

MEMORANDUM

TO: Edward I. Koch
MAYOR

FROM: Allen G. Schwartz
Corporation Counsel

RE: Federal "Standby Guarantees"

DATE: August 11, 1980

You have asked me to determine whether there is any legal impediment under the New York City Loan Guarantee Act of 1978 (the "Act")¹ or the Agreement to Guarantee dated as of November 15, 1978 among the United States, The City of New York (the "City") and others (the "Agreement to Guarantee") to the issuance by the Secretary of Treasury (the "Secretary") of Standby Guarantees during the City's 1981 and 1982 fiscal years. For the reasons discussed below, I have concluded that (i) no condition exists at this time which precludes the Secretary from issuing such guarantees and (ii) a number of factors suggest the desirability of the Secretary's issuing such guarantees under the loan guarantee program.

As you know, Standby Guarantees are defined in the Agreement to Guarantee as "Guarantees issued or to be issued pursuant to this Agreement during the 1981 Fiscal

Year or the 1982 Fiscal Year,"² Pursuant to the Agreement to Guarantee, Standby Guarantees covering up to \$900 million of long-term City indebtedness may be issued.³

A. "Credit Elsewhere" Test

Section 103 of the Act lists several conditions of eligibility which must be satisfied prior to the issuance of Standby Guarantees. Among these conditions, the most significant potential obstacle is the "credit elsewhere" test contained in Section 103(2) of the Act, pursuant to which the Secretary may issue Standby Guarantees only if:

"...the Secretary determines that the city is effectively unable to obtain credit in the public credit markets or elsewhere in amounts and terms sufficient to meet the city's financing needs."

Since the Municipal Assistance Corporation For The City of New York ("MAC") can apparently sell an aggregate of \$800 million of its bonds in FY 1981 and 1982,⁴ it may be contended that the City has credit elsewhere and is therefore ineligible for Standby Guarantees. Indeed, Senators William Proxmire and Jake Garn of the Senate Committee on Banking, Housing, and Urban Affairs wrote to the Secretary on June 2, 1980 that "it is clear from the statutory language that so long as MAC has the capacity to meet the city's financing needs in 1981 and 1982, no further Federal guarantees can be issued". Although MAC is a State agency established as a financing agent for the City, a careful reading of the legislative history and the Agreement to Guarantee (executed

pursuant to the Act) reveals that the "credit elsewhere" test applies solely to the ability of the City to obtain credit (which it currently cannot do except in inadequate amounts)⁵ and that MAC's capacity to raise funds need not be considered.

The key reference on this subject may be found in the Conference Report which reconciled the Senate and House versions of the legislation. In the section discussing the "credit elsewhere" test, the following language appears:

Credit Availability

"The House bill required, as a condition to the making of guarantees, that the Secretary determine that the city is effectively unable to obtain credit through traditional sources in amounts and terms sufficient to meet its financing needs. The Senate amendment required the determination by the Secretary that credit was not otherwise available to the city or a financing agent on reasonable terms.

The conference report contains the House provision."⁶

Since the Conference Report specifically rejected the Senate version of the legislation, which would have included MAC, the City's "financing agent", in applying the "credit elsewhere" test, the Secretary is directed to consider only the City's ability to obtain credit in making the determination required by this provision. Accordingly, the final wording of the "credit elsewhere" test, contained in Section 103(2) of the Act and Section 3.1.2 of the Agreement to Guarantee, refers only to the credit of the City and contains no reference

to MAC whatsoever.

Section 3.3.3 of the Agreement to Guarantee, dealing with Standby Guarantees, supports this interpretation of the "credit elsewhere" test:

"Section 3.3.3 Standby Guarantees. The issuance of the Standby Guarantees shall be subject to compliance by the City, the State and MAC with such other terms and conditions as the Secretary shall reasonably deem appropriate pursuant to the Guarantee Act, including the inability of MAC to sell MAC Indebtedness in the public or private credit markets on reasonable terms and conditions."

Although the Secretary may refuse to issue guarantees based on this provision, it is significant that MAC's market access or lack thereof is merely deemed an additional term or condition for the Secretary to consider in issuing Standby Guarantees, rather than a required component of the "credit elsewhere" test contained in Section 3.1.2 of the Agreement to Guarantee, which provides as follows:

"Section 3.1.2 Credit Elsewhere. The City is effectively unable to obtain credit in the public credit markets or elsewhere in amounts and on terms sufficient to meet the City's financing needs as set forth in the Financial Plan and the Secretary shall have received a certificate of the Financial Advisor and the City to such effect."

Accordingly, the conclusion is inescapable that the omission of MAC in the "credit elsewhere" provision was not an oversight, but rather a deliberate action consistent with the Committee's intentions.

Further, it should be understood that MAC proposes to use its \$800 million of public debt issuances during FY 1981-

1982 to fund an escrow that will help meet the City's capital needs during the three fiscal years after the end of the original four year Financing Plan. To enable MAC to finance these needs during FY 1983-1985, the State legislature has increased MAC's borrowing authority by \$1.2 billion. This additional borrowing capacity, in combination with the escrow to be funded by MAC during FY 1981-1982, is designed to ensure that the City has a reasonably certain source of capital after the expiration of the Federal guarantee program. The guarantees are essential to this effort, since MAC could not borrow enough to fund \$900 million of FY 1981-1982 City capital expenses (which is the role proposed for the guarantees) in addition to the escrow necessary to provide for the post-FY 1982 period.

Of course, under the original four year Financing Plan, it was assumed that MAC financing would be available to the City to meet all capital expenses in FY 1981-1982 on the theory that full market access would be regained for City bonds immediately after completing one City fiscal year with a budget balanced in accordance with generally accepted accounting principles. Two developments have made it unwise to continue to proceed on the basis of this assumption. First, it now appears unlikely that the City's bonds will receive an investment grade rating from both of the major credit rating agencies until a series of balanced budgets

has been reported.⁷ Second, the condition of the credit markets has been and may continue to be extraordinarily unfavorable to issuers whose credit is perceived as unproven.

In terms of the "credit elsewhere" test, the role proposed for MAC financing in FY 1981 and 1982 is thus seen to be similar to its role during the past two years: despite the issuance of approximately \$847 million of MAC bonds to the public and \$938 million in private placements for purposes other than financing the City's immediate capital needs, the "credit elsewhere" test was deemed to be satisfied because these other needs were recognized as valid and essential to the success of the four year plan. Financing the MAC escrow is no less valid and essential since there now appears to be no other method available to ensure that the City's capital needs can be met after FY 1982 through the public credit markets--which is a paramount objective of the Act. To the extent MAC financing is needed to satisfy this objective, it is clearly not available for other purposes and cannot be considered a source of credit to meet the City's current capital needs.

Based on the foregoing, the Secretary clearly has the authority to issue Standby Guarantees notwithstanding MAC's ability to issue bonds during FY 1981 and 1982.

B. Other Applicable Provisions

Before considering the advisability of the Secretary's issuing Standby Guarantees in FY 1981 and FY 1982, a brief discussion of two other provisions of the Act and the Agreement to Guarantee is necessary. First, Section 2.1 of the Agreement to Guarantee provides that the amount of available Standby Guarantees must be reduced by any City or MAC public sales made after June 30, 1980. Once again, however, action by the Secretary in this respect is discretionary, not mandatory. Pursuant to Sections 2.1 and 7.2 of the Agreement to Guarantee, the Secretary has the right to waive this requirement, thereby enabling Standby Guarantees to be issued notwithstanding any City or MAC public bond sales during this period.⁸

Second, Section 103(4) of the Act and Section 3.1.4 of the Agreement to Guarantee direct the Secretary to determine as a condition to the issuance of Standby Guarantees that the City will be able to meet all of its long-term and seasonal borrowing needs through the public credit markets after June 30, 1982. At this time, there is doubt as to whether the City alone will be able to achieve this objective by the original target date. As discussed above, however, with assistance from MAC, this goal will be met, and further Federal assistance will not be required provided the remaining guarantees are made available. A review of the legislative history on this point reveals that assistance from MAC is not precluded and will not affect the City's compliance with

this statutory requirement.⁹

C. Advisability of Issuing Standby Guarantees

As the preceding discussion demonstrates, each of the potentially troublesome conditions to the issuance of Standby Guarantees can be satisfied. Assuming that all of the remaining conditions set forth in the Act are met, which we are advised is presently projected, the only relevant issue then is whether it is desirable for the Secretary to proceed.

It is clearly within the spirit and objectives of the Act for the Secretary to issue Standby Guarantees under the circumstances now prevailing. The objectives of the Act were (i) to enable the City to effect needed reforms so that it could satisfy all of its financing needs after June 30, 1982 without Federal financing assistance and (ii) to assist the City with its financing needs during the interim period.

Despite the fact that the City has effected all the fiscal reforms envisioned by the Guarantee Act well within the schedule set forth, unforeseen conditions have made it advisable to give MAC the means to finance the bulk of the City's capital needs until three years of truly balanced City budgets have been completed and audited. As discussed above, use of the remaining Federal guarantees will achieve this. If the Federal guarantees are withheld, there will be a substantial risk that MAC and the City will be unable to finance the City's capital needs after the end of the guarantee program, thus inviting the risk that continued Federal

financing assistance will have to be sought for the period after FY 1982. Since the use of the remaining guarantees will provide reasonable assurance that MAC can furnish the City with financing for the necessary period, it would appear to be in the interest of the Federal government to choose this option rather than the risk associated with refusing further guarantees. In this connection, Senators Proxmire and Garn indicated in their recent letter that "it is clearly preferable to return the responsibility for meeting all of New York City's financing needs to the State and local level as soon as possible."

Although Standby Guarantees were considered an alternative under the Financing Plan to be used only if both the City and MAC could not sell long-term bonds to the public in sufficient amounts on reasonable terms and conditions in FY 1981 and 1982, it is clear that the Financing Plan can be modified from time to time with the consent of the Secretary.¹⁰ An adjustment of the Plan, at this time, would be legally permissible and appropriate to complete the recovery program approved by Congress in 1978.

FOOTNOTES

¹ P.L. 95-339 (1978), codified at 31 U.S.C. §§ 1521, et seq.

² Section 1.1 of the Agreement to Guarantee (definition of "Standby Guarantees")

³ Section 2.1 of the Agreement to Guarantee

⁴ Oral statement by Felix G. Rohatyn, Chairman of the Board of Directors of MAC, at the MAC Board of Directors meeting held on June 3, 1980.

⁵ The general view is that the City would be able to sell publicly approximately \$100 million of its bonds as a speculative investment. Although the City is obligated by Section 103(10) of the Act to offer to sell its long-term bonds to the public in FY 1981 and FY 1982, the Secretary has the authority to waive all such required City bond sales. The City plans to issue \$100 million of bonds in the last quarter of the current fiscal year.

⁶ Joint Explanatory Statement of the Committee of Conference, H. Conf. Rep. No. 95-1369, 95th Cong., 2d Sess. 12, reprinted in [1978] U.S. Code Cong. & Ad. News 1251.

The Senate and House reports should also be consulted in this connection. S. Rep. No. 95-952, 95th Cong. 2d Sess. 13, reprinted in [1978] U.S. Code Cong. & Ad. News 1225 and H. Rep. No. 95-1129 Pt. I, 95th Cong., 2d Sess. 15 (1978).

⁷ Testimony of Freda Stern Ackerman, Senior Vice President of Moody's Investors Service, before the Senate Committee on Banking, Housing and Urban Affairs on January 28, 1980, in which she stated the following:

"The general rule in financial analysis is that three years of sound, realistically balanced operations can be defined as a trend. We expect the end of fiscal 1981 or 1982, whichever the City chooses, to mark the beginning of that trend

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United States Senate

COMMITTEE ON BANKING, HOUSING, AND
URBAN AFFAIRS

WASHINGTON, D.C. 20510

June 2, 1980

The Honorable G. William Miller
Secretary
U. S. Department of the Treasury
Washington, D.C. 20220

Dear Mr. Secretary:

We were interested to learn from press reports that New York City and State officials are discussing with the Treasury Department the possibility of using the remaining \$900 million in Federal guarantees authorized under the New York City Loan Guarantee Act of 1978, should the City be unable to market its own bonds in that amount in fiscal years 1981 and 1982, as scheduled.

Presently these guarantees are held on "stand-by", to be used only in the event that neither the City nor the State's Municipal Assistance Corporation (MAC) can raise the necessary amounts in the public bond market. The proposal, as described, would be to use the Federal guarantees as the first resort rather than the last resort, in order to free up \$900 million more of MAC's borrowing authority for potential use in fiscal years 1983 and 1984, should the City continue to have problems in selling its bonds.

As Chairman and Ranking Minority Member of the Senate Banking, Housing and Urban Affairs Committee, which has jurisdiction over the Act, we see no way that the provisions of existing law would permit such use of the remaining guarantee authority, and we assume that the Treasury Department will confirm this interpretation, as it has done on numerous occasions in the past. The law states that guarantees may be made only if "the city is effectively unable to obtain credit in the public credit markets or elsewhere in amounts and terms sufficient to meet the city's financing needs." Thus it is clear from the statutory language that so long as MAC has the capacity to meet the city's financing needs in 1981 and 1982, no further Federal guarantees can be issued.

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The question of whether and under what conditions the remaining guarantees could be used has been discussed a number of times, most recently in the course of the Committee's oversight hearings in January and February, 1980. The following colloquy between Senator Lugar and Assistant Secretary Altman indicates in detail and unequivocally that the standby guarantees cannot be used in the event of failure by the City to sell its bonds in sufficient amounts so long as MAC is able to meet the City's financing needs:

Mr. Altman....We see no reason why the remaining \$900 million of guarantee authority will need to be used and it was not foreseen to be used in the original plan. I think the original plan is working and those standby guarantees will remain standby and not be used because any failure by the city to re-enter the markets on schedule, which would be next year for \$300 million and the next year for \$645 million, will be made up by MAC, not the Federal Government.

Senator Lugar. What is the triggering mechanism that would bring in that \$900 million?

Mr. Altman. A failure by the city and a failure by the Municipal Assistance Corp. to be able to get into the public markets or any other bond markets to raise the amounts that have to be raised in fiscal years 1981-82. In other words, the city schedule calls for the public sale of \$300 million in fiscal year 1981 and \$645 million the following year. If the city cannot sell these amounts publicly, MAC has sufficient reserve debt capacity to meet the city's needs. Only if both the city and MAC fail would the standby Federal guarantees be used.

Senator Lugar. It's your judgment, then, even after this \$100 million is guaranteed and we reach the \$750, that throughout the rest of this calendar year of 1980 there would not be a need for further Federal guarantees?

Mr. Altman. Yes.

Senator Lugar. And there is some reserve capacity with MAC now that would obviate the need for that in the foreseeable future or, to be very specific, throughout the entirety of this 4-year plan?

Mr. Altman. Yes; MAC has \$1.1 billion of scheduled, unused, funding authority during the remainder of the plan. If the city can't meet its plan for \$945 million of its

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own bonds, you have that as a backup and MAC continues to have access to the public credit market.

It is clear, then, that the \$900 million in standby guarantees could become available to New York City only if neither the City nor MAC were able to market bonds in amounts and terms sufficient to meet the City's needs. There are two ways in which this might occur. One would be due to circumstances beyond the City's control, such as a collapse of the municipal bond market. The recent recovery in the bond markets suggests that MAC is likely to have continued market access, and there is some potential market for City bonds as well. The other way would be through a "self-inflicted wound," such as a City labor contract settlement so generous as to render it extremely unlikely that the City could balance its budget in accordance with generally accepted accounting principles in 1981 or 1982 or succeeding fiscal years. Should this seem probable, it would be grounds for Congress to consider exercising its authority to veto further guarantees. However, both the Mayor and the Governor assured the Committee that they will not agree to a settlement which would not conform to the City's January 15, 1980 Financial Plan, projecting GAAP-balanced budgets for 1981 and thereafter, so this should not be a problem.

Going beyond the statutory barriers, we see no reason to believe that it would be either necessary or desirable to provide the standby guarantees in order to give MAC "a cushion of an extra \$900 million in borrowing power over the next few years." In his testimony at the Committee's oversight hearings, the Chairman of MAC recommended an increase in MAC's statutory borrowing authority from the present \$8.8 billion to \$10 billion and stated that the latter amount would be "ample to finance the city through 1984," and well within MAC's economic capacity and maximum funding requirements. At that same hearing, the Governor said that he would recommend that the New York State Legislature approve such an increase in borrowing authority.

It should be further noted that the \$10 billion figure is based on a worst case assumption that New York City would not be able to sell any of its own bonds during that period, and if that were to occur, then a \$900 million "cushion" provided by the Federal Government would not solve the problem in any event. However, the MAC Chairman said he did not anticipate this occurring and then went on to offer the following scenario of the City's re-entry into the credit markets:

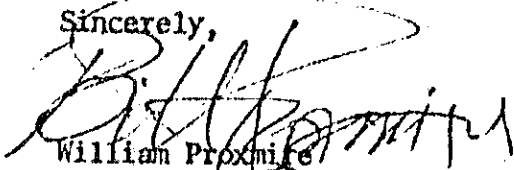
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If the city continues on track, within a reasonable economic environment, the city capital funding requirement of 1983 and 1984 could be met through a combination of MAC issuances supplemented in ever-increasing amounts by the city's own debt. It is entirely plausible that the city, having implemented four consecutive GAAP balanced budgets and having successfully issued ever-larger amounts of debt for two years, would then be able to fully meet its own capital needs.

We should also note here that New York City officials and their financial advisors told the Committee that they are exploring other means of meeting the City's long-term financing needs after 1982, including the possible establishment of special enterprise agencies, such as a water and sewer authority, to borrow through a revenue bond device.

Aside from the fact that providing the remaining \$900 million in Federal guarantees "up-front" would be both unnecessary and contrary to the law, the only real effect of doing this would be to relieve New York State of the responsibility to increase the borrowing authority of the Municipal Assistance Corporation. In our view, this would be most undesirable. Given the intent of the law that the Federal government be the lender of last resort, and given the reluctance of Congress to provide further Federal guarantees, it is clearly preferable to return the responsibility for meeting all of New York City's financing needs to the State and local level as soon as possible.

Sincerely,



William Proxmire
Chairman



Jake Garn
Ranking Minority Member

WP:eb1

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Telephone: (212) 775-0010

MUNICIPAL
ASSISTANCE
CORPORATION
FOR THE CITY
OF NEW YORK

24 April 1980

TO: Felix G. Rohatyn
FROM: Robert F. Vagt *RFV*
SUBJECT: Use of Standby Guarantees

REVIEW OF STATUS

The use of Standby Guarantees during FY 1981 and FY 1982 seems to be permissible under both the Guarantee Act and the Agreement to Guarantee. It is the opinion of Counsel that this could be done without any additional Congressional action (also assuming the absence of a One House Veto).

The Guarantee Act itself makes only a minimal distinction between the guarantees available in fiscal years 1979 and 1980 and those available thereafter. The one condition seems to be that the City attempts to publicly market its own long-term debt in fiscal years 1981 and 1982.

The Agreement to Guarantee, however, has several pertinent provisions:

- A. Credit elsewhere: The Secretary must find, prior to the issuance of any guarantees, that the City "is effectively unable to obtain credit in the public credit markets or elsewhere in amounts or on terms" sufficient to meet its needs (Section 3.1.2.). The Treasury's definition of this is not clear, as MAC could have issued some amount of additional debt this year, thus providing the City with "credit elsewhere" if the narrow interpretation were intended.
- B. Section 3.3.3: This Section specifically states that Standby Guarantees can be issued only if the Secretary determines that there exists "the inability of MAC to sell MAC Indebtedness in the public or private credit markets on reasonable terms and conditions". Past discussions with Treasury employees have indicated that current (not future) market capacity is about the only rationale which would move them to find that MAC could not issue.

*Municipal Assistance Corporation
For The City of New York*

24 April 1980

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- C. Financing Plan: Exhibit A to the Agreement to Guarantee is the Financing Plan. It reflects no specific use of proceeds, simply a gross amount of debt to be issued. It, too, indicates that MAC must be unable to market its Bonds for the Standby Guarantees to be available. Amendment of this Plan requires the approval of Treasury. However, were the FCB approved Financial Plan to include the budgetary effects of additional MAC refunding, the argument could be made that MAC's capacity is being used for a recognized purpose and is not fully available as a backup to the City in FY 1981 and 1982.
- D. There is a requirement in both the Act and the Agreement that the Guarantees are issued with the assumption of a balanced City budget in 1982.

Thus, a review of the documents would indicate that the issuance of Guarantees is allowable, but it requires that the Secretary exercise some judgement.

NEXT STEPS

It is my judgement that the only case under current law which can be made by which Guarantees could be issued is based on the City's capital needs. That is, because the City will not have access to the credit markets, MAC's capacity will be required beyond 1982 to support even a modest capital program.

The arguments in favor of the use of Standby Guarantees seem to focus on the following:

- A. Assistance to the City has always been done with the participation of "all parties". Extension of some amount of guarantees in FY 1981 and FY 1982 would be matched by the State's extending and raising MAC's ceiling and by the waiving of the \$8.8 billion cap by the parties to the BPA. It is done at no cost to the Federal government, and draws in once again the State, the financial institutions, and the unions.
- B. The supply of MAC debt going forward through 1984 (assuming no Standby Guarantees) will be inordinately large.
- C. MAC will have little refunding capacity, in the absence of Standby Guarantees.

DATE..... June 2, 1980

MEMORANDUM

To

Municipal Assistance
Corporation For The
City of New York

From Allen L. Thomas
Paul S. Pearlman

Subject

Issuance of "Standby
Guarantees" by the Secretary of
the United States Department of
the Treasury

You have informed us that the Municipal Assistance Corporation For The City of New York (the "Corporation") and The City of New York (the "City") are currently developing methods of financing the City's capital projects during the fiscal years immediately following expiration of the four-year financing plan of the City adopted in November 1978 (the "Financing Plan"). In connection with this study, you have asked us to determine whether, under the circumstances described below, the Secretary of the United States Department of the Treasury (the "Secretary") may permissibly issue "Standby Guarantees"* pursuant to the New York City Loan Guarantee Act of 1978 (the "Guarantee Act") and the Agreement to Guarantee (the "Agreement to Guarantee"), dated as of November 15, 1978, by and among the United States of America (the "United States"), acting by and through the Secretary, the State of New York (the "State"), the City, the New York

* As used herein the term "Standby Guarantees" refers to Guarantees to be issued by the Secretary pursuant to the Agreement to Guarantee during the City's 1981 and 1982 fiscal years.

State Financial Control Board and the Corporation.

As discussed in detail below, we are of the view that the Secretary may permissibly issue such Standby Guarantees under the circumstances described, if he were to waive -- as he has the legal right, but not the obligation to do -- the contractual requirement contained in the Agreement to Guarantee that the amount of such Standby Guarantees be reduced in any fiscal year of the City by the amount of bonds of the Corporation issued to the public during such fiscal year, and also if (i) all other required conditions precedent to the issuance of such Standby Guarantees have been fulfilled, and (ii) neither the Senate nor the House of Representatives of the United States shall have passed a resolution prior to the commencement of the fiscal year of the City in which such Standby Guarantees are to be issued stating in substance that such body disapproves such Standby Guarantees.

Statement of Facts

The Financing Plan was adopted to provide approximately \$4.5 billion of long-term financing for the City during its 1979 through 1982 fiscal years. As outlined in Exhibit A to the Agreement to Guarantee, the Financing Plan includes four long-term financing components: (i) the sale of up to \$1.8 billion of the Corporation's bonds to various commercial banks, savings banks and insurance companies and

four City employee pension funds (the "City Pension Funds"); (ii) the sale of up to \$750 million of federally guaranteed City bonds to the City Pension Funds and two State employee pension funds (the "State Pension Funds"); (iii) sales to the public of up to \$1 billion of the Corporation's bonds; and (iv) sales to the public during the City's 1981 and 1982 fiscal years of up to \$950 million of City bonds that are not federally guaranteed, or, to the extent neither the City nor the Corporation is able to sell its bonds to the public in sufficient amounts on reasonable terms and conditions to fulfill this element of the Financing Plan, the United States has agreed to guarantee up to \$900 million of City bonds and the City and State Pension Funds have agreed to purchase such bonds (see footnote 6 of such Exhibit A).

The major portion of the funds to be generated by the Financing Plan are to be used to finance the City's capital programs during the four years of the Plan. As stated in the report of the United States Senate Banking, Housing and Urban Affairs Committee, the primary objective of the Plan is to enable the City to regain full reentry into the long-term public credit markets, thereby permitting the City to finance its capital needs on its own after the expiration of the Plan. (S. Rep. No. 95-952, 95th Cong. 2d Sess. 8, 14.) To that end, Section 103(10) of the Guarantee Act and Section 6.16 of the Agreement to Guarantee require that the City

attempt to sell through public offerings some amount of long-term bonds during its 1981 and 1982 fiscal years, unless the Secretary "determines that such offer would be inconsistent with the financial interests of the City." (Section 6.16 of the Agreement to Guarantee.) To the extent the City is unable to sell such bonds, the Financing Plan (as outlined in Exhibit A to the Agreement to Guarantee) provides that the City's capital needs would be met during those years, in the first instance, by sales of the Corporation's bonds to the public or, if the Corporation is unable to market publicly such bonds on reasonable terms, by the sale of federally guaranteed City bonds to the City and State Pension Funds.*

You have advised us that despite the successful operation of the Financing Plan to date and the significant budgetary progress the City has made during the past few years, it has become increasingly apparent that the City will be unable to market publicly the amount of bonds required to finance its capital needs during its 1981 and 1982 fiscal years. In addition, it appears unlikely that the City will be able to sell publicly such required amount of bonds during

* It should be noted that a large portion of the City's capital needs during its 1981 and 1982 fiscal years will be met pursuant to the Financing Plan by private placements of the Corporation's bonds to various commercial banks, savings banks and insurance companies (collectively the "Financial Institutions") and the City Pension Funds pursuant to the Bond Purchase Agreement, dated as of November 15, 1978, by and among, such Financial Institutions, City Pension Funds and the Corporation.

its 1983 and 1984 fiscal years. Accordingly, alternative sources of financing will have to be arranged to enable the City to finance its capital needs during those years. You have informed us that the City's bondable capital requirements are expected to range from approximately \$700 million to \$1.2 billion during each of its 1981 through 1984 fiscal years.

In this regard, the Corporation has stated its intention to ask the State legislature for increased borrowing authority and an extension of its authorization to issue debt through the 1984 calendar year in order to be prepared to help the City meet its financing needs to the extent necessary during the City's 1983 and 1984 fiscal years. The Corporation has recently been advised by its managing underwriters, however, that, assuming no unforeseen dramatic changes in the economy or market conditions for municipal bonds, it is their expectation that the Corporation's ability to market publicly bonds on reasonable terms will be limited to approximately \$600 million annually through the City's 1984 fiscal year. Consequently, if the Corporation were to issue such amount of bonds during the 1983 and 1984 fiscal years of the City, the proceeds of such sales, together with the limited amount of bonds that the City is expected to be able to market publicly in those years, would be insufficient to finance all of the City's projected capital needs for such years.

You are therefore considering a proposal (the "Proposed Plan") pursuant to which the Corporation would issue to the public during the City's 1981 and 1982 fiscal years the amount of bonds it is capable of issuing on reasonable terms, and set aside the proceeds of such sales to, in effect, prefund a portion of the City's capital needs for its 1983 and 1984 fiscal years. The funds derived from these sales would be available to the City to the extent required to finance the City's projected capital programs in the City's 1983 and 1984 fiscal years. Thus, the Proposed Plan would permit the City to meet all of its 1983 and 1984 capital requirements without the necessity of Federal assistance in the form of guarantees or otherwise. Thereafter, assuming the City is able to continue the budgetary progress it has made to date, it is expected that the City will regain sufficient access to the public credit markets to finance its capital projects entirely through the public sale of its bonds.

In connection with the Proposed Plan, we have reviewed the New York State Municipal Assistance Corporation Act, as amended by the Municipal Assistance Corporation For The City of New York Act (the "Act"), other laws which we considered relevant and the agreements implementing the Financing Plan and are aware of no prohibitions against the issuance of bonds by the Corporation in one year to

prefund a portion of the City's capital programs for subsequent years.* In addition, we believe such issuance of bonds would be within the Corporation's authorized purposes. We assume, of course, that you will be consulting with Hawkins, Delafield & Wood for their views with respect to any arbitrage problems which may result from the Proposed Plan.

As discussed above, the Financing Plan contemplates that the City's capital projects for its 1981 and 1982 fiscal years will be partially financed by public sales of City bonds during such years, and in the event the City is unable to sell such bonds on reasonable terms, such capital projects would be partially financed, in the first instance, by public sales of the Corporation's bonds during those years, none of which sales are currently scheduled. Because, however, the Proposed Plan contemplates that the proceeds of any public sales of the Corporation's bonds during the City's 1981 and

* As you know, Section 3037 of the Act provides that any amounts paid to the City by the Corporation to finance the City's capital projects are to be evidenced by bonds of the City delivered to the Corporation. Although restrictions may exist with respect to the issuance of bonds by the City in one year to prefund its capital programs for subsequent years, such restrictions should not affect the Proposed Plan, because bonds of the City are to be delivered to the Corporation pursuant to Section 3037 only at the time the Corporation pays moneys to the City, which, as we interpret the Proposed Plan, will not occur until the year in which the moneys are actually required for the City's capital program.

1982 fiscal years would be used to prefund a portion of the City's 1983 and 1984 capital requirements, other funds will be required to finance the City's 1981 and 1982 capital projects. Under the Proposed Plan, such funds would be provided from sales of federally guaranteed City bonds to the City and State Pension Funds provided the Secretary is willing to issue the Standby Guarantees. Thus, you have asked us to determine whether the Secretary may permissibly issue such Standby Guarantees under the factual situation described.

Legal Discussion

The Guarantee Act and the Agreement to Guarantee authorize the Secretary to guarantee the payment of principal of and interest on up to \$1.65 billion in aggregate principal amount of outstanding City indebtedness issued to any City or State employee pension fund during the 1979 through 1982 fiscal years of the City. Pursuant to the Guarantee Act and the Agreement to Guarantee, the Secretary has guaranteed the payment of \$750 million of City bonds during the City's past two fiscal years, and is authorized pursuant to Section 2.1 of the Agreement to Guarantee to guarantee, on a standby basis, the payment of \$900 million of such bonds during the City's 1981 and 1982 fiscal years if certain specified conditions are met. After reviewing the Guarantee Act and the

Agreement to Guarantee, we believe that there are three such conditions which could clearly affect the Secretary's ability to issue the "Standby Guarantees" under the Proposed Plan.

One such condition is contained in Section 103(2) of the Guarantee Act which provides that prior to the issuance of any Guarantee the Secretary must determine that:

"the city is effectively unable to obtain credit in the public credit markets or elsewhere in amounts and terms sufficient to meet the city's financing needs."

Because the Proposed Plan calls for the Corporation to raise money in the public credit market during the same period the Standby Guarantees are to be issued, two questions may be raised with respect to the "credit elsewhere" test contained in Section 103(2). First, should the test be integrated to require that both the City and the Corporation be unable to obtain credit in the public credit markets or elsewhere prior to the issuance of any Guarantees? Second, even if the answer to that question is No, if the Corporation has raised money does it become an "elsewhere" where the City might obtain credit?

Section 103(2) of the Guarantee Act was adopted, virtually without change, from the House version of the Guarantee Act. The Senate version of such Act had provided, however, that "the Secretary determine that credit is not otherwise available to the city or a financing agent [the

Corporation] on reasonable terms before he agrees to guarantee . . . any city indebtedness." (S. Rep. No. 95-952, 95th Cong. 2d Sess. 13). The adoption of the House version of the bill, and the concomitant rejection of the Senate version, we believe, evinces a Congressional intent that only the City's ability to obtain credit in the public credit markets or elsewhere be considered by the Secretary prior to the issuance of any Guarantees.*

As to the second question, although the Corporation is expected to have certain market access during the City's 1981 and 1982 fiscal years, the Corporation intends to use that access under the Proposed Plan not to finance the City's capital needs for those years but for the purpose of raising funds to enable the City to finance its capital needs, without Federal assistance, in the years following the expiration of the Financing Plan. As discussed above, this purpose is consistent with the primary objective of the Financing Plan.

* The House Report, in discussing Section 103(2), states in pertinent part that such Section:

" . . . requires the Secretary to determine that the city's financing needs cannot be met effectively through borrowings in the private credit market. The use of the word "effectively" is intended to create a test of the practical unavailability of credit, including maturity and rate, through the private market. The Secretary has discretion to determine when that test has been met."

(H. Rep. No. 95-1129 Pt. I, 95th Cong., 2d Sess. 15.)

Accordingly, because the Corporation will use its full available market access for this purpose, it will be unable to issue indebtedness in the public markets on reasonable terms to provide funds for the City's capital needs for the City's 1981 and 1982 fiscal years. Similarly, during the City's 1979 and 1980 fiscal years, the Corporation had certain access to the public credit markets but used that access not to finance the City's capital needs for those years but for other purposes consistent with the Financing Plan without causing the City to fail to meet the "credit elsewhere" test.

For the reasons discussed above, therefore, we believe that it would be appropriate and consistent with the Guarantee Act for the Secretary to determine that the requirements of Section 103(2) of the Guarantee Act have been satisfied in connection with the issuance of Standby Guarantees under the Proposed Plan.

Sections 2.1 and 3.3 of the Agreement to Guarantee provide in pertinent part that the amount of Standby Guarantees which may be issued in the City's 1981 and 1982 fiscal years shall be reduced by the amount of the Corporation's bonds publicly sold during those years. As discussed above, this requirement is consistent with the Financing Plan (as outlined in Exhibit A to the Agreement to Guarantee) which contemplates that the public sale of the Corporation's bonds act as the

first back-up to the extent the City is unable to market publicly its bonds on reasonable terms during its 1981 and 1982 fiscal years, which event now appears likely. However, since this requirement is contained only in the Agreement to Guarantee and not in the Guarantee Act, it may be waived by the Secretary in accordance with Section 7.2 of the Agreement to Guarantee, which provides in relevant part that "[t]he Secretary may waive any provision of [the] Agreement . . . which is intended for the benefit of the United States and may consent to any modification of any term [t]hereof . . . which is intended for the benefit of the United States as he may deem appropriate." Correspondingly, Section 2.1 of the Agreement to Guarantee specifically provides that the requirement that the amount of the Standby Guarantees in any year be reduced by the amount of the Corporation's bonds publicly sold during such year is subject to the Secretary agreeing otherwise. Consequently, because the Proposed Plan is designed to enable the City to finance its capital needs after the expiration of the Financing Plan without Federal assistance, which, as discussed, is similarly the ultimate objective of the Financing Plan, we believe that the Secretary has the legal power to waive this requirement and that it would be appropriate for the Secretary to grant such a waiver.

The third condition which could affect the Secre-

tary's ability to issue Standby Guarantees is contained in Section 103(4) of the Guarantee Act which provides that prior to the issuance of any Guarantee the Secretary must determine that:

"during the four-year period ending June 30, 1982, the long-term and seasonal borrowing needs of the city . . . will be met through commitments from the State, an agency of the State, private sources, or through the public credit markets, in amounts which will be sufficient to enable the city, when the guarantee authority conferred by this title has terminated, to meet all of its long-term and seasonal borrowing needs through the public credit markets"

This condition would apparently be satisfied under the Proposed Plan because the primary objective of such Plan is to enable the City to finance its capital needs in the years immediately following the expiration of the Financing Plan through the public sale of the City's and the Corporation's bonds. Although literally read, Section 103(4) could be interpreted to require that the City meet on its own, without assistance from the Corporation, all of its financing needs beginning with its 1983 fiscal year, the legislative history to the Guarantee Act indicates that what is contemplated by Section 103(4) is that the City merely be able to meet its financing "needs in the credit markets without Federal assistance." (S. Rep. No. 95-952, 95th Cong., 2d Sess. 15.) In fact, the report of the Senate Banking, Housing and Urban Affairs Committee states that it is desirable

that the Corporation retain some borrowing authority after the expiration of the Financing Plan in case such authority is required to help the City meet its financing needs once the guarantee authority terminates. (S. Rep. No. 95-952, 95th Cong., 2d Sess. 10.) Thus, we believe that the Secretary would be able to make the determination required by Section 103(4) under the Proposed Plan.

Accordingly, if the Secretary were to waive the requirement contained in Sections 3.1 and 3.3 of the Agreement to Guarantee, and assuming all other required conditions precedent to the issuance of the Standby Guarantees are satisfied, we are aware of no legal impediments to the issuance of the Standby Guarantees by the Secretary under the Proposed Plan.

Other Factors

There are other factors which conceivably could prevent implementation of the Proposed Plan and the issuance of the Standby Guarantees. For example, the Guarantee Act and the Agreement to Guarantee both provide that either the Senate or the House of Representatives may veto the issuance of Standby Guarantees by passage of a resolution stating in substance that such body disapproves such Guarantees. Such resolution, however, must be adopted prior to the commence-

ment of the fiscal year of the City in which such Guarantees are to be issued. Any such disapproval terminates the Secretary's authority to issue such Guarantees in any subsequent fiscal year to the extent of the amounts disapproved. You may therefore wish to consider whether it is appropriate to consult with key Congressional leaders to convince them of the desirability of the Proposed Plan in order to ensure that neither body will attempt to veto such Plan by passing such a resolution.

In addition, the City and State Pension Funds, which are obligated pursuant to Section 1.1 of the Guaranteed Bond Purchase Agreement, dated as of November 15, 1980, by and among the City, the United States, acting by and through the Secretary, and the City and State Pension Funds, to purchase any City bonds that are guaranteed by the Secretary, will also have to be consulted, because such Pension Funds may seek to influence the Secretary not to make the necessary waivers and issue such Standby Guarantees, particularly in view of the sensitive labor negotiations currently underway between the City and certain of the municipal labor unions.

A.L.T.
P.S.P.