitants and the continuation of orderly government in the city." (A47-48)

The Legislature's express purpose in enacting the Moratorium Act was

"... to ameliorate the disastrous consequences, to taxpayers, to holders of short term obligations and to city residents, of an inability by the city to meet its financial and governmental responsibilities in full ... and ... to avoid undue disruption of the process of financial recovery already underway, so as to facilitate restoration of the city's financial integrity and the payment of all its obligations." (A48)

With these legislative findings and purposes in mind, we turn now to the operative provisions of the Moratorium Act.

The Moratorium Act

The Act imposes a three-year moratorium on the enforcement of outstanding notes* of the City -- specifically in order "to avoid destructive actions during the time the city requires to regain its financial health." (A48) Nothing in the Act, however, precludes the City from paying its notes during the moratorium if it is financially able to do so.

To be more specific, the Moratorium Act provides that, during the "moratorium period", the enforcement of judgments and liens based upon any "short-term obligations" of the City, as well as the commencement or continuation of any actions upon such short-term obligations, shall be suspended, even though payment on such short-term obligations may be due according to their terms. (A50-51)

* City "notes", as distinguished from "bonds", are obligations with maturities of a year or less, while bonds have maturities that generally are substantially longer.
The Act defines the "moratorium period" as the period expiring three years from the effective date of the Moratorium Act -- November 15, 1975 -- unless shortened by subsequent act of the Legislature. (A48) The "short-term obligations" subject to the Act are tax anticipation notes ("TANS"), bond anticipation notes ("BANS"), revenue anticipation notes ("RANS"), budget notes and urban renewal notes ("URNS") issued by the City. (Ibid.)

The Act further provides that the moratorium shall be effective only as to those holders of City notes who (1) are offered an opportunity voluntarily to exchange their City notes for long-term MAC bonds in an equal principal amount* and (2) are paid interest on their City notes, as prescribed in the Act. (A51, 53) The Act prescribes, as a condition of the moratorium, that interest shall be paid to holders of City notes at the rate stated in the notes until their maturity. Thereafter, those noteholders who decline to exchange their City notes are to receive interest at an annual rate of at least 6%.** However, if a rate of interest higher than 6% is specified for the period after maturity in any agreement between the City and another noteholder or is held to be constitu-

* Pursuant to the terms of the Moratorium Act, MAC, on November 26, 1975, announced an offer to exchange its 8% bonds due July 1, 1986 for City notes. The Exchange Offer was made to all holders of City notes including the public, but not including the State, MAC, the 11 New York Clearing House Banks and certain City pension and sinking funds, who waived their right to participate in the exchange. The exchange offer was completed on December 29, 1975. A copy of MAC's Official Statement in connection with the exchange offer (hereinafter referred to as "Off. Stat.") was submitted to the Court below and will be submitted as a separate exhibit on this appeal.

** Compare General Municipal Law, § 3-a, providing for a rate of interest to be paid by the City of only 3% per annum "upon any judgment or accrued claim", which would include unpaid City notes.
tionally mandated, the Act requires that such higher rate of interest after maturity be paid to all holders of City notes covered by the moratorium. (A51, 53)

The Present Action

On November 17, 1975, just two days after the passage of the Moratorium Act, appellant commenced this action to declare the Act unconstitutional. (A30-42) Appellant purports to sue on behalf of all holders of City notes maturing on or prior to June 30, 1976 who do not accept the exchange offer. (A31) To date, however, no application to allow this action to proceed as a class action has been made. See CPLR 902. Accordingly, there is no way to tell at this point whether, in fact, appellant represents any interests other than its own in this action.

Decision of the Court Below

This matter was heard and determined below by Mr. Justice Harold Baer of the Supreme Court, New York County, upon motions and cross-motions by all parties seeking summary judgment. The Court granted respondents' motions, denied appellant's cross-motion, and declared the Moratorium Act to be valid and constitutional. In a careful and well-reasoned opinion, the Court rejected each of appellant's challenges to the Moratorium Act, holding that the Act was a legitimate exercise of the State's police power in response to a grave economic emergency confronting the City and State of New York.

First, the Court below held that the Moratorium Act does not violate the Contract Clause of the United States Constitution (Art. I, § 10). (A12-16) In so holding, the Court gave weight to
the finding of the Legislature that the state of emergency in New
York City compelled the exercise of the State's police power. (All)
It relied upon the numerous decisions of the United States Supreme
Court and the New York Court of Appeals sustaining legislation simi-
lar to the Moratorium Act in circumstances comparable to those
existing with respect to New York City.* (A12-16) Those precedents,
the Court concluded, firmly established

"... the power and duty of states to prevent the literal
enforcement of contractual terms in order to protect the
health, safety and welfare of their citizens." (A12)

The Court below also rejected appellant's challenge to the
Moratorium Act under Article 8, Sections 2, 10 and 12 of the New
York State Constitution. It found that the argument was based upon
misreading of those provisions and a misunderstanding of their appli-
cation to the City notes in question. (A17-18)

The Court below next disposed of appellant's claim that
the Moratorium Act conflicts with Section 83(i) of the Federal Bank-
ruptcy Act, which prohibits State legislation binding non-consenting
creditors to a "composition" plan. The Court concluded that the
Moratorium Act does not involve a "composition", but at most an "ex-
tension" of indebtedness, which is not proscribed by the Federal
Bankruptcy Act. (A18-19)

* Far from failing to cite "any of the applicable decisions", as
appellant claims (App. Br. 3-4), the Court below discussed or
cited in its opinion the seven most applicable decisions of
the United States Supreme Court and this State's Court of
Appeals interpreting the Contract Clause. (A12-16). Obvi-
ously, appellant's complaint is that the cases it offered were
not cited by the Court below -- and for good reason, since
they are all outdated or inapposite. See pp. 38-48, infra.
Finally, the Court below held that the application of the Moratorium Act to City notes but not to City bonds does not violate the Equal Protection Clause of the Federal or State Constitutions. It found the State Constitution "replete with differences in the rights of and obligations to bondholders and note holders" and concluded that the legislative distinction between notes and bonds for purposes of the Moratorium Act was reasonable under the circumstances.* (A19-20)

Some "Fundamental Errors" of Appellant

The Court below did not commit "fundamental errors", as appellant suggests. (App. Br. 3-6.) Rather, it is appellant that errs repeatedly throughout its brief, by misstating facts, mischaracterizing issues, misreading constitutional and statutory provisions, misinterpreting cases and generally distorting the matters before this Court. We deal here with only the most egregious of these distortions:

1. Appellant tries to create the impression that only $1.6 billion in City notes is outstanding, and that this amount was reduced to $1.142 billion by MAC's exchange offer. (App. Br. 6-7, 12, 15.) In fact, however, the City's debt involves not merely $1.142 or $1.6 billion, but nearly $5 billion in short-term City obligations. This was the principal amount of City notes that were outstanding on the effective date of the Moratorium Act, November 15,

* One claim advanced by appellant on this appeal -- that the Moratorium Act is an unconstitutional "taking" of appellant's property (App. Br. 34-37) -- is not alleged in appellant's complaint (A30-42) and was not raised below. Thus, as appellant concedes (App. Br. 1-2), the Court below did not treat this argument. Nevertheless, we deal with it in Point II, infra.
1975, and which were scheduled to mature within the 12 months between that date and November 10, 1976. Appellant would have this Court overlook the more than $3 billion in City notes held by the 11 New York Clearing House Banks, certain City pension and sinking funds, MAC and the State, which notes were also affected by the Moratorium Act. (A64, 166-68; Off. Stat. 3-4; RA58-60)

2. Appellant repeatedly states that the Moratorium Act effects a reduction in the interest that would otherwise be payable to City note holders. (App. Br. 2, 33-34, 37, 48-49.) But, General Municipal Law § 3-a -- the terms of which are impliedly a part of every note holder's contract -- limits the interest payable on a City note not redeemed at its maturity (whatever its face rate of interest) to 3% per annum. (See p. 7, supra.) Thus, rather than forcing a reduction in interest, the Moratorium Act increases the rate of interest payable to City note holders after the maturity of their notes. Appellant misleadingly compares the 6% interest to be paid on City notes after maturity, pursuant to the Moratorium Act, with the higher interest rates payable on the notes prior to maturity. The only fair comparison, however, is between the 6% post-maturity interest rate provided for in the Moratorium Act and the 3% interest rate that City note holders would otherwise be entitled to receive subsequent to maturity -- which is only 3%. (See pp. 53-54, 67-68, infra.)

3. Appellant makes the spurious suggestion that, if there were no Moratorium Act, or if the Act were declared uncon-
stitutional, the effect would "merely" be to "open the door of the
court to the noteholders", which would result in City noteholders
receiving prompt payment of their notes. (App. Br. 14-15.) To the
contrary, the unequivocal fact is that, in the absence of the Morato-
torium Act, which is designed to make possible payment to City note-
holders of (a) interest to maturity as provided in their notes, (b)
interest after maturity at 6% per annum, and (c) eventual repayment
of principal in full, City noteholders would not even receive the
interest due on their notes, much less repayment of principal. The
City, it is clear, cannot pay its notes now; the Financial Plan for
eliminating the City's operating deficit over the next three years
still makes no funds available for such payment (although the plan's
purpose is to restore the City's access to the market as a means
of repaying its notes); and the City has not received any commitment
from any other source, including the Federal Government, that would
enable it to make such payment. (App. Br. 12-13; A167-71; R16-17,
20-23; Off. Stat. 12-16.) None of these cold facts would change
if the Moratorium Act were held invalid. Rather, City noteholders
would then most likely be forced to assert their claims in a munici-
pal bankruptcy proceeding -- in which the noteholders could be ex-
pected to receive far less than full value for their notes. As for
appellant's suggestion (App. Br. 14) that "mandamus enforcement pro-
ceedings" brought by thousands of noteholders in the courts would
provide an easy remedy for the extraordinarily complex financial
problems facing the City, the best response was made almost 35 years
ago by Mr. Justice Frankfurter, in Faitoute Iron & Steel Co. v. City
of Asbury Park, 316 U.S. 502, 510 (1942):

"The experience of two modern periods of municipal
defaults . . . shows that the right to enforce claims
against the city through mandamus is the empty right to litigate."

Appellant, however, chooses to ignore the realities of the situation.

4. Assuming the role of self-styled expert on municipal finance, appellant cavalierly asserts that the City could easily raise the money needed to pay its maturing short-term indebtedness* by increasing the real estate tax, because "[t]he City's fiscal emergency does not involve its real estate tax base." (App. Br. 9-12.) But, appellant's assertion is squarely contradicted by the express findings of the Legislature: (a) that "a financial emergency" exists in the City; (b) that this emergency has "dramatically worsened"; (c) that there is "an imminent danger" that the City cannot pay its outstanding notes; (d) that, without the Moratorium Act, "all funds now available to the City will be exhausted" before the emergency situation can be corrected (emphasis supplied); (e) that, if unpaid holders of City obligations were to "seek judicial enforcement of their legal rights" -- i.e., to compel through mandamus the levy of additional real estate taxes, as appellant suggests (App. Br. 14) -- "the exodus from the City of corporate and individual taxpayers would increase, thereby . . . imposing a greater burden on the remaining taxpayers"; and (f) that "a conditional three-year moratorium on the enforcement of outstanding short-term obligations of the City" is essential "to avoid destructive actions during the time the City

* Part of appellant's problem is that it grossly understimates the principal amount of the City's current short-term indebtedness as being $1.42 billion (App. Br. 12) when, in fact, it is $2.9 billion, exclusive of City notes held by MAC, which totalled $1.858 billion on November 15, 1975, the date the Moratorium Act was enacted, and $2.2 billion now. (Al66-68)

Under the circumstances, appellant's assertion that there is
requires to regain its financial health." (A47-48; L. 1975, ch. 868, § 1.)

These legislative findings amply demonstrate the existence of a total emergency situation in the City and, we submit, are entitled to the greatest weight -- notwithstanding appellant's assertions to the contrary.* (App. Br. 9-12.) Unlike appellant, the Legislature recognized the truth in these times of the following observation by Mr. Justice Frankfurter in Faitoute Iron & Steel Co. v. City of Asbury Park, 316 U.S. 502, 509 (1942), supra:

"The principal asset of a municipality is its taxing power and that, unlike an asset of a private corporation, can not be available for distribution. An unsecured municipal security is therefore merely a draft on the good faith of a municipality in exercising its taxing power. The notion that a city has unlimited taxing powers is, of course, an illusion. A city cannot be taken over and operated for the benefit of its creditors, nor can its creditors take over the taxing power. Indeed, so far as the Federal Constitution is concerned, the taxing power

* Indeed, the Legislature's wisdom -- and appellant's ignorance -- in regard to the true condition of the City's real estate tax base is proven by a recent report issued by the City, projecting that due to the virtual halt of new construction and the continuing abandonment of property, the total value of the City's taxable real estate will decline this year for the first time in 33 years. See N.Y. Times, Feb. 3, 1975, p. 1, col. 4. As a result, just to maintain the present level of real estate tax revenues, the City's real estate tax rate, which has risen each year since 1967, will have to rise again this year to compensate for the declining real estate values. Ibid.; N.Y. Times, Jan. 15, 1976, p. 1, col. 4. It is predicted that such a tax rise will inescapably lead, among other things, to a rise in rents in rent-controlled and rent-stabilized apartments, further abandonment of property and an increased loss of business and industry by the City. Ibid.; N.Y. Times, Feb. 8, 1975, Sec. 8, p. 1, cols. 1-5. A loss in City residents is also forecast. See N.Y. Times, Feb. 23, 1976, p. 1, cols. 1-2. Understandably, these facts have led to a warning against a further increase in the City's real estate taxes. See Editorial, N.Y. Times, Feb. 9, 1976, p. 26, col. 2.

Under the circumstances, appellant's assertion that there is "no emergency or crisis situation with respect to the real estate tax base of the City" is truly incredible. (App. Br. 9.)
of a municipality is not even within its own control --

it is wholly subordinate to the unrestrained power of
the State over political subdivisions of its own creation.

* * *

"The intervention of the State in the fiscal affairs of
its cities is plainly an exercise of its essential reserve
power to protect the vital interests of its people by sus-
taining the public credit and maintaining local government.
The payment of the creditors was the end to be obtained,
but it could be maintained only by saving the resources of
the municipality -- the goose which lays its golden eggs,
namely, the taxes which alone can meet the outstanding
claims." (316 U.S. at 509, 512; emphasis supplied.)

In other words, as the Supreme Court recognized in Faitoutte, there
comes a point, irrespective of statute or regulation, where taxpayers
cannot or will not pay more. The conclusion that such point has al-
ready been reached in the City is implicit in the legislative find-
ings accompanying the Moratorium Act. Appellant suggests no valid
reason for supplanting that legislative judgment.*

*In any event, appellant's discussion of the City's real estate taxes
reveals its lack of familiarity with the subject. (App. Br. 11-12.)
Appellant fails to take into account that its proposed tax increase
-- assuming such increase could be collected without destroying the
City's tax base -- would seriously impair the City's operating budget.
Thus, Article 8, § 10 of the State Constitution and Article 12A of
the Real Property Tax Law limit the amount that the City can raise
through real estate taxes to pay its operating expenses to an amount
equal to 2-1/2% of the average full valuation of City real estate
for the preceding five years less the amount raised through real
estate taxes to service its short-term indebtedness (other than
11), the constitutional limit on the amount that the City can now
raise through real estate taxes to pay its operating expenses is
$1.858 billion (i.e., 2-1/2% x the average full valuation of City
real estate from 1971-76) less whatever real estate tax proceeds it
uses to pay its aforesaid short-term indebtedness. Accordingly, the
City cannot raise through real estate taxes the amount necessary to
redeem its outstanding short-term indebtedness -- which totals more
than $1.858 billion exclusive of BANS -- without totally absorbing
the real estate taxes available to meet the City's operating budget
-- a budget which the Legislature has determined cannot sustain fur-
ther significant cuts beyond those required by the City's three-year
Financial Plan. (A47-48; L. 1975, ch. 868, § 1.)
5. Appellant contends that the Moratorium Act is the "same" as legislation prohibiting the City from using its real estate tax proceeds to pay its notes. (App. Br. 6.) The truth is otherwise. Nothing in the Moratorium Act precludes the City from paying its notes during the moratorium if it is financially able to do so. Nor does anything in the Act withdraw any right or power of the City to tax its real estate or to use the proceeds in any proper way. Decisions as to what is to be taxed, at what rates and for what purposes (within constitutional limits, of course), are left where they belong -- with the City and the State Legislature -- and are completely unaffected by the Moratorium Act. (See pp. 56-58, infra.) Far from prohibiting payment of the City notes, the Moratorium Act is an essential component of a program designed -- after lesser measures proved insufficient -- to enable the City ultimately to pay its noteholders. (A48, 153-54)

6. Appellant, throughout the pre-argument portion of its brief, repeatedly makes the sweeping assertion that certain "explicit" State constitutional "guarantees" which were "embodied in the noteholder's contract with the City" have been violated by the Moratorium Act. (App. Br. 4, 5, 6, 7-9, 17.) But, when one reads the relevant State constitutional provisions (see pp. 18-19, infra) and the noteholders' "contract" (A92-106), it becomes readily apparent that certain of these alleged State constitutional "guarantees" do not exist at all; that appellant has misconstrued those that do exist; and that no applicable State constitutional provision or "guarantee" has been violated by the Moratorium Act. (See pp. 54-60, infra).

7. Finally, appellant lectures us on the principles of
"constitutional adjudication", relying upon references to the Bicentennial and Watergate, hearsay speculations from the president of Standard and Poor's, and a citation to Sgaglione v. Levitt, 37 N.Y.2d 507 (1975). (App. Br. 14-18.) But, appellant's rhetoric and extra-record quotations are irrelevant, and the Sgaglione decision does not advance its cause.

The Sgaglione case involved neither the Contract Clause nor any of the State constitutional provisions relied upon by appellant here. Rather, it dealt solely with the unique State constitutional provision applicable to pension benefits. (N.Y.S. Const., Art. 5, § 7.) Indeed, the Sgaglione decision supports the constitutionality of the Moratorium Act, for the Court of Appeals there recognized

"... the dire financial condition of the City of New York, which has been found to be not only a threat to the welfare of the metropolis, but also to the State, if not indeed to the Nation, of which it is a part." (37 N.Y.2d at 511.)

Moreover, in Sgaglione, the Court of Appeals found "the problem ... novel and close precedents nonexistent" (37 N.Y.2d at 511). On the other hand, the Moratorium Act, as we shall show, is squarely supported by authoritative interpretations of the Contract Clause by the United States Supreme Court and the New York Court of Appeals in numerous moratorium cases and other relevant precedents, and by the fact that no court has ever found the New York State Constitution to be an obstacle to legislation of this nature. (See pp. 20-21, infra.)

Constitutional and Statutory Provisions Involved in this Appeal

The full text of the Moratorium Act is reproduced in appellant's appendix. (A46-53)
The constitutional provisions relied upon by appellant in challenging the Moratorium Act are as follows:

U.S. Const., Art. I, § 10, Cl. 1:

"No State shall . . . pass any . . . law impairing the obligation of contracts . . . ."

U.S. Const., Amdt. V:

". . . [N]or shall private property be taken for public use, without just compensation."

U.S. Const., Amdt. XIV, § 1:

"No State shall . . . deprive any person of . . . property, without due process of law . . . ."

N.Y.S. Const., Art. I, § 7, Cl. (a):

"Private property shall not be taken for public use without just compensation."

N.Y.S. Const., Art. 8, § 2, ¶ 2, Cl. 1:

"No indebtedness shall be contracted by any . . . city . . . unless such . . . city . . . shall have pledged its faith and credit for the payment of the principal thereof and the interest thereon."

N.Y.S. Const., Art. 8, § 2, ¶ 2, Cl. 2:

"Except for indebtedness contracted in anticipation of the collection of taxes actually levied and uncollected or to be levied for the year when such indebtedness is contracted and indebtedness contracted to be paid in one of the two fiscal years immediately succeeding the fiscal year in which such indebtedness was contracted, all such indebtedness and each portion thereof from time to time contracted, including any refunding thereof, shall be paid in annual installments, the first of which, except in the case of refunding of indebtedness heretofore contracted, shall be paid not more than two years after such indebtedness or portion thereof shall have been contracted, and no installment, except in the case of refunding of indebtedness heretofore contracted, shall be more than fifty per centum in excess of the smallest prior installment."
N.Y.S. Const., Art. 8, § 2, ¶ 4:

"Provision shall be made annually by appropriation by every . . . city . . . for the payment of interest on all indebtedness and for the amounts required for (a) the amortization and redemption of term bonds, sinking fund bonds and serial bonds, (b) the redemption of certificates or other evidence of indebtedness (except those issued in anticipation of the collection of taxes or other revenues . . . and those issued in anticipation of the receipt of the proceeds of the sale of bonds theretofore authorized) contracted to be paid in such year out of the tax levy or other revenues applicable to a reduction thereof, and (c) the redemption of certificates or other evidence of indebtedness issued in anticipation of the collection of taxes or other revenues, or renewals thereof, which are not retired within five years after their date of original issue. If at any time the respective appropriating authorities shall fail to make such appropriations, a sufficient sum shall be set apart from the first revenues thereafter received and shall be applied to such purposes. The fiscal officer of any . . . city . . . may be required to set apart and apply such revenues as aforesaid at the suit of any holder of obligations issued for any such indebtedness."

N.Y.S. Const., Art. 8, § 10, ¶ 1:

[Limitations on amount to be raised by real estate taxes for local purposes; exceptions]

"Hereafter, in any . . . city . . . the amount to be raised by tax on real estate in any fiscal year, in addition to providing for the interest on and the principal of all indebtedness, shall not exceed an amount equal to [2-1/2%] . . . of the average full valuation of taxable real estate of such . . . city . . . less the amount to be raised by tax on real estate in such year for the payment of the interest on and redemption of certificates or other evidence of indebtedness. . . ."

N.Y.S. Const., Art. 8, § 12:

"The legislature shall not . . . restrict the power [of any city] to levy taxes on real estate for the payment of interest on or principal of indebtedness theretofore contracted."

U.S. Const., Amdt. XIV, § 1:

"No State shall . . . deny to any person within its jurisdiction the equal protection of the laws."
N.Y.S. Const., Art. 1, § 11:

"No person shall be denied the equal protection of the laws of this State or any subdivision thereof."

U.S. Const., Art. I, § 8, Cl. 4:

"The Congress shall have the power . . . to establish . . . uniform laws on the subject of bankruptcies throughout the United States."

Federal Bankruptcy Act, § 83(i) (11 U.S.C. § 403(i)):

". . . No State law prescribing a method of composition of indebtedness of [municipalities] . . . shall be binding upon any creditor who does not consent to such composition, and no judgment shall be entered under such state law which would bind a creditor to such composition without his consent."

Argument

I.

THE MORATORIUM ACT DOES NOT VIOLATE THE CONTRACT CLAUSE OF THE UNITED STATES CONSTITUTION

Appellant's main argument against the Moratorium Act (App. Br. 19-34) is based upon the Contract Clause of the United States Constitution. (Art. I, § 10, see p. 18, supra.)

However, as the Court below correctly concluded (Al2-16), appellant's argument misconstrues the Contract Clause and ignores the long line of authorities of the United States Supreme Court and this State's Court of Appeals expressly upholding State legislation similar to the Moratorium Act as an appropriate exercise of the State's police power, despite the appearance of interference with contracts, both public and private. Appellant also overlooks the underlying state of emergency in New York City which precipitated the enactment of the Moratorium Act, and fails to recognize -- as
the courts have -- that statutes such as the Moratorium Act, when appropriately invoked, do not "impair" contracts, but are valid legislative efforts to enable a municipality to honor its contracts.

In short, the Contract Clause provides no bar to the enactment of the Moratorium Act.

A. The Moratorium Act is a Valid Exercise of the State's Police Power

Numerous decisions of the highest Federal and State courts long ago repudiated the notion -- which appellant here espouses -- that the Contract Clause presents a rigid bar to the protection of vital public interests. The decisions recognize that every contract, public or private, implicitly reserves to the State the essential attributes of sovereign power to protect the health, safety or welfare of its citizens, which is the State's paramount duty. See e.g., Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398 (1934), supra; East New York Sav. Bank v. Hahn, 326 U.S. 230 (1945), aff'g 293 N.Y. 622 (1944); Faitoute Iron & Steel Co. v. City of Asbury Park, 316 U.S. 502 (1942), supra; City of El Paso v. Simmons, 379 U.S. 497 (1965); Klinke v. Samuels, 264 N.Y. 144 (1934); Matter of People of the State of New York v. Title & Mortgage Guar. Co., 264 N.Y. 69 (1934); Maguire & Co. v. Lent & Lent, Inc., 277 N.Y. 694 (1938).

Here, the Legislature enacted the Moratorium Act in the exercise of precisely that power and in fulfillment of just that duty.

The compelling circumstances which gave rise to the Moratorium Act are detailed in the legislative findings accompanying the Act:
"The grave public emergency found and declared to exist by the legislature in adopting the New York State Financial Emergency Act for the City of New York has dramatically worsened in the last two months. Today, not only is the City of New York threatened with default on its outstanding obligations, but financially sound agencies of the state itself are similarly threatened because of public fears about the effects of default by the city.

"Significant and drastic steps have been and continue to be taken by the city and the state pursuant to the New York Municipal Assistance Corporation Act and the New York State Financial Emergency Act of the City of New York to eliminate the causes of this crisis and to restore the city to financial health. It is now apparent, however, that there is not enough time for the effects of these steps to be demonstrated before all funds now available to the city will be exhausted.

"There is therefore an imminent danger that the city of New York will be unable to pay its outstanding short-term indebtedness and even to provide those basic services essential to the health, safety and welfare of its inhabitants and the continuation of orderly government in the city. The legislature recognizes and insists that the pledge of the 'faith and credit' of the city to the payment of its obligations must be respected. The legislature further recognizes that in the current financial crisis, this pledge can be honored only if the viability and resources of the city are preserved and that the continuation of essential services is vital to such preservation. The preservation of the city, the honoring of its obligations and the restoration of public confidence in the agencies of the state and of the state itself are all matters of imperative state concern and require the extraordinary exercise of the state's essential reserve and emergency powers set out in this Act to protect the vital interests of the people by sustaining the public credit and maintaining local government."

(A47-48)

Giving due regard, therefore, to the legislative findings,* the emergency declared by the Legislature to exist with

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* This Court can and should take judicial notice of the facts which compelled the Legislature to act. See, e.g., New York City Tunnel Auth. v. Consolidated Edison Co. of New York, Inc., 295 N.Y. 467, 476 (1946); Cole Fisher Rogow, Inc. v. Carl Ally, Inc., 29 App. Div. 2d 423, 426 (1st Dep't 1968), aff'd, 25 N.Y.2d 943 (1969). Moreover, the courts of this State have traditionally recognized that legislative findings, particularly legislative declarations of emergency, are entitled to great weight. See, e.g., East New (footnote continued)
respect to New York City presents a classic occasion for the exercise of the State's emergency police powers in general — and for the challenged exercise of that power, the Moratorium Act, in particular.

Appellant's notion that the Contract Clause of the United States Constitution is an absolute bar to a State's intrusion into contracts was conclusively laid to rest over 40 years ago by the United States Supreme Court in *Home Bldg. & Loan Ass'n v. Blaisdell*, 290 U.S. 398, 428 (1934), supra. The issue before the Court in *Blaisdell* was the validity of the Minnesota Mortgage Moratorium Law. That law, like the Moratorium Act here, was enacted by the State Legislature in response to an "economic emergency" — there, the depression of the 1930's — which was threatening "the vital interests of the community" (290 U.S. at 444). The Minnesota moratorium law, again like the Moratorium Act here, authorized the suspension of the right of a creditor (the mortgagee) to collect the principal of his debt, either by seeking foreclosure or bringing an action for a deficiency judgment, for a period up to two years. (290 U.S. at 416-18.)

In upholding the constitutionality of the Minnesota moratorium law, the Supreme Court defined the relationship between the State's police power and the Contract Clause in terms which explicitly govern the present case:

(footnote continued)
* York Sav. Bank v. Hahn, 293 N.Y. 622, 627 (1944), aff'd, 326 U.S. 230 (1945). Adherence to this doctrine is especially appropriate in this case, where both the root of the emergency and its solution entail complex problems of budgeting and taxation — areas in which the courts have traditionally deferred to the legislative and executive branches of government. See Becker v. Levitt, 489 F.2d 1087, 1090 (2d Cir. 1973).
"while emergency does not create power, emergency may furnish the occasion for the exercise of power.....

"Not only is the constitutional provision qualified by the measure of control which the State retains over remedial processes, but the State also continues to possess authority to safeguard the vital interests of its people. It does not matter that legislation appropriate to that end 'has the result of modifying or abrogating contracts already in effect'..... Not only are existing laws read into contracts in order to fix obligations as between the parties, but the reservation of essential attributes of sovereign power is also read into the contracts as a postulate of the legal order. The policy of protecting contracts against impairment presupposes the maintenance of a government by virtue of which contractual relations are worthwhile -- a government which retains adequate authority to secure the peace and good order of society. This principle of harmonizing the constitutional prohibition with the necessary residuum of state power has had progressive recognition in the decisions of this Court." (290 U.S. at 426, 434-35; emphasis supplied.)

The Supreme Court went on to recognize that

"... [e]conomic interests of the State may justify the exercise of its continuing and dominant protective power notwithstanding interference with contracts"

and that, in such instances, the sole question for judicial determination

"... is not whether the legislative action affects contracts incidentally, or directly or indirectly, but whether the legislation is addressed to a legitimate end and the measures taken are reasonable and appropriate to that end." (290 U.S. at 437-38.)

This reaffirmation of the nature and scope of the fundamental police power of the State was echoed in a later Supreme Court decision sustaining New York's own mortgage moratorium law -- after which the present Moratorium Act is closely patterned. See East


The State of New York first enacted a moratorium law, suspending the right of a mortgagee to seek to enforce his mort-
gage by foreclosure or suit for non-payment of principal, in 1933. (L. 1933, ch. 793.) As appellant concedes, this original moratorium law was in effect for over a decade. (App. Br. 31.) The New York Court of Appeals sustained the original enactment of the moratorium law against constitutional challenge in Klinke v. Samuels, 264 N.Y. 144 (1933), supra, and subsequently sustained its extension in East New York Sav. Bank v. Hahn, 293 N.Y. 622 (1944), supra.

In 1945, the Hahn case reached the United States Supreme Court -- and the challenge to the New York mortgage moratorium, then in effect for 12 years, was rejected summarily and without dissent. As the Supreme Court stated:

"The Blaisdell case and decisions rendered since [citations omitted] yield this governing constitutional principle: when a widely diffused public interest has become enmeshed in a network of multitudinous private arrangements, the authority of the State 'to safeguard the vital interests of its people,' . . . is not to be gainsaid by abstracting one such arrangement from its public context and treating it as though it were an isolated private contract constitutionally immune from impairment."

"The formal mode of reasoning by means of which 'protective power of the State,' . . . is acknowledged is of little moment. It may be treated as an implied condition of every contract and, as such, as much part of the contract as though it were written into it, whereby the State's exercise of its power enforces, and does not impair, a contract. A more candid statement is to recognize . . . that the power 'which in its various ramifications is known as the police power, is an exercise of the sovereign right of the Government to protect the . . . general welfare of the people, and is paramount to any rights under contracts between individuals.' [Citations omitted.] Once we are in this domain of the reserve power of a State we must respect the 'wide discretion on the part of the legislature in determining what is and what is not necessary.' Ibid. So far as the constitutional issue is concerned, 'the power of the State when otherwise justified,' [citations omitted], is not diminished because a private contract may be affected." (326 U.S. at 232-33; emphasis supplied.)
B. The State's Police Power May Affect Public Contracts as Well as Private Contracts

Appellant's contention that the foregoing cases are inapplicable here because they involved "contracts between private parties", while here we have a "contractual debt obligation between the State's own municipal creation, the City, and its noteholders" (App. Br. 23), was expressly rejected by the Court below (A15-16) and is wholly without merit.

While Blaisdell and Hahn involved private contracts, the Supreme Court at no time suggested that the doctrine that State police power is implicitly reserved in contractual obligations in situations of public emergency would not apply equally to public contracts. On the contrary, in Blaisdell, the Court expressly recognized the applicability of its holding (rejecting the Contract Clause argument) to "all contracts, whether made between States and individuals, or between individuals only" (290 U.S. at 435). This is only logical. Whether the rationale of the cited decisions is taken to be that the essential exercise of State police power is "an implied condition of every contract" (Hahn, supra, 326 U.S. at 232) or that contracts "enmeshed" with a "widely diffused public interest" become subject to the State's power and duty to protect that interest (ibid.), that same rationale applies, a fortiori, to public contracts. Clearly, it turns logic upside down to argue, as appellant does here, that, in the exercise of its police power, a State has less freedom to alter the contracts of its own political subdivision -- which by definition directly affect the public interest -- than it has to alter contracts which are wholly private.
and which affect the public interest only indirectly. As the Supreme Court has put it:

"If a State retains police power [to alter contracts] with respect to building and loan associations [citation omitted], because of their relation to the financial well-being of the State, and if it may authorize the reorganization of an insolvent bank upon the approval of a state superintendent of banks and a court, but over the dissent of one fourth of the depositors (except preferred or secured claimants) [citation omitted], a State should certainly not be denied a like power for the maintenance of its political subdivisions and for the protection not only of their credit but of all the creditors..."

(Paitout Iron & Steel Co. v. City of Asbury Park, 316 U.S. 502, 513-14 (1942), supra; emphasis supplied.)

In any event, the merits of appellant's lame attempt to distinguish between public and private contracts need not be debated here. That issue, too, has already been resolved -- against appellant -- and, again, by the highest Court of the land. Thus, the United States Supreme Court has sustained, against constitutional attack under the Contract Clause, State legislation exactly like the Moratorium Act -- i.e., legislation barring holders of municipal obligations from seeking to enforce those obligations in the courts for a period of time. See Paitout Iron & Steel Co. v. City of Asbury Park, 316 U.S. 502 (1942), supra. Appellant's assertion that "[t]here is no decision by the Supreme Court which has sanctioned" State legislation such as the Moratorium Act, therefore, is just plain wrong. (App. Br. 20.)

In Paitout, the Supreme Court unanimously upheld a New Jersey statute enacted, as was the Moratorium Act here, "'to meet the public emergency arising from a default in the payment of municipal obligations, and the resulting impairment of public credit'" (316 U.S. at 504). The New Jersey statute included not only "moratorium"
provisions -- like those in the Moratorium Act here -- suspending the right of holders of municipal obligations to seek to enforce those obligations, but also "composition" provisions -- beyond anything in the Moratorium Act -- permitting municipalities to require holders of its outstanding obligations, without their consent, to exchange their obligations for other obligations with different maturity dates and interest rates.

The Faitouté case, therefore, is directly in point, and provides clear and controlling authority establishing the constitutionality of the Moratorium Act in this case.

Moreover, subsequent to Faitouté, the Supreme Court, in City of El Paso v. Simmons, 379 U.S. 497 (1965), again upheld State legislation substantially modifying contracts existing between private individuals and a governmental entity. In so doing, the Court expressly and fully approved the teachings of Blaisdell without any suggestion that they should be applied differently to public and private contracts.

Appellant attempts to sidestep El Paso by arguing -- from random quotations taken wholly out of context -- that the decision there "does not in any way diminish the vitality of the special sanctity of the State's own obligations under the Contract clause." (App. Br. 25-26.) The basis of that contention is less than clear. The statute in question in El Paso drastically reduced the time in which purchasers of State land could cure defaults in installment payments due pursuant to their contracts with the State and thereby redeem their property. The practical effect of the modification upon plaintiff in that case, therefore, was to deprive him of his
land entirely -- an effect hardly consistent with "the sanctity of the State's ... obligations."

While the Supreme Court's decisions in Blaisdell, Hahn, Paitoute and El Paso, supra, are notable for their thorough and well-reasoned rejection of attacks on emergency State legislative action based upon the Contract Clause, those cases are not "unique" or unprecedented. (App. Br. 4.) The authority of a State to regulate contractual rights in furtherance of vital community interests is well established by a multitude of relevant decisions.*

Thus, for example, in Veix v. Sixth Ward Bldg. & Loan Ass'n, 310 U.S. 32 (1940), the Supreme Court upheld a New Jersey statute prohibiting creditors of financially threatened building and loan associations from bringing suit to withdraw their short-term investments in accordance with their agreements. In dismissing a constitutional challenge to that legislation, the Court observed (at 37-39):

"We are dealing with financial institutions of major importance to the credit system of the State.

"With institutions of such importance to its

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* The cases supporting our view of the Contract Clause are actually legion. See, e.g., in addition to those discussed in the text above, Block v. Hirsh, 256 U.S. 135 (1921), and People ex rel. Durham Realty Corp. v. LaFetra, 230 N.Y. 429 (1921), in which the Courts upheld local rent control statutes which, among other things, suspended the contractual right of landlords to remove tenants at the expiration of their lease term; and Doty v. Love, 295 U.S. 64 (1935), in which the Supreme Court upheld a Mississippi statute permitting banks which were closed during the Depression to re-open pursuant to plans which restricted the existing contractual right of depositors to withdraw their funds. Additional authorities on the State court level are Security Unit Employees v. Rockefeller, 76 Misc.2d 435 (Sup. Ct. Albany Co. 1974); Matter of Farrell v. Drew, 19 N.Y.2d 486, 493 (1967); Matter of Dep't of Bldgs. of the City of New York (Philco Realty Corp.), 14 N.Y. 2d 291, 297-98 (1964).
economy, the State retains police powers adequate to . . . regulat[e] the withdrawal of shares . . . .

"[T]he authority retained by the State over contracts . . . is not limited to health, morals and safety. It extends to economic needs as well."

A learned review of the relevant decisions is contained in the recent opinion of the Superior Court of New Jersey in United States Trust Co. v. State of New Jersey, 134 N.J. Super. 124, 338 A.2d 833 (1975), which was affirmed on February 25, 1976 by the Supreme Court of New Jersey (Docket Nos. A-45/46/47) based upon the opinion below. The Court there upheld a State statute which, based upon a legislative finding that the development of a mass transit system was in the public interest, repeal a 1962 New York-New Jersey covenant prohibiting the use of Port Authority revenues for mass transit, thereby precluding Port Authority bondholders from seeking to enforce that covenant even though it was in effect at the time they purchased their bonds. In rejecting the plaintiff-bondholder's challenge based, as here, upon the Contract (and Due Process) Clauses of the United States Constitution, the Court stated (134 N.J. Super. at 188-90):

"During the span of more than a century between Ogden v. Saunders [1827] and Blaisdell [1933] the court had held on numerous occasions that the states retained the power to impair contractual obligations -- including those to which the state was a party -- in the exercise of their always reserved police powers to act in the interest of the public health, safety and general welfare. First in dictum, Boyd v. Alabama, 94 U.S. 645, 650, 24 L. Ed. 302 (1877), and then by direct application of the doctrine, the court held that a lottery franchise granted for a definite term of years could be repealed. Stone v. Mississippi, 101 U.S. 814, 25 L. Ed. 1079 (1880); Douglas v. Kentucky, 168 U.S. 488, 18 S. Ct. 199, 42 L. Ed. 553 (1897). In Northwestern Fertilizing Co. v. Hyde Park, 97 U.S. 659, 24 L. Ed. 1036 (1878), it was held that a franchise to operate a fertilizer factory at a given location could be negated by the exercise of the police power to abate a nuisance. Similarly, the
power to control the use of the public streets may not be bargained away, Atlantic Coast Line R. Co. v. Goldsboro, 232 U.S. 548 34 S. Ct. 364, 58 L. Ed. 721 (1914); Denver & Rio Grande R. Co. v. Denver, 250 U.S. 241, 39 S. Ct. 450, 63 L. Ed. 958 (1919), nor can the state contractually bind itself not to exercise its power of eminent domain, West River Bridge Co. v. Dix, 47 U.S. (6 How.) 507, 12 L. Ed. 535 (1848); Pennsylvania Hospital v. Philadelphia, 245 U.S. 20, 38 S. Ct. 35, 62 L. Ed. 124 (1917), or to change the location of its governmental subdivisions, Newton v. Mahoning County, 100 U.S. 548, 25 L. Ed. 710 (1880). The broadest expression of this view of the police power during this period is to be found in Chicago & Alton R.R. v. Tranbarger, 238 U.S. 67, 35 S. Ct. 678, 59 L. Ed. 1204 (1915), where Justice Pitney said:

'It is established by repeated decisions of this court that neither of these provisions of the Federal Constitution (the Contract and Due Process Clauses) has the effect of overriding the power of the state to establish all regulations reasonably necessary to secure the health, safety, or general welfare of the community; that this power can neither be abdicated nor bargained away and is inalienable even by express grant; and that all contract and property rights are held subject to its fair exercise * * *. And it is also settled that the police power embraces regulations designed to promote the public convenience or the general welfare and prosperity, as well as those in the interest of public health, morals or safety.' (238 U.S. at 76-77. 35 S. Ct. at 682)

"While Blaisdell placed great emphasis upon the emergency character of the Minnesota law to validate the action taken, decisions of the court since then have sanctioned non-emergent legislation impairing contractual rights and remedies where necessary to protect the economic well being of state. See Veix v. Sixth Ward B. & L. Ass'n of Newark, 310 U.S. 32, 60 S. Ct. 792, 84 L. Ed. 1061 (1940); Gelfert v. National City Bank, 313 U.S. 221, 61 S. Ct. 898, 85 L. Ed. 1299 (1941)."

Perhaps the most recent reaffirmation of these principles came in a series of cases decided by the Appellate Division, Second Department, on January 6, 1976, but not yet officially reported.

Matter of Schwab v. Bowen, ___ A.D. 2d ___ (2d Dep't 1976); Matter of Bd. of Educ. v. Yonkers Fed'n of Teachers, ___ A.D. 2d ___ (2d Dep't 1976); Yonkers School Crossing Guard Union v. City of Yonkers, ___
A.D. 2d ___ (2d Dep't 1976); see N.Y.L.J., Jan. 27, 1976, p. 1, col. 3.

* The Court there sustained the constitutionality of recent emergency State legislation for Yonkers and municipal action in Long Beach permitting those cities to dismiss their employees despite any contrary provisions in those cities' agreements with the employees. As the Court stated in Schwab:

"[T]he fiscal crisis facing the City of Long Beach threatens its very ability to govern and to provide essential services for its citizens. The City must not be stripped of its means of survival." (RA, p.A-1)

The problems of New York City are certainly no less grave, nor are these words any less appropriate in this case.

C. The Moratorium Act Does Not "Impair" the City Notes Within the Constitutional or Common Meaning of the Word

Incidental to the holdings in the cases cited above is a recognition of the fact -- lost on appellant here -- that flexibility in the enforcement of obligations may be essential to preserve their value. Given the financial crisis which now exists in New York City, the greatest threat to the security of City noteholders arises not from responsive legislative action, but from widespread litigation which will disrupt and impede the City's financial recovery.

It has already been observed that passage of the Moratorium Act was premised on a legislative finding of an imminent danger that New York City would be unable to pay its outstanding notes when they matured, regardless of its more theoretical than real powers over taxation and spending. (A47-48; RA15-18; see pp. 5-6, 11-15, supra.)

* Copies of these decisions have been included as addenda to respondent's joint appendix. (RA, p. A-1 et seq.)
The avowed purpose (and obvious effect) of the Moratorium Act is "to ameliorate the disastrous consequences" that would otherwise flow from such inability of the City to meet its obligations -- such as "destructive actions" by disgruntled noteholders -- "so as to facilitate restoration of the City's financial integrity and payment of all its obligations." (A48) As the Legislature also stated:

"The legislature recognizes and insists that the pledge of the 'faith and credit' of the city to the payment of its obligations must be respected. The legislature further recognizes that in the current financial crisis, this pledge can be honored only if the viability and resources of the city are preserved and that the continuation of essential services is vital to such preservation." (Ibid.)

By furthering the goal of preserving "the viability and resources of the city" in order to permit the eventual payment of notes which the City cannot now pay, the Moratorium Act, therefore, enhances rather than impairs the value of City obligations and avoids constitutional proscription:

"Impairment of an obligation means refusal to pay an honest debt; it does not mean contriving ways and means for paying it. The necessity compelled by unexpected financial conditions to modify an original arrangement for discharging a city's debt is implied in every such obligation for the very reason that thereby the obligation is discharged, not impaired." (Faitoute Iron & Steel Co. v. City of Asbury Park, 316 U.S. at 511, supra.)

Appellant's speculations to the contrary notwithstanding (App. Br. 12-13.), the Moratorium Act contemplates that the City will be in a position to pay the principal on its outstanding notes at the end of three years. In the meantime, the Act provides for the noteholders to be paid interest at the rate called for by their notes until their stated maturity date and, thereafter, at a rate no less than twice that to which such noteholders would otherwise be legally entitled. (A51, 53; Gen. Mun. Law, § 3-a; see pp. 7-8, 11, supra.)
Like the legislation in *Faitoute*, then, the Moratorium Act is not a statute which "impairs" the note holders' contracts with the City, but a valid effort by the Legislature to enable the City to honor its contracts.

Beyond this, the Moratorium Act does no more than impose a temporary and conditional stay on the remedies available to City note holders in furtherance of the remedial programs for the City embodied in the earlier Municipal Assistance Corporation Act (L. 1975, ch. 169) and Financial Emergency Act (L. 1975, ch. 868, et seq.)* Moreover, the judicial remedies which have been suspended as part of the legis lative rescue effort have traditionally proven illusory.

Thus, whether or not a moratorium exists, creditors are barred from enforcing judgments against public property, including bank deposits and other monetary reserves of the City. See, e.g., *Hernandez v. City of New York*, Index No. 3044/67 (Sup. Ct., Bronx Co., November 6, 1975) (RA8-14). Similarly, municipal creditors have no right to set off their claims against taxes or other obligations owed to the City. *Piscataway Township v. First Nat'l City Bank*, 111 N.J.L. 412, 168 Atl. 757 (Ct. Err. & App. 1933). And, finally, the remedy which has traditionally been available to municipal creditors -- a mandamus proceeding to compel the levy and collection of additional taxes -- has consistently proven unavailing. See *Faitoute Iron & Steel Co. v. City of Asbury Park*, 316 U.S. 502, 510-11 (1942), *supra*. "The experi-

*addition, the Moratorium Act was apparently viewed by President * as an essential ingredient of the "financial package de signed to restore New York City's fiscal integrity", the adoption which caused the Administration to support the New York City Municipal Financing Act of 1975, which will provide critical Federal short-term loans to the City. (A164-65; RA20-22, 57)
ence of the two modern periods of municipal defaults," the Supreme Court said in Faitoute (316 U.S. at 510), "shows that the right to enforce claims against the city through mandamus is the empty right to litigate."* Manifestly, such an "empty right" is not one with which the Constitution is concerned. As the Court also stated in Faitoute (at 514-15):

"The Constitution is 'intended to preserve practical and substantial rights, not to maintain theories.' [Citation omitted.] Particularly in a case like this are we in the realm of actualities and not of abstractions and paper rights, of what things are worth in dollars and cents, and in what is proposed to realize paper values. The question whether the remedy on this contract was impaired materially is affected not only by the precarious character of the plaintiff's right, but by considerations of fact -- of what the remedy amounted to in practice." [Citation omitted.] This was said of the claim of a creditor of a private corporation. How much more pertinent is it to claims of these appellants against the municipality . . . in the circumstances before us. To say that the right of the Asbury Park bondholders in 1935 was of precarious character is pure understatement. And we have already seen how empty was the remedy with which to enforce that right."

D. Faitoute Is Indistinguishable From the Present Case

As we have seen, in the Faitoute case (316 U.S. 502, supra), the Supreme Court upheld, against a Contract Clause challenge, a State statute which, among other things, suspended the right of holders of municipal obligations to seek to enforce those obligations in the

* Mandamus, of course, is a discretionary remedy. (See, e.g., N.Y.S. Const., Art. 8, § 2, ¶ 4.) Even absent a statutory command like the Moratorium Act, State courts have denied relief by way of mandamus in the exercise of such discretion where hardship or impairment of the municipality's essential services would otherwise result. See, e.g., Matter of Coombs v. Edwards, 280 N.Y. 361 (1939); Faitoute Iron & Steel Co. v. City of Asbury Park, 127 N.J.L. 239 (Ct. Err. & App. 1940), aff'd, 316 U.S. 502 (1942), supra. Even where courts were inclined to grant such relief, problems of enforcement have historically rendered their efforts nugatory. (See 316 U.S. at 510-11.)
courts. (See pp. 27-28, supra.) In attempting to evade the effect of \textit{Faitoute}, appellant relies on arguments which are either without basis in fact or without relevance to the constitutional doctrine underlying the Supreme Court's opinion. (App. Br. 4-6.)

1. Appellant apparently seeks to distinguish \textit{Faitoute} on the ground that it involved a State statute authorizing a "composition". (App. Br. 4.)

But, as previously noted, \textit{Faitoute} upheld a statute imposing both a composition and a moratorium. (See p. 28, supra.) The fact that the New Jersey statute went beyond the present Moratorium Act, and was upheld in all respects by the Supreme Court, adds rather than detracts from its strong precedential value.

2. Next, appellant relies on a single sentence of dictum at the end of the opinion in \textit{Faitoute} (316 U.S. at 516) in which the Supreme Court acknowledged a decision by the New Jersey courts that, "under [the New Jersey] statute", certain types of municipal notes (tax anticipation and revenue notes) "stand on entirely different footing from other municipal obligations" and "in relation to them no claim is affected by" the New Jersey statute. (App. Br. 5.)

On its face, however, this sentence reflects no more than a recognition by the Supreme Court of a State court decision that the specified notes were not intended by the New Jersey legislature to be covered by the New Jersey statute in issue, and thus stood on "a different footing" from the other New Jersey municipal obligations covered by the statute. The Supreme Court did not express any opinion as to whether the New Jersey Legislature could have enacted a moratorium covering those notes. On the contrary, the Court said:
"We do not go beyond the case before us." (316 U.S. at 516.) Moreover, the fact that certain types of notes were not covered by the New Jersey statute, while other types of municipal obligations were covered, is beside the point here. All City notes are expressly covered by the Moratorium Act. Nothing in the Faitoute opinion indicates that TANS, RANS or any other kind of municipal obligation stand on "a different footing" from any other kind of municipal obligation under the Contract Clause, or that emergency moratory legislation could not encompass all such obligations without violating that clause. Indeed, the entire thrust of the Supreme Court's opinion is to the contrary.

3. Appellant next argues that the "faith and credit" pledge and other "guarantees" in provisions of Article 8 of the New York State Constitution (§§ 2, 10, 12) add a special dimension to the contract of a City noteholder which somehow overcomes the limitations upon the Contract Clause recognized in Faitoute. (App. Br. 5.)

But, as previously noted, appellant's interpretation of the relevant provisions of the New York State Constitution is erroneous. (See pp. 16, 19-20, supra, and 54-60, infra.) Moreover, as the Record on Appeal (p. 22) in the Supreme Court in Faitoute reveals, the municipal obligations covered by the moratorium in that case, like the City notes here, were "valid and legally binding obligations of the City payable as to both principal and interest from unlimited ad valorem taxes upon all the taxable property within the City."
Thus, the cases cannot be distinguished on the basis of the obligations affected.

4. Appellant then advances the remarkable proposition that
Congress "overruled" the Supreme Court's decision in Faitoute by enacting Section 83(i) of the Federal Bankruptcy Act, 11 U.S.C. § 403(i). (App. Br. 5.)

Congress, of course, cannot "overrule" or replace the Supreme Court as the final arbiter of the United States Constitution. Nor did Congress purport to do so in enacting Section 83(i). As we shall show, that provision was not intended to, nor did it, affect that aspect of the decision in Faitoute holding that a State moratorium on the enforcement of municipal obligations was not violative of the Contract Clause of the United States Constitution. (316 U.S. at 509 et seq.) Rather, Congress sought merely to overcome the other aspect of the Supreme Court's decision, which sustained a State-mandated "composition" of municipal indebtedness. (See p. 27-28, supra, and pp. 68-69, infra.)

E. The Cases Cited By Appellant Are Outdated and Inapposite.

To support its argument that the Moratorium Act violates the Contract Clause, appellant relies upon a smattering of cases which are almost universally irrelevant and which, to the extent they do collide with the Supreme Court's validation of moratory legislation in Faitoute, Hahn, and Blaisdell, are without continuing vitality.

While the venerability of the alleged "applicable decisions" on which appellant relies is undeniable,* so too is their

* Thus, every one of the Supreme Court cases cited by appellant -- most of which were decided between 1810 and 1882 -- predate the critical Faitoute and Hahn decisions. (App. Br. 19-27, 30-34.)
lack of authoritative viability in the present case. (App. Br. 3.) Indeed, the United States Supreme Court has noted as much with respect to the first of the cases cited by appellant, *Sturges v. Crowinshield*, 17 U.S. (4 Wheat.) 122 (1819). (App. Br. 19.) Thus, Mr. Justice Frankfurter stated in *Faitoute* (316 U.S. at 513, supra):

> "From time to time, ever since *Sturges v. Crowinshield*, 4 Wheat, 122, 199, it has been stated that a state insolvency act is limited by the Contract Clause of the Constitution in authorizing composition of preexisting debts. So it is, but it all depends on what is affected by such a composition and what state power it brings into play. The dictum from *Sturges v. Crowinshield* is one of those inaccurate generalizations that have gained momentum from uncritical repetition." (Emphasis supplied.)

But the momentum of the "inaccurate generalizations" attributable to *Sturges* and the other tarnished precedents relied upon by appellant was blunted well before the announcement of its demise in *Faitoute*. Clearly, the extensive analysis of the Contract Clause contained in *Blaisdell* put it beyond question that early cases restricting State action under the Contract Clause cannot be expanded beyond their narrow context when the effect of such expansion would be to incapacitate a State in times of emergency. (See pp. 23-24, supra.)

The seminal nature of the *Blaisdell* decision was commented upon by the Supreme Court in *East New York Sav. Bank v. Hahn*, 326 U.S. 230 (1945), supra, upholding the New York Mortgage Moratorium Law and, more recently, in *El Paso v. Simmons*, 379 U.S. 497 (1965), supra, which, as previously noted, applied the principles of *Blaisdell* to uphold State legislation retroactively limiting rights of redemption accorded purchasers of State land. (See pp. 24-29, supra.)
Thus, in Hahn, the Supreme Court stated:

"Since Home Bldg. & L. Assn. v. Blaisdell, 290 U.S. 398, there are left hardly any open spaces of controversy concerning the constitutional restrictions of the Contract Clause upon moratory legislation referable to the depression. The comprehensive opinion of Mr. Chief Justice Hughes in that case cut beneath the skin of words to the core of meaning. After a full review of the whole course of decisions expounding the Contract Clause--covering almost the life of this Court -- the Chief Justice, drawing on the early insight of Mr. Justice Johnson in Ogden v. Saunders, 12 Wheat, 213, 286, as reinforced by later decisions cast in more modern terms, e.g., Manigault v. Springs, 199 U.S. 473, 480; Marcus Brown Co. v. Feldman, 256 U.S. 170, 198, put the Clause in its proper perspective in our constitutional framework. The Blaisdell case and decisions rendered since (e.g., Honeyman v. Jacobs, 306 U.S. 539; Veix v. Sixth Ward Assn., 310 U.S. 32; Gelfert v. National City Bank, 313 U.S. 221, Faitoute Co. v. Asbury Park, 316 U.S. 502), yield this governing constitutional principle; when a widely diffused public interest has become enmeshed in a network of multitudinous private arrangements, the authority of the State 'to safeguard the vital interests of its people,' 290 U.S. at 434, is not to be gainsaid by abstracting one such arrangement from its public context and treating it as though it were an isolated private contract constitutionally immune from impairment." (326 U.S. at 231-32.)

Similarly, in El Paso, the Supreme Court observed that:

"The Blaisdell opinion, which amounted to a comprehensive restatement of the principles underlying the application of the Contract Clause, makes it quite clear that '[n]ot only is the constitutional provision qualified by the measure of control which the State retains over remedial processes, but the State also continues to possess authority to safeguard the vital interests of its people. It does not matter that legislation appropriate to that end 'has the result of modifying or abrogating contracts already in effect.' Stephenson v. Binford, 287 U.S. 251, 276. Not only are existing laws read into contracts in order to fix obligations as between the parties, but the reservation of essential attributes of sovereign power is also read into contracts as a postulate of the legal order . . . . This principle of harmonizing the constitutional prohibition with the necessary residuum of state power has had progressive recognition in the decisions of this Court. 290 U.S. at 434-435." (379 U.S. at 508; emphasis supplied.)
Appellant would (to paraphrase El Paso) strip away decades of progressive interpretation of the Contract Clause and have this Court shape the future of New York City and State on the basis of emanations from outdated and inapposite decisions. The position is hardly tenable. As the Court stated in rejecting a similar effort by the plaintiff-bondholders in United States Trust Co. v. State of New Jersey, 134 N.Y. Super. 124, 197, 338 A.2d 833, 874 (1975) -- discussed at pp. 30-31, supra -- appellant

"...seeks to recreate a theory of the Contract Clause which, if ever imbedded in our constitutional law, no longer exists. As reflected in the course of more than 150 years of its judicial interpretation, the Contract Clause must be construed in harmony with the power of the states to alter or modify their contractual obligations where an important public interest requires."

Moreover, apart from their age and the force of subsequent decisions, the cases relied upon by appellant would not be controlling here in any event.

The case of W. B. Worthen Co. v. Kavanaugh, 295 U.S. 56 (1935), is the only decision cited by appellant (other than the Fort Lee case, discussed below) arising under circumstances in any way comparable to those which necessitated the Moratorium Act. And the legislative response in Worthen was held unconstitutional only because of offending aspects having no counterpart in the Moratorium Act.

Thus, the mortgage moratorium law challenged in Worthen -- a statute of the same type upheld in Blaisdell and Hahn -- indiscriminately imposed a blanket moratorium on the enforcement of all mortgages, regardless of the debtor's ability to pay. Here, however, there is but one debtor -- the City -- and its inability to pay, as
found by the Legislature, is clear. In addition, the statute before the Court in *Worthen* disrupted all incidents of the mortgage contract, including the obligation to pay interest. Specifically, that statute relieved debtors of liability for the nonpayment of all interest for a period of at least 6-1/2 years. (295 U.S. at 61.) By contrast, the *Moratorium Act* requires that interest be paid on the City notes at the stipulated rate until maturity, and at double the applicable statutory rate thereafter. (See pp. 7-8, 11, *supra*, and 53-54, 67-68, *infra*.) Moreover, the length of the stay imposed in *Worthen* was unrelated to the foreseeable duration of the emergency. In this case, however, the three-year suspension of noteholders' claims imposed by the *Moratorium Act* corresponds exactly to the period within which the City must balance its budget and to the duration of the City's Financial Plan. (Al58)

Finally, as the Supreme Court noted in *Faitoute* in distinguishing *Worthen*: "[T]he challenged changes of remedy [in *Worthen*] were found to be 'an oppressive and unnecessary destruction of nearly all the incidents that give attractiveness and value to collateral security.' Here we have just the opposite -- no security whatever except the effective taxing power of the municipality" and, as the Court went on to observe, a State plan calculated to preserve the effectiveness of that power by avoiding oppressive and self-defeating tax levies. (316 U.S. at 515-16.) The same can be said of the *Moratorium Act*. Indeed, the very language from *Worthen* quoted by appellant (App. Br. 32-33) acknowledges that moratory legislation will be upheld so long as it evinces "moderation [and] reason" rather than "a spirit of oppression." (245 U.S. at 60.) The *Moratorium Act*, we submit, clearly meets this test.
Indeed, the statute challenged in Faitoute was no less "oppressive" than the statute in Worthen, and was not nearly as "moderate" and "reasonable" as the Moratorium Act. Thus, in Faitoute, investors in municipal obligations having durations of no more than five years were compelled to exchange their obligations for refunding bonds maturing in 35 or more years. And, the Asbury Park plan at issue in Faitoute provided for a reduction of the interest rates payable during the term of the original investments from over 5% to 3%, and for interest to be paid on the refunding bonds at a rate of 4%. (Record on Appeal, pp. 13-17.) Nevertheless, the statute and plan were unanimously upheld by the Supreme Court.

Borough of Fort Lee v. United States, 104 F.2d 275 (3d Cir. 1939), relied upon by appellant, is also easily disposed of, although for different reasons. (App. Br. 27-28.) Unlike Worthen, the facts of Fort Lee are admittedly virtually identical with those here. Its infirmity as a precedent for appellant's position lies in the fact that the Supreme Court, three years later, implicitly overruled Fort Lee in the Faitoute case.

Like the Moratorium Act here, the New Jersey statute "principally relied upon" in Fort Lee -- N.J.S.A. § 52:27-33 -- which was a section of the New Jersey Municipal Finance Commission Act, provided for a suspension of the right of holders of municipal obligations to enforce those obligations in the courts. (104 F.2d at 281.) Appellant, however, glosses over the fact that the New Jersey Municipal Finance Commission Act was also passed upon in Faitoute, and that the very same section relied upon in Fort Lee was incorporated by reference in the provisions which the Supreme Court upheld. Among
those provisions -- set out in full in the Faitoute opinion (316 U.S. 505-06) -- is the following:

"52:27-38. Continuance of stay of proceedings against municipality; action by creditor to enforce claim restricted. After the institution of any proceeding provided for in this article and pending the determination thereof, the supreme court [of New Jersey] by a justice thereof may by order continue the stay provided by sections 52:27-32.1 and 52:27-33 of this title. (Emphasis supplied.)

Upon authorization and approval of a refunding plan, the stay was automatically converted to a permanent bar. The stay of judicial proceedings was therefore a vital element of the statute considered in Faitoute, and one of which the Supreme Court was keenly aware. It would, in any event, follow a fortiori that, if a permanent bar of judicial proceedings is constitutionally permissible, as held in Faitoute, a temporary stay of judicial proceedings, such as was considered in Fort Lee, under substantially identical circumstances, must also be constitutionally permissible as a lesser "impairment" of the obligation in issue. Thus, Faitoute clearly overruled Fort Lee and leaves its interpretation of the Contract Clause without continuing validity.

Furthermore, the Third Circuit in Fort Lee affirmed a District Court order extending the time for repayment of the municipal obligations in question, in the exercise of the Court's inherent discretion, for 15 years and, in so doing, held that:

"[t]he operating expenses of the municipality are to be paid before the claims of holders of municipal bonds" because

"[t]he safety and health of the citizen are of prime importance and neither can be endangered because a creditor wants his due." (104 F.2d at 284.)
This is the surviving principle of *Port Lee*, embraced by the United States Supreme Court in *Faitoute* and by the New York State Legislature in enacting the Moratorium Act.

Appellant's reliance on the Gold Clause case of *Perry v. United States*, 294 U.S. 330 (1934), for the proposition that there is a "stringent limitation on the exercise of police power applicable to legislative changes in governmental obligations" is completely unfounded. (App. Br. 24-25.) First, the *Perry* case did not even involve the issue of State police power, much less its exercise in an emergency. Second, the Contract Clause of the Constitution was never there in question. Third, plaintiff in *Perry* lost his challenge against the governmental action. Fourth, the decision in *Perry*, if anything, supports the Moratorium Act. Thus, the Court observed (294 U.S. at 354):

"The fact that the United States may not be sued without its consent is a matter of procedure which does not affect the legal and binding character of its contracts. While the Congress is under no duty to provide remedies through the courts, the contractual obligation still exists and, despite infirmities of procedure, remains binding upon the conscience of the sovereign."

Similarly, nothing in the Moratorium Act "affects the legal and binding character" of the City's notes, but merely suspends the note-holders' "remedies through the courts." The Supreme Court in *Perry* also noted (at 348):

"The bond in suit differs from an obligation of private parties, of States or municipalities, whose contracts are necessarily made in subjection to the dominant power of Congress."

Such "dominant power" of State legislatures over municipal obligations was subsequently recognized by the Supreme Court in *Faitoute*. 
The remaining cases cited by appellant have even less to do with the issues at hand.

Thus, Groves v. Board of Public Instruction, 109 F.2d 522 (5th Cir. 1940), which appellant claims to be an "a fortiorari" case, involved a statute which affirmatively deprived a municipality of a large measure of the taxing authority on which it depended for payment of its obligations. (App. Br. 28-29.) Similar facts were presented in United States v. City of Quincy, 4 Wall. 535 (1867), Wolff v. New Orleans, 103 U.S. 358 (1881), and Louisiana v. Pillsbury, 105 U.S. 278 (1882).* (App. Br. 21-23.) In contrast, the Moratorium Act in no way impairs the City's taxing authority. Every tax which the City was previously empowered to levy or collect -- including ad valorem real estate taxes -- it retains the authority to levy and collect today. Indeed, the Moratorium Act was followed immediately by legislation broadening the City's powers of taxation.**

Appellant simply fails to recognize the distinction between a statute which destroys a municipality's pre-existing ability to meet its obligations as they mature and a statute, like the Moratorium Act, calculated to cope with and cure a present inability to

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* Wolff and Louisiana illustrate the pitfalls encountered in relying, as does appellant, upon ancient cases. Both held unconstitutional, as an impairment of contracts, the legislative repeal of a State tax on "real property and slaves." By the same logic, which appellant here adopts, the abolition of slavery would be unconstitutional on the same ground.

** During the same Extraordinary Session at which the Moratorium Act was passed, the Legislature enacted legislation increasing the City cigarette tax (L. 1975, ch. 877); imposing a City estate tax (L. 1975, ch. 879); and increasing the City personal and corporate income taxes (L. 1975, chs. 881, 887). This was in addition to tax increases of some $325 million imposed by the City in July, 1975. (A155; RA20-21, 57)
do so. That difference, however, is critical from a constitutional standpoint. Thus, in the City of Quincy case, 4 Wall. at 554, supra, cited by appellant (App. Br. 21), the Supreme Court found that, "[b]ut for the Act [at issue] there would be no difficulty in enforcing" the bonds. Palpably, that is not the situation here. Indeed, the cases, notably Faitoute and the Port Lee case cited by appellant (App. Br. 27-28), demonstrate that the process of repayment is likely to take longer in the absence of a moratorium than with the moratorium in place. See pp. 42-44, supra.)

None of the additional cases on which appellant relies involves either the taxing power, the power to contract indebtedness or the emergency police power of the State. Notably, Sturges v. Crowninshield, 17 U.S. (4 Wheat) 122 (1819), supra, and Fletcher v. Peck, 6 Cranch 87 (1810) -- which appellant terms "the landmark Contract Clause opinion" -- as well as the City of Quincy case, supra, were all expressly considered by the Supreme Court in Blaisdell, and were held inapplicable to emergency exercises of a State's police power. As the Court stated:

"None of these cases, and we have cited those upon which appellant chiefly relies, is directly applicable to the question now before us in view of the conditions with which the Minnesota statute seeks to safeguard the interests of the mortgage-purchaser during the extended period. And broad expressions contained in some of these opinions went beyond the requirements of the decisions, and are not controlling." (290 U.S. at 434; emphasis supplied.)

Wood v. Lovett, 313 U.S. 362 (1941), which appellant acknowledges to be similar to Fletcher v. Peck, supra, is equally inapposite --- and, if anything, supports the judgment below. (App. Br. 24.) In Wood, the Court held that repeal legislation which restored
the rights of delinquent taxpayers to set aside forced sales of their
property by the State -- a right which had been abrogated by statute
earlier in the Depression to stimulate such sales and the resultant
revenues for the State -- could not be applied retroactively. How-
ever, it was the original statute, rather than the repeal legisla-
tion, which subordinated the rights of property owners to the finan-
cial needs of the State. And the effect of the Court's decision in
Wood was to perpetuate that original statute.

Nor is there any precedential value in the State court
cases cited by appellant. (App. Br. 29-30.) None involved the use
of the State's emergency police power or a direct challenge to the
State's authority to regulate contracts to protect the health, safety
or welfare of its citizens. Moreover, insofar as the cases involved
State or municipal obligations, those obligations -- unlike the City
notes here -- were secured by specific collateral (such as a lien on
land or on specific tax assessments levied against the property
owners benefitting from the issuance of the obligations), not by a
pledge on the general credit of the municipality. In each case, the
security -- unlike the City's general credit here -- was adequate to
meet the obligations, and it was only the State's action which im-
paired that security. Finally, whatever their tangential relevance
here, each of the State court cases cited by appellant pre-dates
the decision of the New York Court of Appeals in *East New York Sav.
Bank v. Hahn*, 293 N.Y. 622 (1944), aff'd, 326 U.S. 230 (1945), supra,
which expressly upheld legislation similar to the Moratorium Act.

* * *

In sum, the case law, as it presently exists, fully supports the
constitutionality of the Moratorium Act under the Contract Clause.
Appellant's attempt to resuscitate the doctrines (real or imagined) of a bygone era is unavailing.

II.

THE MORATORIUM ACT TAKES NO PROPERTY IN VIOLATION OF THE UNITED STATES CONSTITUTION OR THE NEW YORK STATE CONSTITUTION

Appellant's contention (App. Br. 34-37) that the Moratorium Act constitutes "a taking of property" in violation of the Fourteenth Amendment to the United States Constitution* and Article 1, § 7, of the New York State Constitution (App. Br. 36) -- a contention which, incidentally, appellant did not make below -- is answered in the first instance by the same decisions which we cited to dispose of the contention that the Act impairs the obligation of contracts.

The relationship of the Contract Clause to the Fifth and Fourteenth Amendments to the United States Constitution was recently explored in the opinion of the Superior Court of New Jersey in United States Trust Co. v. State of New Jersey, 134 N.J. Super. 124, 338 A.2d 833 (1975), discussed at pp. 30-31, supra. There, as previously noted, holders of Port Authority bonds challenged the legislative repeal of a 1962 New York-New Jersey covenant prohibiting the use of Port Authority revenues for mass transit. Plaintiffs contended that such legislative action constituted an "impairment"

* While appellant cites only the Fourteenth Amendment (App. Br. 36), we assume the reference is actually to the Fifth Amendment's prohibition -- identical to that in Article I, § 7, of the State Constitution -- against the taking of private property without just compensation, which prohibition is made applicable to the States by the Fourteenth Amendment.
or "taking" of the security of their bonds in violation of the Contract Clause, the Fifth Amendment and the Fourteenth Amendment to the United States Constitution. The Court rejected the Contract Clause argument as unsound -- and expressly held that such rejection disposed automatically of plaintiff's remaining constitutional claims. In the words of the Court:

"[T]he test of constitutional validity as applied to repeal legislation is the same under the Contract and Due Process Clauses, i.e., if an unlawful impairment has occurred there has been a 'taking', and if not, then there is no taking." (134 N.J. Super. at 182 n.36.)

In reaching that conclusion, the Court relied, inter alia, on the decision of the United States Supreme Court in Veix v. Sixth Ward Bldg. & Loan Ass'n, 310 U.S. 32 (1940), discussed at pp. 29-30, supra. In Veix, after rejecting plaintiff's Contract Clause contention in circumstances closely analogous to the present case, the Supreme Court made short shrift of plaintiff's Fourteenth Amendment claims, simply stating:

"Separate consideration of the objection to the legislation under the due process and equal protection clauses of the Fourteenth Amendment seems wholly unnecessary." (310 U.S. at 41.)

And in Fairhouette Iron & Steel Co. v. City of Asbury Park, 316 U.S. 502 (1942), supra -- the definitive Supreme Court precedent in the area -- the Due Process issue was again apparently found unworthy of separate treatment, although presented prominently in plaintiff's brief to the Supreme Court.

The settled principle that legislation which does not violate the Contract Clause likewise does not violate the Fourteenth Amendment is particularly appropriate in the present case. For an
analysis of the "taking of property" argument on its own merits, beginning with a threshold examination of what has been "taken" by the legislation challenged here, quickly reveals that there is no violation of the Fourteenth Amendment or of Article 1, § 7, of the State Constitution.

Specifically, the Moratorium Act, as previously noted, does not relieve the City of its obligation to pay principal and interest on its notes. Nor does the Act prevent or restrict the City's use of any of the resources on which the fulfillment of its obligations depends. Rather, the Moratorium Act merely suspends temporarily the noteholders' access to the courts to enforce their notes,* in order to provide the time necessary to fashion and implement a plan whereby the City's ability to meet its obligations can be restored, and City noteholders thereby assured ultimate repayment of their obligations. Such suspension of judicial remedies does not give rise to a "taking" of constitutional dimensions.

The right of recourse to the courts to enforce general obligations of a municipality which is incapable of paying those obligations, as the Supreme Court recognized in Faitoute (316 U.S. at 310), is no more than "an empty right to litigate." The Moratorium Act does no more than suspend that "empty right." Appellant's claim that, as a result of the Moratorium Act, its property has been "taken" without just compensation, so as to transgress the Federal

* Obviously, as demonstrated by this very litigation, City noteholders are not barred access to the courts to contest the genuineness of the emergency which caused the Legislature to act, or the reasonableness of the Legislature's response in enacting the challenged Moratorium Act.
and State Constitutions, is thus theoretical at best. And, as the Supreme Court went on to observe in *Faitoute* (316 U.S. at 514), the Constitution is "intended to preserve practical and substantial rights, not to maintain theories."

The fundamental flaw in appellant's "taking of property" argument -- like that which undermines its Contract Clause contention -- is that appellant confuses cause and effect. Appellant thus ignores the distinction between the technical and insubstantial "deprivation" (of an "empty right to litigate") attributable to the Moratorium Act, and the real and substantial deprivation (of timely payment of the notes) attributable to the intervening economic factors which, independent of any legislative action, prevent the City from discharging its obligations to noteholders at the present time. The relevance of this distinction was recognized by the Supreme Court in *Faitoute*, supra at 511, when it stated:

"Impairment of an obligation means refusal to pay an honest debt; it does not mean contriving ways and means for paying it. The necessity compelled by unexpected financial conditions to modify an original arrangement for discharging a city's debt is implied in every such obligation for the very reason that thereby the obligation is discharged, not impaired."

This rationale is readily adapted to defeat appellant's newly conceived objection to the Moratorium Act based on the Fourteenth Amendment to the United States Constitution and Article 1, § 7, of the State Constitution: the Supreme Court's logic is not disturbed by substituting the word "taking" for "impairment". Appellant's attempt to bifurcate what is essentially one constitutional claim, and to achieve under the general language of the Fourteenth Amendment that which it could not achieve below under the specific language of the Contract Clause, must therefore fail.
The cases cited by appellant do not advance its cause. (App. Br. 36.) Neither Phelps v. United States, 274 U.S. 341 (1927); Panhandle Eastern Pipe Line Co. v. State Highway Comm'n, 294 U.S. 613 (1935); nor City of Buffalo v. Clement Co., 28 N.Y.2d 241 (1971), involved emergency legislation of a type like the Moratorium Act, nor demands for the fulfillment of obligations in the face of intervening events rendering literal performance of such obligations impossible. None of the cases, therefore, suggests that a failure of a municipality to meet its obligations in the compelling circumstances found by the Legislature to exist here, or the passage of emergency moratory legislation intended to cope with, and hopefully to correct, those circumstances in order to permit the municipality ultimately to meet its obligations, constitutes an unconstitutional "taking" in any way.

Similarly, appellant's discussion of interest rates on other obligations and its reference to judicial determination of the adequacy of interest rates (App. Br. 35-37) are wholly inapposite, for here the parties have, in effect, contracted with respect to the rate of interest payable after accrual of the noteholders' right to payment. The fact is, as previously noted (pp. 7-8, 11, supra), that General Municipal Law, § 3-a, was applicable to, and thus formed a part of, each and every note issued by the City.* That section, by providing that interest on "accrued claims" against a municipality would be payable at a rate of 3% per annum, expressly established the rate of interest which City noteholders would be entitled to

* Appellant concedes that the noteholders' "contracts" with the City were "augmented by an array of State statutory provisions in force at the time the notes were issued. . . ." (App. Br. 9 n.) General Municipal Law, § 3-a, was one of them.
receive after maturity of their notes in the event the City did not pay the principal of the notes at that time. The Moratorium Act provides the noteholders with 6% interest, twice the required rate. Under the circumstances, then, such rate of interest cannot be termed "unjust".

Appellant's observation that, if not for the Moratorium Act, the noteholders could pursue their remedies and obtain a judgment against the City is, we submit, altogether beside the point. (App. Br. 37.) As previously indicated, any judgments obtained by noteholders against the City would likely remain unsatisfied throughout the moratorium period, if not longer. (See pp. 5-6, 11-15, supra.) And Section 3-a of the General Municipal Law, which would be applicable during such period, also limits the rate of interest on "judgments" against the City to 3%.

III.

THE MORATORIUM ACT DOES NOT VIOLATE THE PROVISIONS OF ARTICLE 8 OF THE NEW YORK STATE CONSTITUTION

Appellant's next assertion is that the Moratorium Act must be held invalid as violative of Sections 2, 10 and 12 of Article 8 of the State Constitution. (App. Br. 38-42.) The Court below found appellant's reliance on these provisions to be misplaced. (A17-18) Appellant simply misreads the language or misunderstands the effect of the State constitutional provisions in question.

A. Article 8, § 2: "Faith and Credit"

Thus, appellant asserts that the Moratorium Act violates Article 8, § 2, ¶ 2, of the State Constitution, which provides that
"No indebtedness shall be contracted by any . . . city . . . unless such . . . city . . . shall have pledged its faith and credit for the payment . . . thereof." But, as its language reflects, this provision merely prohibits the City from contracting indebtedness without pledging its "faith and credit" for payment. There is no question that the City did, in fact, make such pledge when it issued the notes held by plaintiff and others. Appellant does not deny that fact and, indeed, the very exhibits which appellant submitted below evidence the making of the pledge. (A92-106)

Nothing in the Moratorium Act relieves the City of liability on its outstanding notes or of its pledge of "faith and credit" with respect to those notes. On the contrary, as the Court below recognized (A17), the Moratorium Act provides for the payment of interest and contemplates the eventual payment in full of the principal of the notes for which the "faith and credit" of the City have been pledged. Indeed, the Act is prefaced by a declaration that the Legislature "recognizes and insists that the pledge of the 'faith and credit' of the city to the payment of its obligations must be respected." (A48) However, just as the United States Supreme Court has made clear that the first and foremost requirement in honoring the Federal constitutional Contract Clause is the preservation of the contracting municipality, even where that can only be achieved by relaxing the duty of strict compliance with contracts, so too must the State constitutional "faith and credit" pledge be interpreted so as to best preserve the value of the municipal obligation in light of existing circumstances. See Paitoute Iron & Steel Co. v. City of Asbury Park, 316 U.S. 502, 509-11 (1942); discussed at pp. 27-28, 32-34, supra.
Although appellant seems to believe otherwise, the "faith and credit" clause does not require the City to, in effect, commit governmental suicide. Cf. *Kennedy v. Mendoza-Martinez*, 372 U.S. 144, 160 (1963). It does not command that the City impose unconscionable and uncollectible taxes, or destroy its tax base, or eliminate vital services in order to pay its indebtedness -- and appellant cites no authority so stating. (App. Br. 39.) The pledge of "faith and credit", as the words indicate, requires no more than that the City make a good faith effort -- which it has made and is making (A154-66; RA33-58) -- and use its credit -- which presently is impaired (A167; RA16-17) -- to pay its indebtedness as soon as practicable, given its overall financial condition and its other obligations to its citizens. See Moak, *Administration of Local Government Debt*, pp. 200-201 (1970); *Fairoute Iron & Steel Co. v. City of Asbury Park*, 316 U.S. 502, 509, 512 (1942), *supra*. The Moratorium Act was passed by the State Legislature for the very purpose of helping the City carry out its pledge or, in other words, as the Court below put it, "to give the City time to put its financial house in order so that it could fully meet its obligations." (A17)

In short, the Moratorium Act does not involve any repudiation or violation of the "faith and credit" provision of the State Constitution.

B. *Article 8, §§ 10 and 12*

Appellant's reading of Sections 10 and 12 of Article 8 of the State Constitution, as the Court below held (A17), tortures the English language. Those sections grant the City the unrestricted power to levy real estate taxes to pay its indebtedness. (See p. 19, *supra*.) Neither of the provisions is infringed by
the Moratorium Act. Nothing in the Act restricts the City's authority
to levy, collect and disburse taxes.

Section 10, contrary to appellant's assertion, does not
"command" the City to impose real estate taxes in any amount for
any purpose. (App. Br. 39.) This is clear simply from a reading
of the entire section, rather than of clauses plucked from the sec-
tion at random. Thus, Section 10 is headed "Limitations on amount
to be raised by real estate taxes for local purposes; exceptions."
As its text reflects, the section merely establishes ceilings on
the amounts which various municipalities in the State can raise by
means of real estate taxes. Appellant would have this Court convert
a constitutional limitation on the power of the City to impose taxes
into an express command to exercise that power. In any event, it is
difficult, if not impossible, to understand how the Moratorium Act,
which suspends the right of City note holders to sue to enforce their
obligations in the courts, can be said to violate a constitutional
provision which authorizes and sets limits on the taxing powers of
municipalities.*

The same is true with respect to appellant's argument
based on Section 12 of Article 8. (App. Br. 40.) That section
provides that the Legislature shall not "restrict" the power of
a municipality to levy real estate taxes to pay its indebtedness.
(See p. 19, supra.) But the Moratorium Act imposes no restriction
of any kind on the City's taxing authority. On the contrary,

* Appellant's assertion that the City might improperly allocate its
real estate tax revenues is, of course, pure speculation at this
point and, in any event, is irrelevant to the issue of the constitu-
tionality of the Moratorium Act. (App. Br. 15, 40-41.)
despite the Moratorium Act, the City is now, and will remain during the period of the moratorium, free to levy taxes on real estate. Appellant misses this point (App. Br. 40), but the Court below recognized it. (A17) And here, again, it is difficult, if not impossible, to understand how the Moratorium Act, which suspends the right of City noteholders to sue to enforce their obligations in the courts, can be said to violate a constitutional provision which prohibits legislative restrictions on the taxing power of municipalities.

C. Article 8, § 2

Appellant's last claim based upon Article 8 suffers from the same infirmity as its prior claims — i.e., a misreading of the pertinent State constitutional provisions. Appellant contends that Article 8, § 2, ¶ 2, of the State Constitution mandates that "City notes shall, under no circumstances, remain outstanding and unpaid later than the second fiscal year succeeding the fiscal year in which such notes were issued." (App. Br. 41.) This is not so, as the Court below held. (A18)

The language which appellant misconstrues provides that:

"Except for . . . indebtedness contracted to be paid in one of the two fiscal years immediately succeeding the fiscal year in which such indebtedness was contracted, all . . . indebtedness and each portion thereof from time to time contracted, including any refunding thereof, shall be paid in annual installments, the first of which, except in the case of refunding of indebtedness heretofore contracted, shall be paid not more than two years after such indebtedness or portion thereof shall have been contracted, and no installment, except in the case of refunding of indebtedness heretofore contracted, shall be more than fifty per centum in excess of the smallest prior installment." (Emphasis supplied.)

Thus, the provision expressly exempts from its coverage at the outset "indebtedness contracted to be paid in one of the two fiscal
years immediately succeeding the fiscal year in which such indebtedness was contracted" -- which includes all outstanding City notes, since they were issued with maturities of less than two years. (A100-03) It was for this reason that the Court below correctly concluded that this provision "does not apply to City short term notes." (A18)

The language which is applicable here is not the two-year provision cited by appellant, but another provision in the same section of the State Constitution. Thus, Article 8, § 2, ¶ 4, provides that

"certificates or other evidence of indebtedness issued in anticipation of the collection of taxes or other revenues [such as the outstanding City notes] . . . which are not retired within five years after their date of original issue",

must be treated on the same terms as outstanding City bonds -- i.e., "the first revenues thereafter received" must be set aside to pay such obligations if the municipality fails to appropriate funds for their redemption. (See p.19, supra; emphasis supplied.)

This constitutional provision is in no way violated by the Moratorium Act. The Act suspends suits to collect on outstanding City notes -- the earliest of which was issued on or about December 13, 1974 -- until November 15, 1978, a period of less than four, not five, years. And, of course, nothing in the Act precludes earlier payment of its notes by the City if circumstances permit.

No doubt recognizing that the language of Article 8, § 2, of the State Constitution does not support its position, but expressly defeats it, appellant ignores the plain language. Instead, appellant purports to rely on what it terms the "fair intendment" of
the provision (App. Br. 41) and its own unsupported theory as to the purpose of the framers of the State Constitution. (App. Br. 42.) However, appellant offers no logical basis on which this Court might reasonably conclude that this constitutional provision was intended to mean anything other than what it says. Moreover, appellant's attempt to find the "intent" of the State Constitution by reference to a section of the Local Finance Law is doomed to failure. (App. Br. 41-42.) Not only was that section enacted after the constitutional provision,* but a statute cannot overrule the plain meaning of a constitutional provision. Nor can this Local Finance Law provision supersede the later Moratorium Act, whose provisions are expressly made operative "notwithstanding any inconsistent provisions of any law, general, special or local." (As0)

It is difficult, if not impossible, to understand how the Moratorium Act can violate a constitutional provision -- Article 8, § 2, ¶ 2 -- which expressly exempts from its coverage the only City notes affected by the Act.

*  *  *

In sum, contrary to appellant's claims, the Moratorium Act does not violate, conflict with or purport to alter any provision of this State's Constitution. Thus, there is no basis for any claim of invalidity of the Act under that Constitution.

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* Local Finance Law, § 25.00(f) was enacted in 1942; while Article 8, § 2, ¶ 2, of the State Constitution was adopted in 1938.
IV.

THE MORATORIUM ACT DOES NOT VIOLATE THE EQUAL PROTECTION CLAUSE OF THE UNITED STATES CONSTITUTION OR THE NEW YORK STATE CONSTITUTION

Appellant next contends that the Moratorium Act violates the Equal Protection Clause of the Fourteenth Amendment to the United States Constitution and of the State Constitution because it "applies to short-term City notes" but "does not apply to City bonds." (App. Br. 43-46.)


Here, as the Court below recognized (A19), the State Constitution, for one thing, not only includes a reasonable basis for the different classification of City notes and bonds, but requires it. For the fact is that, contrary to appellant's claim, City note-holders and bondholders just do not "stand in the same creditor position" as a matter of State constitutional law. (App. Br. 43.)

Thus, as previously noted, Article 8, § 2, ¶ 4, of the State Constitution grants bondholders a right to "first revenues" of a municipality where sufficient funds are not appropriated to
pay the principal of their bonds, while expressly withholding such right from note holders for five years. (See pp. 19, 59, supra.)

This is hardly a "meaningless distinction". (App. Br. 45.) On the contrary, the "first revenues" provision is, in effect, a State constitutional guarantee of timely payment of City bonds, which is not applicable to City notes.

Even apart from the basic State constitutional distinction, sound practical considerations justify the legislative differentiation between notes and bonds challenged by appellant. For instance, debt service (i.e., principal and interest) on City notes maturing in the 12-month period commencing December 11, 1975 -- without including the approximately $2.2 billion in principal amount of notes presently held by MAC -- totals a staggering $3.149 billion,* all of which must be paid from income received in that period. By contrast, the annual debt service for City bonds is substantially lower, and is partially payable out of segregated sinking funds. (A86, 109, 166-67, 170) Indeed, as appellant conceded below, only approximately $530 million** in principal amount of City bonds will mature in the City's fiscal year ending June 30, 1976 (RA62), compared to

* As previously noted (pp. 10-11, supra), the $1.6 billion figure relied upon by appellant in making its equal protection argument is misleading. That figure represents only the principal amount of City notes held by "the public" before MAC's exchange offer. (App. Br. 43.) It does not include the more substantial amount of City notes which are held by entities such as the 11 New York Clearing House Banks and City pension funds -- and which also come due for payment during the next year. (A167-68; RA59-61) These entities only "voluntarily extended" the due dates of their City notes because of the existence of the Moratorium Act. (App. Br. 43 n.; A168.)

** The $2.75 billion figure cited by appellant in his brief on this appeal is the principal amount of bonds maturing in the next three years. (App. Br. 43.)
the $2.9 billion in principal amount of City notes (exclusive of
notes held by MAC) maturing in the next year. (Al66) In short, as
found by the Legislature, while the City lacks the capability to
meet its short-term (note) obligations, it apparently has the capa-
ability to meet its long-term (bond) obligations despite the finan-
cial crisis. (Al07)

The Court below took note of -- and, indeed, based its
decision on -- just these legal and factual differences between
City notes and bonds. (Al9) Contrary to appellant's assertion,
its equal protection argument was not treated below in "a cryptic
and unstudied fashion". (App. Br. 44.) Rather, the Court rejected
the argument based upon the following unassailable finding:

"There are many differences between notes and bonds.
Article 8 of the State Constitution is replete with dif-
fences in the rights of and obligations to bondholders
and noteholders. The city has a problem in meeting its
short term (note) obligations of over $3. billion, while
it is capable of meeting its long term indebtedness.
Therefore, the Legislature imposed a moratorium on the notes
and not on the bonds. This can hardly be considered a
constitutional violation of equal rights." (Al9)

Under all the circumstances, then, the decision of the Legi-
slature to impose a moratorium with respect to City notes, but not
bonds, can hardly be deemed unreasonable for purposes of the Equal
Protection Clause. Rather, the fact that, in terms of principal
amount, nearly six times more City notes than bonds would have to
be (but could not be) paid by the City in the next year, in and of
itself, provides the "real and substantial basis" which appellant
says must exist to uphold the State Legislature's determination to
exercise its police powers so as to suspend the enforcement of notes
alone. (App. Br. 44.)
Once again, as the Court below noted (A19), the Supreme Court's decision in *Home Bldg. & Loan Ass'n v. Blaisdell*, 290 U.S. 398 (1934), supra, is in point. There, in rejecting a similar argument that the Minnesota moratorium law discriminated unfairly between mortgages and other debt instruments, the Supreme Court concluded (at 448):

"Nor do we think that the statute denies to the appellant the equal protection of the laws. The classification which the statute makes cannot be said to be an arbitrary one. [Citations omitted.]"

V.

THE MORATORIUM ACT DOES NOT VIOLATE THE FEDERAL BANKRUPTCY ACT

Appellant's last argument is that the Moratorium Act violates Section 83(i) of the Federal Bankruptcy Act. (App. Br. 46-49.) This argument was rejected by the Court below, and properly so; it is clearly erroneous. (A18-19).

Section 83(i), 11 U.S.C. § 403(i), provides that no State law

"prescribing a method of composition of indebtedness of [municipalities] shall be binding upon any creditor who does not consent to such composition. . . ."

By its own terms, then, Section 83(i) has no bearing on State legislation which (1) does not prescribe a method of composition, and (2) does not compel non-consenting creditors to be bound to a composition. On both these points, the section has no relevance to the present case.

Appellant mistakenly asserts that Section 83(a) of the Bankruptcy Act, 11 U.S.C. § 403(a), contains a "statutory definition"
of the term "composition". (App. Br. 47-48.) However, Section 83(a), as its very language reflects, merely enumerates the kinds of additional provisions which "may" be included in a "plan of composition", without attempting to define either "composition" or "plan of composition."

"Composition" is a term of art, having a definite and precise meaning. It is, in short, an arrangement whereby "a debtor is able to discharge his debts by only partially paying them." In re Mayorga, 355 F.2d 89, 90 (4th Cir. 1966). This definition, and thus the limitation which it places on the scope of Section 83(i), was recognized by Congress when it enacted the statute in 1946. Specifically, the Report of the House Committee on the Judiciary which considered the bill embodying the relevant provision of Section 83(i) recites that Congress' intent was to prevent disparate State legislation pursuant to which holders of municipal obligations "are required to surrender or cancel their obligations." H.R. Rep. No. 2246, 79th Cong., 2d Sess., U.S. Code Cong. Serv. 1246, 1249 (1946).

Nothing in the Moratorium Act empowers the City to discharge or cancel its notes or to force the holders to surrender their notes -- other than by paying them in full. The Moratorium Act merely suspends the right of City noteholders to sue to enforce their obligations in the courts for a limited period. At most, the Act permits an "extension" of indebtedness, which is different from a composition and is not within the statutory proscription of Section 83(i).*

* Plaintiff can hardly argue that the Moratorium Act constitutes a "composition" under Section 83(i) in light of the fact that the Exchange Offer required by the Act only binds consenting noteholders. (A51)
This is no mere technical distinction. In Perry v. Commercial Loan Co., 383 U.S. 392, 398-99 (1966), the Supreme Court observed that:

"Extension plans . . . differ materially from . . . plans by way of composition, all of which contemplated only a partial payment of the . . . debt. Indeed, under an extension plan, the [petitioner] who makes the required payments will have paid his debts in full . . . . " (Emphasis supplied.)

Further, the Federal Bankruptcy Act itself distinguishes between extensions, on the one hand, and compositions, on the other hand. See, e.g., Bankruptcy Act, § 606(6), (7), 11 U.S.C. § 1006(6), (7). Appellant's suggestion that the Perry case and Bankruptcy Act, § 606, are somehow unique in their description of a "composition" is readily negated. (App. Br. 48.) See Black's Law Dictionary, 357 (4th rev. ed. 1968) ("composition" is an "agreement" between a debtor and his creditors "whereby the latter, for the sake of immediate or sooner payment, agree to accept a dividend less than the whole amount of their claim"); In re Goldberg, 97 F. Supp. 75, 76 (S.D.N.Y. 1951) (a "composition" is a "contract" between a debtor and his creditors "by which he obtains a settlement of the claims against him by paying an agreed sum into court for distribution to such creditors" and "receives as consideration for his agreement what is in effect a discharge"). Nothing of the sort is provided by the Moratorium Act.

Notably, despite the fact that plans of extension are different from plans of composition, and that plans of extension receive separate recognition in the Bankruptcy Act -- and have since before 1946, when Section 83(i) was enacted in its present form -- Section 83(i) prohibits only State plans of composition. The omission of any limitation on the power of States to extend obligations in times of
emergency must be presumed to have been conscious and deliberate on the part of Congress.

Indeed, were Section 83(i) to be given a broader construction -- one beyond that which its express terms require -- doubts would be raised about its constitutional validity. The history of municipal bankruptcy legislation is one of tension between Federal jurisdiction and State sovereignty. Thus, in Ashton v. Cameron County Water Improvement Dist., 298 U.S. 513 (1936), the first municipal bankruptcy act was held to be an unconstitutional encroachment on State sovereignty merely because it empowered municipalities to file for relief without State approval. The present act (Chapter IX) was upheld only because the Supreme Court found that Congress had been "especially solicitous to afford no ground" for the "objection" that application of the new act to political subdivisions of the State "'might materially restrict [the State's] control over its fiscal affairs.'" United States v. Bekins, 304 U.S. 27, 50 (1938).

The unique and expansive construction which appellant would place on Section 83(i) -- effectively precluding the State from taking any action to avert a municipal financial disaster -- would, we submit, result in just the sort of unnecessary interference with State sovereignty that the Supreme Court condemned in Ashton. No such reading of the section is warranted here.

Appellant also suggests that the Moratorium Act amounts to a "composition" because the Act "reduces the interest payable to noteholders during the extension period." (App. Br. 48-49.) As previously indicated, there is no such reduction in interest. (See pp. 7-8, 11, 53-54, supra.) Thus, the relevant City notes pro-
vide that their stated rate of interest shall be paid "at maturity". (A100-03) This provision of the notes is honored by the Moratorium Act, which requires that all noteholders be paid interest "at the rate stated in such short-term obligation to the date of its maturity." (A51, 53) After the maturity date, however, if the note is not paid -- as is the case here -- the noteholder merely has an "accrued claim" against the City, on which the rate of interest is limited by statute to 3%. Gen. Munic. Law, § 3-a. Appellant, therefore, misses the point that, by requiring 6% interest after the stated maturity date of the City notes, the Moratorium Act actually increases the interest otherwise payable to the noteholders. Accordingly, there is no "composition" of indebtedness.

It is for this reason that In re Hoag, 62 F. Supp. 527 (D. Vt. 1945), and American United Life Ins. Co. v. Haines City, 117 F.2d 574 (5th Cir. 1941), cited by appellant, are inapplicable. (App. Br. 49.) Unlike the situation in Hoag, the City noteholders will not, as a result of the Moratorium Act, receive "a lesser rate of interest during an extension period" than they would have received during such period absent the Act. (App. Br. 49.) And, unlike the situation in Haines, the City noteholders are not being forced by the Moratorium Act to accept payment for "past due interest and accrued interest on past due bonds . . . on a lower percentage basis" (117 F.2d at 575). These two cases simply have no relevance here.

Finally, appellant accurately states that Section 83(i) was adopted to overcome an aspect of the Supreme Court's decision in the Faitoute case, supra. (App. Br. 47 n.) But appellant misunderstands, or at least misstates, the particular aspect of that decision which Congress sought to overrule. As previously noted
(pp. 27-28, 35-38, supra), the Supreme Court in Paitoute upheld not only a provision of a State statute suspending the right of holders of municipal obligations to seek to enforce those obligations in the courts, but also a provision permitting a municipality to adopt a "'plan of adjustment or composition of the claims of all creditors'" which would be binding on all creditors "[i]f approved by 85 per cent in amount of the creditors" (316 U.S. at 504). The latter provision goes far beyond anything in the Moratorium Act -- and was the only type of "composition" plan which Congress sought to, and later did, prohibit by Section 83(i).

In sum, the express language of Section 83(i), its legislative history and the case law all establish that the Moratorium Act does not violate the Federal Bankruptcy Act.

CONCLUSION

The judgment entered below should be affirmed.

Dated: February 26, 1976

Respectfully submitted,

PAUL, WEISS, RIFKIND, WHARTON & GARRISON
Attorneys for Respondent
Municipal Assistance Corporation for the City of New York

Of Counsel
Simon H. Rifkind
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Jonathan Siegfried
January 30, 1976

Ms. Judith Chazen
Municipal Assistance Corporation
For the City of New York
Two World Trade Center
New York, New York 10047

Flushing Nat. Bank Cases

Dear Ms. Chazen:

Here is the litigation information you requested:

Flushing I (alleged diversion of sales tax revenues)

1. Date of oral argument on motions by MAC and State defendants for summary judgment: November 25, 1975 (Sup. Ct., N.Y. Co., Hyman Korn, Justice).

2. Date of N.Y. Supreme Court decision granting defendants' motions for summary judgment: December 3, 1975.

3. Date judgment entered: January 16, 1976.

No notice of appeal filed as yet.
Flushing II (challenge to Note Moratorium Act):

1. Date of oral argument on motions by MAC, State and City defendants for summary judgment and on plaintiff's motion for a preliminary injunction: December 19, 1975 (Sup. Ct., N.Y. Co., Harold Baer, J.)

2. Date of N.Y. Supreme Court decision granting defendants' motions and denying plaintiff's motion: December 23, 1975.

3. Date judgment entered: December 24, 1975.


5. Date of oral argument on plaintiff's renewed motion in the Appellate Division for a preliminary injunction: December 29, 1975.

6. Date of decision denying plaintiff's injunction motion in the Appellate Division: December 29, 1975 (decided from the bench).

I hope the above information is sufficient for your purposes. If I can be of any further assistance to you in this regard, please do not hesitate to call.

Sincerely,

Dean B. Allison

DBA/si

By Hand
January 22, 1976

James R. Keegan, Esq.
Municipal Assistance Corporation
For the City of New York
2 World Trade Center
New York, New York

MAC

Dear Jim:

Enclosed herewith as you requested are two print-outs sent to me by Park Benjamin showing principal and interest payments for each debt service for the Series A-AA Bonds (one showing unaccrued interest deducted and one showing accrued interest included).

Also, enclosed is a schedule from Park showing the principal and interest for each debt service on the Series 1-4 Bonds of the corporation issued pursuant to the exchange offer.

Best regards.

Sincerely,

James M. Dubin
James Keegan, Esq.
Municipal Assistance Corporation
Two World Trade Center
New York, New York

Agreement of November 26, 1975

Dear Jim:

Enclosed are two fully executed copies of the Amended and Restated Agreement of November 26, 1975. We have retained one executed version here but I thought that you might wish to have one for the MAC files and one for the EFCB.

Things are as ever here, I hope they are well with you too.

Sincerely,

[Signature]

Marschall Smith

Enclosures

BY HAND