Informational Meeting

Finance and Management Committee

Erie County Legislature

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Testimony

By

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Deputy County Executive

Good morning Honorable Members of the Erie County Legislature. I would like to thank you, Mr. Chairman. for inviting me to offer testimony at today's meeting of the Finance and Management Committee of the Erie County Legislature.

While I am pleased to be with you, I am deeply disturbed about the circumstances that have brought me here today. I am here to comment on the Budget Amendments proposed on Friday by six members of the Legislature.

On November 28, 2012, County Executive Poloncarz wrote to the Legislature about the then proposed budget amendments, that are almost identical to the ones before us today. He stated that the

> **"...cuts are both unrealistic and irresponsible and will cause the 2013 Budget to be out of balance."**

Mr. James Sampson, Chair of the Erie County Fiscal Stability Authority, stated in his written communication that:

> **"...an $8.5 million per year reduction in the property tax levy (without corresponding spending reductions and/or revenue enhancements), would create concerns that would lead the ECFSA to have to re-evaluate whether the budget is in balance and whether the four year plan is achievable.."**

Erie County Comptroller David Shenk in his communication to you dated November 29, 2012 reached the same conclusion. In his November 29, 2012 letter the Comptroller stated that:

> **"The Minority Caucus's proposed set of budget reductions is a substantial concern. If the proposed set of amendments is incorporated into the budget for fiscal year 2013, then the budget will not be structurally sound; i.e. the expenditure estimates will not be reasonable and appropriate...."**

These amendments are like making a decision to amend the family budget by reducing the amount you plan to pay for utilities, without turning the thermostat down. The bill is going to come and you are going to have to pay it; you have only fooled your family and maybe yourself for a little while. In the end the bill will be paid.

I have become something of an expert in municipal finance with more than 30 years of experience in government budgeting and crisis response. My experiences include:

- Closely watching County Executive Ned Regan deal with a budget crisis in Erie County in the 1970s,
- Studying municipal law and municipal finance in Law School,

- Being called back from a canoe trip into James Bay, with Assemblymen Bill Hoyt and Rollie Kidder, in 1975 so they could vote to extend the life of the NYS Urban Development Corporation for one more month,
- Watching from the floor of the Assembly when the NYC financial control board was created in 1975 and again when the Yonkers control board was created. I followed the events closely and with an eye on when a control board might be necessary for the City of Buffalo,
- Working to pull Erie County out of its budget crisis under County Executive Ed Rutkowski in the mid-1980s including drafting special state legislation that helped Erie County for a time,
- Serving as a founding member of the Buffalo Control Board, on which I served as a board member from July 2003 to January 2006. We had to impose draconian measures to save Buffalo from financial collapse,
- Working with the late David Rutecki to try to avert the Joel Giambra Red-Green budget fiasco,
- And, until recently, I taught a bridge course at the Law school with Jim Magavern, a true expert in municipal finance, on Control Boards in NYS and how other states handle crisis in municipal finance.

While teaching, we read a report by The Committee on Municipal Affairs of The Association of the Bar of the City of New York titled **Proposals to Strengthen Local Finance Laws in New York State** dated January/February 1979. It was largely written by my Law School colleague Clarence Sundram. It is the definitive legal history of how NYC went down the slippery slope to financial ruin. Beginning on page 18 you will find a synopsis of the path that New York City took to this sad outcome. I have attached a copy of this report.

In New York City, the problem can be traced back to the early 1960s when the City began to have annual budget deficits. It financed these deficits by deficit borrowing. In 1966 the Temporary Commission on City Finances warned that this practice "might well lead to a deterioration of the City's credit standing," an understatement if there ever was one. The city became deeply committed to this unwise practice. The city's cash balance decreased from almost $70 million to less than $200 thousand. Other revenues were similarly depleted. The city then used, and failed to restore, its rainy day fund. The city began to borrow more and more to cover annual expenses and also used one shot tricks, such as spin-ups and improper accruals. Eventually the city began to use deficit financing, including in one year the selling of bonds to cover annual pension payments and to pay for operating expenses. By 1975 the City needed to borrow $500 million per quarter to pay for prior borrowings and current operating expenses. This meant more than $2 billion per year of new borrowing to cover annual expenses. When the national economy suffered a significant downturn, NYC with its heavy debt load, absence of resources, depleted reserves and ongoing need to borrow to cover current operating costs, could not and did not survive as an independent government.

New York City started down this path with a very modest budget deficit which could have been dealt with by a relatively easy set of real spending cuts. However, in the next year the size of the problem more than doubled because the adopted prior year budget was not truly balanced and the new budget thus had twice as far to go to gain balance. So another trick was used to put off the day of reckoning. With each year the problem grew.

The lesson is that once an unbalanced budget is adopted and one shot solutions are used, it is harder each year to get the budget truly back into balance. The real gap gets bigger and bigger, and reserves are consumed. In each later year the consequences are more and more difficult to accept. Government can use, but will eventually run out of, one shot revenues. A time will come when you cannot put off additional expenses to a future date. Eventually, the slippery slope becomes so steep that the slide cannot be stopped and the crash is profound and very hurtful.

In Erie County, we currently have a balanced budget, and it and the 2013-2016 Four Year Financial Plan have already been approved by ECFSA and validated as balanced and reasonable.

We also have a confluence of very positive events that hold out promise for a far brighter future after so many years of struggle. Let me name a few:

- A Governor committed to our area as no other has ever been,
- The billion dollars for Buffalo economic development,
- The positive impact from the 2% property tax cap,
- Two balanced state budgets passed on time for the first time in 30 years,
- A locally developed regional economic development plan that all key parties buy into and accept as a blue print,
- A list of regional accolades from highly credible outside parties in which our area is lauded for its positive attributes such as:
    - Affordable and sustainable real estate market
    - Tremendously livable neighborhoods and communities with a tradition of excellent architecture
    - One of the best and most vibrant cultural settings in the nation
    - One of the best communities for working mothers
    - One of the shortest commutes in a major metro,
- A reviving manufacturing base,
- Significant attention being paid to workforce development with state and federal funding increasingly becoming available,
- The Say Yes to Buffalo program along with the Promise Neighborhood initiatives,
- The growth of the Buffalo Niagara Medical Campus,
- The rising international prominence of our institutions of higher education, particularly the University of Buffalo,
- Improvements in the movement of people and goods across our Canadian border and growing international trade, and

- Companies finally relocating here such as Welded Tube, which we hope is the beginning of a new trend.

This list could go on and on.

These positive self-reinforcing events will never reoccur. We must take advantage of this moment in time. Let me say this again. These events will not reoccur. We must seize this opportunity for a better future for this County.

And yet, all this positive, forward energy and growth is threatened by our budget battle that is now drawing to a close.

The Budget itself was prepared and must be seen in light of the world and national events of which we are a part:

- The federal budget battles now underway and the possible sequestration of millions and millions of dollars that we rely upon to help feed and house the elderly and needy and that we use to protect our citizens from all manner of danger, including middle class families that benefit from non-public assistance programs such as federal funding for roads, bridges, day care, education, senior citizen nutrition, and law enforcement,
- The turmoil in the European Union where we do so much business,
- The repercussions from Hurricane Sandy will certainly be felt here in declining state tax collections and a slow down on cross-state business,
- The possible loss of the current federal income tax deductions by middle class families that has helped fuel the recovery and the repercussions from such a loss upon our sales tax collections, and
- Some uncertainty across our northern border and the always volatile issue of day shoppers into Erie County from Canada.

Mark Poloncarz's election as Erie County Executive revolved in large part around the issues that are now being called the People's Mandates-libraries, cultural institutions, rodent control, road improvements and other quality of life issues. Of course these items are expensive, and you can see the costs in the budget that the County Executive presented to you.

We believe that these are items that the citizens of Erie County want and are willing to pay for. We have properly funded them in the budget.

The Legislature, of course, can accept or reject these and other items of spending. We would disagree with certain cuts, but are prepared to work with you to get to an agreed upon budget. That agreement might include cuts in things we believe should receive funding, but we understand there might be differences of opinion and we are prepared to compromise.

Even now, there is time to prepare a real consensus budget. The County Executive is in his office. When this Committee meeting ends, we would invite you to come to his office to discuss a budget that will be truly balanced. What we cannot accept is another set of budget decisions that leaves an unbalanced

budget and tougher decisions for tomorrow. County Executive Poloncarz has said that he will not allow the County to return to the days of the Red and Green budget.

The proposed budget amendments put on the table on Friday afternoon by the 6 members of this house so destabilizes the budget and does so so clearly and unequivocally that the County Control Board has criticized the proposed amendments and issued a warning about the future of the County's fiscal health. The County Executive, the County's chief budget officer, the County Comptroller and the independent Fiscal Stability Authority have all come to the same conclusion. The budget was balanced as presented by the County Executive and the amendments proposed by the six legislators that are now before the Legislature would create a significantly unbalanced budget.

The reasons this amendment package is unbalanced are simple. It does not reduce costs, it only takes away resources to pay for items that we are obligated to pay and will have to pay for in 2013. The issues are:

- Existing and new lawsuits will not go away and parties will not suddenly drop the more than 700 current claims against the county because we do not have funds to pay judgments. The amendments proposed by the six members take our liability or risk retention account, our self-insurance fund, from $3,000,000 to $69,498 for all of 2013, thus reducing the account by $2,930,502. For a budget to be balanced anticipated expenses must match anticipated costs. How can it in any way be reasonable to budget that the County will only incur $69,498 in litigation related losses in all of 2013?
- Overtime in the jail and correctional facility will not go away simply because the legislature reduces the budgeted funds and we all know that overtime in these facilities routinely exceeds the budgeted amounts.
- We cannot achieve vacancy controls of $1.8 million without dramatic negative impacts on all County departments and of course high vacancies put upward pressure on overtime usage. This is particularly true in the uniformed services, but elsewhere in the budget as well.
- The need for snowplowing, for lawn mowing and for cleaning and protective services in public buildings will not be reduced because the budget has been cut. The winter will not get milder, the grass will continue to grow, and safety needs will not become less costly or any less important because we are without funds to attend to these matters.
- The number of needy in the county who are helped by Safety Net when they lose their jobs or have a catastrophic healthcare or financial setback in their lives - who we are mandated by law to serve - will not be reduced simply because the Legislature does not want to provide for their care. We have seen new cases rising as was shown on page 40 of the Budget Message. Unfortunately, the Department of Social Services has seen a spike in the number of Safety Net cases in the past couple of months. The Department advised you of this trend last month. Unfortunately, rather than heed this advice, you have cut into an already lean budget. State law requires us to pay for all who qualify, and pay we shall regardless of the budget cuts. But where will the money come from?

- And in the name of budget cutting the six legislators have added new costs:
  - $10,000 is added to the budget for the Amherst Symphony Orchestra,
  - Overtime is cut throughout the budget, but the County Clerk is to get a $7,500 increase in overtime, and
  - Project Prime Time is to get an extra $20,000.

If the legislature wants to face the consequences of these budget actions, it should identify real cuts that will reduce recurring expenses and thus offset the loss of recurring revenue that is proposed. Rather than do this, those who support this package are hiding behind false cuts that remove revenue, but they do not remove expenses.

Just a moment ago I asked "Where will the money come from to pay for items that are proposed to be cut?" The money will have to come from the small portion of the budget that is not mandated spending.

There is roughly $100 million of discretionary spending in our $1.4 billion budget. Of that $100 million approximately $22 million is allocated to the Library and will be immune from cutting under the proposed budget amendments. Thus, there is only $78 million of spending from which to cut $8.5 million. If these cuts are spread among the discretionary programs, on average, we will see a cut of more than 10% across all discretionary County programs. You know the program areas as well as I do.

- Sheriff's Road Patrol,
- Highways,
- Buildings and Grounds,
- Arts and Culture,
- Tourism,
- Economic Development,
- Environment and Planning and the Land Bank,
- Parks,
- Health including rodent control,
- Mental Health,
- Senior Services, and
- Central Police Services.

These are the very programs that the public has indicated it wants and will pay for. Removing needed funding from risk retention, Safety Net and the other programs will with certainty lead to cuts in the very programs that the people mandated. A number of the supporters of the Amendment Package have said they do not want to cut these program areas. Make no mistake about it: your package will cut these program areas just as much as if you did it directly and intentionally.

Budget Director Keating in just a minute will describe the true impact of these false cuts. Before he does, I want to describe one important consequence.

I can tell you with complete certainty that economic development will become far more difficult if the control board goes hard. Economic development will be far more difficult if we are divided against ourselves. If these budget amendments are adopted, I foresee year-long budget squabbles that will include cut after painful cut in important services including quality of life services. We will find ourselves returning to the days we had hoped to put behind us, where the Legislature and Executive are constantly at odds with each other and nothing gets done. Should this occur, companies will look askance at coming here and I will be constantly explaining why we behave in such an unpleasant fashion.

We should reject the spectacle now playing out in Washington. We are better than that. We can work together to find our own solutions that will be real and enduring. But this means tough, honest decision making, not this type of sham.

I ask you to think long and hard before you plunge us down this path. How many times have we criticized leaders of the past for bad decisions? We no doubt have all done so. We are now at a crossroads for ourselves. It is bad votes like this one that seem so easy when taken that lead eventually to disaster.

These events are occurring on our watch. The onus for this irresponsible proposal will fall on all those who vote for this package. The wounds you feel will all be self-inflicted. However the burden will fall on many innocents who will be impacted by the cuts that are to come.

So, in conclusion,

- we have presented you with a balanced budget with reasonable assumptions and the Control Board concurs,
- The County Executive, the County Comptroller and the Control Board have all warned in no uncertain terms that the amendment package will lead to an out of balance budget,
- we have great opportunities for significant improvements in our county with momentum building and gains now being realized,
- we face a starkly uncertain world with impacts upon us yet to be realized from a hurricane downstate to tempests in Washington that threaten to sweep us up in their wake,
- We have the results of an election here in Erie County in which the electorate spoke in favor of the People's Mandates, and
- We now face a choice: act prudently with the reasonable budget that was presented, or put our heads in the sand and resort to politics as usual here in Erie County.

So, rather than find that we have to sit in an unnecessarily cold, dark county for all of 2013 because we failed to properly provide sufficient revenue to pay our bills and we also failed to turn the thermostat down in time, let us try one more time.

I urge you to reply to the County Executive's request for a meeting where we can hammer out a deal this afternoon. He is prepared to work with you as long as it takes to amend the budget so long as it remains real, honest, and balanced. The people of Erie County deserve no less.

Committee on Municipal Affairs, The Association of the Bar of the City of New York, Proposals to Strengthen Local Finance Laws in New York State, 34 Record, January/February 1979, No. 1/2

THE ASSOCIATION OF THE BAR
OF THE CITY OF NEW YORK
42 West 44th Street, New York 10036

Proposals to Strengthen Local Finance Laws in New York State

By THE COMMITTEE ON MUNICIPAL AFFAIRS

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SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS

The Committee has undertaken this Local Finance Project* because it believes that the time is ripe for re-examination of the basic constitutional and statutory provisions which regulate local finances in New York State. The evidence of this need is the failure of the provisions of existing law to prevent the financial collapse of the City of New York and the severe financial difficulties experienced by a number of other New York State localities.

A short history of the New York City fiscal crisis is set forth in Chapter One of this Report. It shows that for many years the City, with authorization from the State legislature, pursued a policy of deficit financing. This policy proved defeating and self-destructive in several important respects. It undercut the most significant restraint on the cost of local government: the need to impose taxes to meet expenditures. It enabled officials to avoid some of the hard choices required to fit expenditures within the tax revenues they were prepared to vote. Deficit financing, which purported to "solve" a problem for one fiscal year, added to the problems of the next. New deficits were added on top of old and increasing amounts of debt were issued to finance current expenditures.

Constitutional debt limits did not prove adequate to deter this policy. The Constitution did not limit the amount of short-term debt which the Legislature could authorize the City to issue to finance deficits. Debt limits on long-term debt became less significant as state and municipally supported public benefit corporations were used to finance public programs outside the debt limit. Because public benefit corporation debt was not City debt as a legal matter, its practical consequences for City finances was not brought to the fore. And since the Constitution excluded certain important categories of debt from the debt limit calculation, there was no overall limit on the amount of debt that the City could incur.

Constitutional restraints proved deficient for another reason—the Constitution was detailed and complex and because of its complexity tended to provoke compliance with its letter rather than its spirit.

Equally important, the Constitution did not establish a watchdog mechanism to insure compliance with its spirit. Rather than placing responsibility on a public body or officer to halt potentially dangerous financial practices notwithstanding compliance with the letter of the law, the Constitution looked primarily to after-the-fact judicial review. It was obviously more difficult for a court to halt practices that were well underway.

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* In the summer of 1977 the Committee received a grant from the Robert Sterling Clark Foundation, the Fund for the City of New York, and the Lucy Wortham James Memorial and the Mulber Fund of the New York Community Trust to support a study of the debt, budget and disclosure practices of New York State municipalities and to prepare revisions to the State Constitution and statutory laws relating to these matters. In May of 1978 a conference was held at Cornell University at which the Committee's draft proposals were discussed. The initial distribution of this Report occurred in November, 1978.

These constitutional weaknesses would perhaps have been less troublesome had full and accurate information about the City's financial condition been available to voters, investors and the media. While the State required localities to prepare financial reports, the significance of columns of numbers was often difficult to discern. Narrative, readable disclosure of problems and of plans to meet those problems was not generally the practice in the public sector and was not required by State law. Had such disclosure been made, there would at least have been the potential for early warning of difficulties.

Early warning alone, however, would not have been enough without a procedure to compel corrective action. An important defect was the absence of a mechanism for State oversight and, when required, State intervention.

All of the weaknesses described above became particularly visible during the New York City fiscal crisis and its continuing aftermath. In the case of the City, they have for the moment been substantially rectified through the creation of special monitors, the Municipal Assistance Corporation for the City of New York (hereafter MAC) and the Emergency Financial Control Board, and the imposition of special restraints.

But the basic constitutional and statutory provisions against which the New York City financial crisis unfolded are still law. These provisions do not establish coherent and effective restraints against the abuses which have occurred in localities throughout the State. We believe that it is in the interest of every local government in New York State that these fundamental laws be changed.

We therefore propose basic revisions to the Local Finance Article of the State Constitution, a new law to make full disclosure the policy of the State, and a new mechanism for state oversight and enforcement of balanced budget requirements.

A. *Proposed Local Finance Article*

The new Article VIII that we propose in Chapter Two is significantly shorter than the existing article. It is based on the following principles:

> —Local governments can give or loan their money, property or credit only when authorized by the legislature for a public purpose. (§1)

Existing law specifies the purposes for which localities can give or loan money, property, or credit. Its restrictions have been circumvented primarily through the creation of authorities. However, the Committee does not believe that further restriction of the potential for cooperation between public and private sectors is warranted. A majority of the Committee believe that the better approach is to bring about increased public accountability by permitting the legislature to authorize direct financial support to private entities when necessary to achieve a public purpose. Indebtedness contracted in this connection will fall within debt limit regulation. Some members of the Committee believe that the existing gift and loans provision should not be modified. (See pp. 8 and 9, *infra*, for a statement of their views.)

—Debt must be paid. (§2)

The proposed Article clarifies and makes certain what many have assumed to be the case—that the law secures the credit of local governments to the maximum extent. Local credit must be secured at all times so that local governments will not be deprived of necessary resources needed to meet their problems in times of difficulty. A clear requirement that first revenues be set aside in the event of non-payment will help to assure this "crisis proof" credit.

—Debt limits should reflect ability to pay debt. (§3)

Existing debt limits are deficient in part because they are based on a percentage of real property value fixed in the Constitution rather than continuing regulation which takes account of current conditions. They do not adequately restrain local borrowing power. For example, New York City was, as of June 30, 1978, approximately $2 billion below its debt limit despite its lack of access to the credit market and the approximately $5 billion in outstanding MAC debt.[1] The proposed Article provides for long-term debt limits to be set by the Legislature as a percentage of a local government's revenues. Only self-supporting and voter approved debt would be excluded. This approach provides a better measure of ability to pay debt since revenue and not property value is the source of money for debt service. Thus, under our proposal, the dedication of revenues to MAC-type obligations would have a direct impact on debt limits. Further protection against unsound debt limit increases is provided by a requirement that such increases be approved by two consecutive sessions of the Legislature. The proposed Article also provides, in the case of all long- and short-term debt, for additional restrictions, reflecting any current financial difficulties, to be promulgated either by the Comptroller or, if the Legislature so provides, by a Local Finance Board.

Some members of the Committee believe that the Legislature should not have the power to increase debt limits without voter approval. (See pp. 9 to 14, *infra*, for a statement of their views.) The majority, however, believe that the voter approval required by the existing Constitution has not worked to assure effective control of local borrowing.[2] Experience has shown that under any constitutional structure financial abuses will occur. The committee's proposal is designed to limit such abuse by providing a framework for legislative decision, focusing responsibility and prohibiting action in haste.

—Planned deficits should be prohibited. (§§3 and 5)

The proposed Article prohibits a policy of deficit financing. It requires a balanced budget and requires that short-term tax and revenue anticipation debt be issued in anticipation of taxes and revenues and not deficits. Notes issued to finance unanticipated deficits will have to be repaid in the fiscal year following the year in which the deficit is incurred. These are the requirements now applicable to the State.

—Bond Anticipation Notes should not be rolled over indefinitely. (§3)

The proposed Article requires that permanent financing be provided within

five years from the issuance of bond anticipation notes. If permanent financing is not obtained, the notes must be retired in the sixth year.

—The legislature should be authorized to create new regional government entities. (§7)

The Constitution now prohibits the creation of certain new entities having the power to tax and contract indebtedness. The Committee's proposal would not prohibit the creation of new entities if the powers of taxation and borrowing are exercised by elected officials.

The proposal would also continue existing constitutional principles of local finance.

These include the following requirements:

—That a locality pledge its faith and credit to the payment of indebtedness.

—That indebtedness not be contracted for longer than the period of probable usefulness of the object or purpose for which such indebtedness is to be contracted.

—That there be a constitutional limitation on the amount of real property taxes that may be raised for operating purposes.

—That all local taxes be authorized by the State legislature.

—That there be provision for pay-as-you-go financing outside the tax limit. (The Committee proposes to encourage New York City to employ pay-as-you-go financing by giving it the full benefit of this principle without the incurrence of so-called "phantom debt.")

—That the Legislature have the power and duty further to restrict the power of taxation, assessment, borrowing money, contracting indebtedness and loaning of credit so as to insure sound fiscal practices and prevent abuses.

The proposed Article continues constitutional limits on real property taxes imposed for operating purposes at existing levels but does not recommend the approach to tax limits recently taken in California with the adoption of Proposition 13. Proposition 13 reduced the real property tax limit by more than fifty percent and imposed a two-third majority requirement on the approval of new taxes.

We take this position because the issue of tax relief cannot be divorced from the question of what services government will provide to its citizens. The issue of tax relief can and no doubt will be part of every budget debate in the foreseeable future. In that debate, which our proposals are designed to facilitate, the consequences of tax relief for local programs will be identified with particularity and there will be a fair opportunity for those adversely affected to present their position.

The Committee opposes subjecting tax measures to a two-thirds majority requirement for related reasons. The Committee believes that tampering with the traditional approach of majority rule cannot be justified as neces-

sary to tax relief. Indeed it is foreseeable that a two-third vote requirement to increase taxes would discourage tax reductions out of fear that once reduced, taxes could not later be increased despite changed circumstances.

The Committee has considered whether the Constitution should fix an overall limit on all local taxes. We oppose this approach because any limit high enough to provide for contingencies would most probably be viewed as a level of taxation that the people have agreed to accept and be used to justify taxes higher than those required by the needs of the moment.

The Committee recognizes that adoption of its proposed Article would not be a total solution to the problems of municipal finance. However, there are limitations to what can be accomplished at the constitutional level. A Constitution can establish a system of checks and balances designed to control expenditures and we believe that our proposal does this. Controlling the cost of government also requires that sound expenditure, personnel, and tax policies be established at the legislative level. These are matters to which the Committee will continue to devote its attention.

B. *Proposed Disclosure Legislation*

While existing legislation regulating in certain respects the issuance of debt is designed to perform a disclosure function, many deficiencies remain in the scope, quality and presentation of information. Thus, the Committee believes that there is a need for mandatory disclosure legislation. For the reasons set forth in Chapter Three we have concluded that the legislation should be at the State rather than at the Federal level.

The Committee recommends revisions to New York's Local Finance Law and General Municipal Law to construct a comprehensive system of financial disclosure by local governments within the basic framework of existing State reporting mechanisms. The proposal relies on three elements:

—Official Statement

The proposed amendment to the Local Finance Law would require an official statement to be filed prior to the sale of bonds or notes. It would make internal information available in a utilizable form but it does not attempt to fix by statute a detailed listing of the information which would be required. Instead it establishes a flexible format under the supervision of the State Comptroller. The Comptroller is required however to give consideration to "voluntary disclosure standards promulgated by national organizations of local governments." The official statement would be signed on behalf of the issuing entity by an authorized official. The Comptroller has the power to waive the normal disclosure requirements in those instances when an official statement is not appropriate by reason of the size of the issue or the nature of the offerees and purchasers of the obligations.

—Summary Annual Report

The proposed amendment to the General Municipal Law would require a summary annual report of important information drawn largely from the

annual report presently filed. The new summary annual report would also contain a narrative discussion of material facts and trends, information which is not required to be included in existing annual reports.

The summary annual report would contain essentially the same information as an official statement and would provide a regular updating of the kinds of information originally furnished in the official statement. The administrative burden of preparing the summary annual report would be offset by two factors: the form of the official statement would closely parallel that of the summary annual report and explicit provision has been made to allow the summary annual report to be incorporated by reference in subsequent official statements. The requirement of a summary annual report would be applicable only to those local governments which have issued obligations subsequent to the effective date of the proposed amendments, have obligations outstanding at the close of their fiscal year and have not been exempted from such requirements by the Comptroller.

—Timely Independent Examination of Financial Practices

This proposal would amend the General Municipal Law to require that the Comptroller perform an examination of the summary annual report within six months of its being filed if the report is unaudited. As an alternative, local governments would have up to 150 days after the close of their fiscal year to file the report if the financial statements presented therein have been examined by independent certified public accountants.

C. *Proposed Fiscal Monitor Legislation*

To implement the balanced budget requirement contained in the proposed Local Finance Article to the State Constitution, the Committee is proposing new legislation to provide for monitoring of local finances by the State Comptroller. The proposal is based on the following principles:

—Monitoring should be increasingly rigorous as financial difficulties become more severe.

The Committee believes that the State's supervisory resources should be focused on the most severe problems. Accordingly, we have proposed a three-stage monitoring mechanism. The initial stage, applicable to all localities, calls for submission and review of annual budgets and material budget modifications. The second stage, applicable to localities that have incurred a substantial deficit, requires quarterly reports of operations and such additional reports as the Comptroller may deem necessary. The third stage—that of impending fiscal crisis—would be handled on an ad hoc basis through legislative action to establish emergency fiscal controls.

—The Comptroller should set standards for what constitutes a balanced budget.

The Committee believes that the Legislature should not attempt to define what constitutes a balanced budget. This is a technical question dependent

in part on evolving accounting methodology and should be entrusted to the Comptroller who has a staff with expertise in this area.

—The Comptroller should have authority to go to court to compel compliance with local finance laws and regulations.

In order to have effective compliance with laws relating to local finance we believe it is desirable to make the official responsible for monitoring also responsible for enforcement. It is expected that in most situations the possibility of court action by the Comptroller will be sufficient to bring about compliance. This approach also serves to protect against arbitrary enforcement since the Comptroller would have to establish in court a basis for the relief sought.

STATEMENT OF MINORITY AND INDIVIDUAL VIEWS

MINORITY STATEMENT

We agree with the Committee's objections to the complicated nature of Article VIII of the Constitution and the untidy and confusing amendments to it. However, we disagree with its recommendations to eliminate the debt limit provision in the Constitution and the removal of the prohibition against the gift and loan of local governments' credit.

The slow process of constitutional amendment, often deemed too cumbersome, is designed to be just that. It affords ample time for public debate and close scrutiny.

Gifts and Loans

The Committee states that the provisions of proposed Section 1 of Article VIII "represents a basic change from New York's traditional prohibition against gifts and loans now contained in Section 1 of Article VIII." (Report at p. 27.) The new provision would permit loans and guarantees of loans to both public and *private* corporations. It would permit public ownership of private corporate stock when authorized by the legislature.

Such a change would take us back to days prior to 1846. The Committee suggests that "nineteenth century prohibitions are ill-suited to the demands of contemporary society." (Report at p. 28.) Those nineteenth century prohibitions were adopted by the people to restrain the demands then made on the public treasury. What is now proposed is the removal of those prohibitions so that public funds can be made available to contemporary (larger) demands.

In the twentieth century, (1938), the prohibition against the gift or loan of state credit was extended to public corporations.

When previously presented to the people in this century, the changes now proposed have been rejected. As the Committee states, the proposed 1967 constitution would have permitted "local governments to make gifts and loans . . . 'for economic and community development purposes (and) for public purposes.'" That constitution was rejected. Again, in 1971 a similar amendment was proposed (The Community Development Amendment) and rejected by almost two to one.

Unless the state and local governments can be fully secured against loss, the gift or loan of governmental credit should be reserved for traditional public purposes.

To permit government to become the lendor or guarantor of last-resort for private enterprises which cannot obtain conventional financing is an invitation to disaster.

Stock in the nineteenth century railroads proved to be inadequate security. Would stock in any of our once proud Twentieth Century railroads have been any better?

Debt Limit

Unfortunately, in its attempt to untangle the constitutional confusion, the Committee has chosen to follow the well travelled path mapped by other committees[8] and urges elimination from the Constitution of the ceiling on debt which local governments may incur. The limit has been included in the State Constitution since 1884. Theretofore, the Legislature had authority to fix such limits. The abuse of that freedom led to the 1884 constitution.

However, what the Committee overlooks in its search for simplicity and order, is the basic reason for *including* the debt limit provision in the Constitution. That restraint was designed to leave to the people of the State the power to decide, through the prescribed referendum procedure when and to what extent borrowing should be permitted beyond the amount specified by the Constitution. The Committee proposes that the Legislature again be vested with the power to determine from time to time the amount which each local governmental entity may borrow.

The constitutional requirement that the people be asked to vote on creation of new debt was first imposed upon the State by the 1846 Constitution. That Constitution was adopted following a period in which the State lent its credit to railroads which were severely hit in the so-called Panic of 1837. The State was then forced to pay debt without anticipated revenues.

As the Committee report states, the constitutional limit on local debt was adopted in 1884 following another period of railroad expansion, speculation and collapse. The impact of that crisis produced a constitutional amendment fixing the amount of debt local governments might incur. To exceed the limit the approval of the people through constitutional amendment was and is required.

Our objection to the inclusion of this proposal is not based upon political considerations. To the contrary, our concern is based upon our perception of governmental problems which representative government now faces in the United States and in this state.

Over the past 20 years, we have seen an increasing divergence between the attitudes of elected officials concerning the expenditures of public funds and the attitudes of the people on the same subject. Initially this divergence was

reflected in repeated rejections by the voters of proposals by elected officials to borrow and spend government funds. While those rejections were chastised by molders of public opinion as short-sighted and selfish, from a perspective of 10 to 15 years later, the popular reaction seems far more rational than it once did.

The divergence between the attitudes of public officials and the people has expanded and is now regarded in many parts of the country as a taxpayers' rebellion. California's Proposition 13 is the latest example of the breadth of the divergence.

In a democratic society, one cannot simply reject repeated popular responses to public issues as selfish and short-sighted, unwise or improper. One must attempt to understand what the public reaction reflects in terms of the operation of our democratic institutions.

In the context of repeated rejections of governmental proposals to borrow and spend money, we appear to be in an era when the people are prepared to give less flexibility rather than more to their elected officials. In light of the manner in which elected officials have utilized their flexibility in the past, we are unprepared to say that the popular attitude is wrong.

Indeed, absent such popularly-mandated restrictions upon the power of government officials, it may very well be that representative government will be unable in the future effectively to perform the essential role of harmonizing the governmental needs and aspirations of the people who are governed.

The Committee proposal disregards all of the above. It adheres to the traditional approach to representative government which seeks to maximize the discretion afforded to public officials. We are not so sure that that traditional approach is as valid as it once seemed.

We do not believe that this is the time to further enhance the discretion of public officials over borrowing on the people's behalf of funds which the people have repeatedly demonstrated they do not wish to see borrowed and which they are increasingly demonstrating they do not wish to have government spend.

The damaging effect of leaving such decision making to the Legislature, as is advocated by the Committee majority, is presented in awesome detail in the report. The results of evading the public decisions to reject borrowing proposals made by the Legislature and the executive by issuance of "moral obligation bonds" is equally clear. The UDC Moreland Act Commission called it "deceptive" (*supra*, at p. 60).

In its report in 1967, the distinguished Special Committee on the Constitutional Convention of this Association (with one member disagreeing) recommended the same solution as that now proposed. In doing so, that Committee wrote:

> "The history of repeated amendments or attempts *at amendments* of the debt limit, particularly for New York City, show clearly that the present provisions are too restrictive in terms of the *desires* of the people of New York City and their government (emphasis supplied)."

The difficulty with that statement stems, it is submitted, from the assumption of some office holders that they *know* what it is that the public "desires." That knowledge transcended negative votes by the people of the state and included the rationalization that the people did not understand the wording of the referendum proposal written by those in office.

We suggest that the public is aware that money borrowed must be repaid with interest and that tax revenues must be devoted to that repayment for many years. The public is interested in and is demanding reduced taxes and less borrowing: The Committee proposal is designed to facilitate (increase) borrowing.

While the committee report eschews any attempt to rid the Constitution of its tax limitations—a proposition for which there are at least as many compelling arguments based on governmental convenience and a history of circumvention and attempted circumvention (see, e.g., *Hurd* v. *City of Buffalo*, 34 N.Y. 2d 628 (1974); *Waldert* v. *City of Rochester*, 44 N.Y. 2d 831 (1978))—it fails to recognize (or admit that removing the debt limitations from the Constitution in effect further weakens the protection of the taxpayers' purse that tax limitations were designed to accomplish. Larger debts will require larger debt service which in turn will require larger tax collections which are not subject to the constitutional tax limitations.

The Legislature of the State of New York has for many years been considered one of the outstanding deliberative bodies in the country. New York statutes have served as models in many fields. It should be permitted to devote its efforts to appropriate legislative matters. The people should retain their present vested right of deciding if funds should be borrowed in excess of the debt limit. This is not to say that some change in the public participation process may not be useful. The Special Committee in 1967 suggested that a local referendum be utilized in some cases rather than a statewide referendum. Such an alternative in the case of smaller communities or in the case of small issues might be desirable.

The danger inherent in eliminating the debt limit is that when operating expenses again become overwhelming, a ponzi style effort to capitalize them will once again be presented to the Legislature by desperate local officials. A legislature should not be pressured under such circumstances to permit unwise borrowing.

It is argued that innovative financing techniques may be authorized by the Legislature on request of local governments in order to promote industrial and commercial development. That is true, but eliminating public participation in authorizing borrowing in excess of constitutional debt limits is not a prerequisite to such innovation. Tax abatement programs now being utilized appear to be encouraging substantial new construction. Such programs are, it is submitted to be preferred since they do not saddle the public with long term obligations in the event the project fails—as they have in the past—and revenue is all that is lost since no debt was incurred and no interest and no principal need be repaid to bond holders.

Various alternatives have been suggested: remove the constitutional limit but require a two-thirds vote in the Legislature; require an affirmative vote in two different legislative sessions; require approval by a Special Committee

or " Borrowing Board." None of these suggestions, however, has the same restraining effect on increasing government cost that the people—those who must pay—can have.

Avoiding decision by the people placed New York City and New York State in financial jeopardy. We should not compound the errors of the past by institutionalizing them. If we do, we will, it has been said, relive history.

The two session proposal goes back at least to the staff report of the Temporary Commission for the Simplification and Revision of the State Constitution (No. 31, at 111).

The Commission itself, however, did not agree with the staff and wrote that it was "convinced that New York State has been fortunate in having the basic principles for control of public borrowing firmly rooted in the Constitution, . . . (and that) the State of New York is not now ready to remove debt and tax limits from the Constitution." Temporary Commission on the Revision and Simplification of the Constitution, *Simplifying a Complex Constitution*, N.Y. Legislative Doc. No. 58, (1961) 20.

One method of relieving the complexity of the provisions of Article VIII without scraping the constitutional debts limit was proposed in 1967 by Mayor Lindsay's Task Force on the Constitutional Convention. That distinguished group wrote (*Report and Proposed Constitutional Amendments.* The Mayor's Task Force on the Constitutional Convention, May 9, 1967 at pp. 8 and 9):

> "All the special debt limit exclusions which are applicable only to New York City should . . . be abolished. To replace (them) . . . , the City's general power to incur indebtedness should be increased from 10% to 15% of the full value of taxable realty, based on a three-year rather than a five-year moving average."

Similarly, in 1967 the Special Committee on Revision of the State Constitution of the New York County Lawyers' Association, wrote in part as follows in connection with local government finance:

> "The constitutionally mandated limitations should be retained but (a) the limitations on local indebtedness contained in Article VIII should be eased so that there may be a consolidated higher limit on all tax supported debt and (b) the limitations on the amount to be raised by real estate taxes for local participation contained in Article VIII should be increased." (Recommendations for Revision of the New York State Constitution, Reports of the Special Committee, New York County Lawyers' Association, May 1967).

We are convinced that efforts to facilitate borrowing are ill-advised. Moreover, we believe, it remains essential for the people themselves to participate in authorizing public borrowing. Improvement and modernization of the existing provisions is desirable, but not at the expense of elimination of public participation.

In *Wein v. State*, 39 N.Y.2d 136, 142 (1976), Judge Breitel after describing the "desperate financial crisis in New York City" (ibid, at p. 140) and the MAC escape mechanism wrote:

> "If the city and the state had enormous aggregate temporary debt, without immediate provision for its liquidation or valid refunding in the aggregate it would be demonstrative that either the constitutional plan is not exact enough to prevent what has happened or that the plan has been violated.
>
> For the reasons to be stated it is concluded that there has been no constitutional violation, but it is apparent that the state in avoiding violaion has been driven to the brink of valid practice."

We believe the general approach taken by the Committee towards assessing the capability of a municipal corporation to incur indebtedness, by utilizing a more comprehensive barometer of its revenues than is provided by the present system of relying on real property values, is a step in the right direction. We disagree strongly with the Committee's suggestion that the firmness of constitutional debt limitations be jettisoned in favor of an approach which leaves it to the sole discretion of the Legislature to determine appropriate debt limitations. Indeed, the Committee's proposal for a "two Legislature" vote on increasing debt limits (without even an intervening election) seems a painful attempt to stifle the voice of the taxpayer who, needless to say, will pay through taxes for the increased debt service which increased debt will inevitably engender.

We believe that the Constitution should contain debt limitations which are based on a more comprehensive assessment of a locality's finances than the current system of relying on real property valuations. However, the process of both fixing the appropriate limitations in the first instance and for amending them should be left to the current process of constitutional amendment which will serve to discourage borrowing as the ultimate solution to governmental problems.

The minority's objection is that the legislature must have restrictions placed upon it—that is the fundamental concept of a constitution.

History has shown the inability of the legislature to resist the needs of local government when that legislature does not have to bear the responsibility for the fund raising. History has also shown the flexibility of the definition of revenue and its inconsistent pattern, especially when dependent upon federal and state grants to local communities.

The difference between the majority point and the minority position is clear. The majority places within the hands of the legislature discretion and flexibility. The minority wishes that flexibility and discretion be placed within parameters set by the people.

Theodore P. Halperin
Burton H. Marks
Clarence J. Sundram

Edward N. Costikyan and Edith Spivak agree with the minority report with respect to retention of constitutional limits on local government debt.

Charles G. Moerdler joins in the minority statement to the extent only of supporting its position on the gifts and loan section (i.e., in opposing the proposal of the majority report that would permit loans and guarantees of

loans to private corporations or permit public ownership of private corporate stock).

ADDITIONAL STATEMENT

JOHN V. CONNORTON, JR. concurs in the Committee's recommendation to substitute a broad "public purpose" standard for the more detailed prohibitions against gifts and loans now contained in Section 1 of Article VIII. Mr. Connorton, however, believes that where the Legislature authorizes a local government to give or loan its money, property or credit to a private individual, corporation or undertaking, some additional safeguard should be established such as requiring a two-thirds instead of a majority vote for legislative action.

CHAPTER ONE

CONSTITUTIONAL AND STATUTORY BACKGROUND

The Constitution of the State of New York imposes detailed restrictions on the issuance of debt by local governments. In 1975, despite these constitutional safeguards, the City of New York was unable to pay certain of its notes as they came due and lost access to the public credit market. In the same year the City of Yonkers also had a severe fiscal crisis. These crises and difficulties experienced by other local governments demonstrate a fundamental inadequacy in the laws governing local finance in this state.

This chapter sketches the history of constitutional and statutory regulation of local finances in the State of New York and identifies some of the major problems revealed by the fiscal crises in New York City and other localities.

A. *Historical Background*

Local governments did not incur large debts until the early Eighteen Hundreds. At that time the issuance of municipal securities required specific approval by the Legislature. Thus, in 1812 the City of New York first petitioned the Legislature for permission to issue funding bonds. It sought this authority to pay off short-term debt incurred by the City for capital improvements including the present city hall.[4] When the Legislature authorized the issuance of the bonds, it did so under the impression that it was "establishing the credit of the corporation on a solid basis."[5]

By the 1840's local governments had begun to issue bonds for the purchase of stock from railroad companies which agreed to construct railroad lines through their territory. Apprehension over this practice as well as increasing tax rates brought on agitation for constitutional restrictions on municipal indebtedness.[6]

At the 1846 Constitutional Convention, the Committee on Municipal Corporations reported an article that would have put substantial restrictions on the issuance of local debt.[7] The Committee's proposal was rejected and a clause put in its place which made it the duty of the Legislature to provide for the organization of cities and incorporated villages, "and restrict their

power to taxation, assessment, borrowing money, contracting debt, and loaning their credit."[8]

Pursuant to this constitutional provision, in 1853 the Legislature enacted Ch. 603 "to restrict and regulate the power of municipal corporations to borrow money, contract debts or loan their credit." Unfortunately, its provisions were too restrictive. Cities and villages continued to resort to their old practice of having the Legislature enact special bills authorizing them to incur debt for specific amounts, projects, and lengths of term.

At the 1867 Constitutional Convention several amendments were introduced to limit the amounts and purposes for which a local government could incur indebtedness, and to prohibit the lending of local credit to private enterprise.[9] After considerable debate all the proposed amendments were rejected.

Without legal obstacles, local debt increased in the decade following the Civil War, on the average, at twice the rate of the increase in assessed property value. As one commentator has noted:

> Borrowing was freely indulged in, even to pay the current expenses of government, and the loans were extended through refunding operations rather than paid off, while taxes were allowed to go delinquent and sometimes were not levied at all.[10]

Instead of curbing the abuse in public borrowing, the Legislature in 1869 enacted Ch. 907, the Town Bonding Act, which gave towns blanket authority to lend money to railroads.[11]

The Constitutional Commission of 1872–73 was created by the Legislature in response to a message from the Governor that called for, among other things, a constitutional provision "limiting the amount of indebtedness which municipalities may incur, and defining the purpose for which it may be incurred."[12] The Committee on Local Indebtedness recommended that the indebtedness of cities, towns and villages be limited to ten percent of assessed property valuation. This proposal was rejected by the Commission.[13] Instead, a substitute amendment was adopted by the Commission and subsequently approved by the Legislature and the people in 1874. This "gifts and loans" provision was the first direct restriction on municipal debt in the New York Constitution. It is substantially the same as the present Art. VIII, §1. While it restricted the purposes for which a municipality could incur debt, it did not restrict the amount. That occurred ten years later.

In the aftermath of the 1873 depression, Governor Tilden called for the establishment of a Commission to study growing municipal debt and the heavy tax burden. The Tilden Commission found that the "public debt of the City of New York, or the larger part of it, represents a vast aggregate of moneys wasted, embezzled or misapplied."[14] It made a number of recommendations. They were not adopted but they focused attention on the problem of municipal debt.

In 1884 a constitutional amendment was adopted which imposed a debt limit and a tax limit on cities with a population of over 100,000 (at that time New York, Buffalo and Rochester) and their counties. The debt limit was

fixed at ten percent of the assessed value of real estate. The tax limit for county or city purposes was fixed at two percent of the assessed value of real and personal property. No tax limit was put on the amount required for debt service. At the 1894 Constitutional Convention the debt limitation was expanded without much discussion to include all cities and counties.[15]

During the period from 1894 to 1938 these constitutional debt limits were liberalized on a piecemeal basis in order to enable cities to finance public improvements. A city would get around the debt limit by increasing the assessed value of real estate or by securing constitutional changes which applied only to the particular situation in the city or a group of cities. The changes took place in 1899, 1905, 1917 and 1927 and were attempted on other occasions. There were no changes during the Great Depression because there was little locally financed improvement. The effect of these changes was to burden the text of Art. VIII of the Constitution "with a multitude of detailed specific exemptions and qualifications, often of an extremely transitory or inconsequential nature which lengthened the text considerably and made it unwieldy and difficult to understand."[16]

A new local finance article was adopted at the 1938 Constitutional Convention. School districts were brought within the "gifts and loans" provision. The term "corporation" was amended to permit the giving or loaning of money or property, but not credit to public corporations. It incorporated those provisions which the drafters felt were ". . . essential . . . to preserve and strengthen local credit."[17] They were as follows:

—indebtedness may not be contracted beyond the period of probable usefulness of the project and in any event not for longer than forty years;

—refunding may not be used to extend repayment of debt beyond the period authorized;

—all indebtedness shall have behind it the faith and credit of the issuing locality;

—all indebtedness other than temporary debt shall be serial bonds payable in annual installments and no installment of principal, except in the case of refunding, shall be more than 50 percent in excess of the smallest prior installment;

—New York City may issue either serial bonds or sinking fund bonds with a maximum maturity of fifty years for water supply, rapid transit or dock construction;

—annual appropriation for interest on all indebtedness and principal on bonds and certain short term obligations shall be made; if there is a failure of such appropriation, the "first revenues" of the locality shall be set apart for such purpose.

A new Section 3 prohibited the creation of a municipal or other corporation (other than counties, cities, towns, villages, school districts or fire districts) possessing both the power to incur debt and to levy taxes or assessments upon real estate.

Towns and villages were brought under the Constitutional debt limits. In place of the existing uniform debt limit of 10 percent, different percentage limits were established for the different classes of government. The computation of the debt and tax limits were tied to a five-year average assessed real property value rather than to the annual assessment. Other sections gathered together the various debt exclusions with some clarifications and extensions. A new section excluded from the tax limit—but not the debt limit—certain expenditures for capital improvement made from current revenues. This provision was adopted to encourage pay-as-you-go financing. The debt incurred under it is called "phantom debt" because bonds are not issued.

The tax limit was extended to all cities and villages although the effective date was postponed. The computation of that tax limitation was modified to exclude personal property. The taxes which could be raised for operating purposes were reduced by the amount of taxes raised for the payment of the debt service on certain short-term debt.

At the 1938 Convention the delegates also adopted a housing article (designated Article XVIII) to enable the State and its political subdivisions to provide low rent housing for persons of low income and for the rehabilitation of substandard areas. It also provides for a housing debt limit of two percent over and above the general debt limit prescribed by Art. VIII, §4.

After the adoption of Articles VIII and XVIII in 1938, it became obvious that statutory law in New York would need revision to bring it into harmony with the Constitution. Inoperative provisions would have to be revised and operative provisions relating to local finance would have to be brought together in a single chapter.[18]

As a result, the Municipal Finance Commission was created.[19] Its draft Local Finance Law was adopted by the Legislature in 1942.[20] Subsequently, the Commission offered extensive amendments including a Schedule of Laws Repealed before its existence and powers were terminated on March 31, 1947.[21] The Local Finance Law has been amended frequently since then, but has remained the basic law governing the issuance of debt by local governments.

The delegates to the 1938 Constitutional Convention hoped to achieve a uniformity of constitutional policy in the new article and many of the provisions they adopted were analogous to then existing constitutional provisions relating to state indebtedness or to existing statutory requirements.[22] No doubt, many of the changes reflected the thinking on local finance during the Depression, but they were to prove inappropriate to conditions during a period of prosperity. The fact that the Constitution had to be revised again in ten years is "a commentary on the tradition of more than half a century that led to the inclusion of these changes . . . in the Constitution rather than in a general statute."[23]

In December, 1947, State Comptroller Frank C. Moore appointed a 16 member committee to study and offer recommendations concerning the constitutional debt and tax limits and the fiscal relation between cities and their

school administrations. The Committee issued several reports which led to numerous changes in the local finance provisions of the Constitution and conforming changes in statutory law.[24]

Between 1949 and 1953, amendments implementing the following Committee proposals were adopted:

—the exclusion of budget notes from the debt limit;

—the exclusion of certain revenue producing debt;

—the substitution of full value for assessed value in the computation of debt and tax limits;

—the exclusion from the New York City debt limit of certain debt for health, transit and educational purposes;

—except for New York City, authorization for pay-as-you-go financing outside debt and tax limits;

—the establishment of separate debt limits for school districts within certain cities.

While the work of the Committee was necessary in the light of the conditions of its time, as was the work of the 1938 Convention, the result was a complex local finance article several times longer than that adopted in 1938.[25]

Since the early 1950's, when the Moore Commission made its proposals, local finance amendments to the Constitution have been few.[26] The proposals for change, however, have been dramatic. The most notable attempt at revision was made by the 1967 Constitutional Convention which sought to simplify the gift and loan and debt limit provisions, and to combine the housing and general debt limits. This simplified local finance article went down to defeat when the people disapproved the proposed Constitution in 1967, apparently over the issue of state aid to religious institutions. It is not clear how the article would have fared on its own.

B. *The New York City Fiscal Crisis*

This section explores the question of how, with so much constitutional and statutory detail on the subject of local finance, the New York City fiscal crisis could have occurred.

In the early 1960's, the City of New York began to have annual budget deficits.[27] They were financed by deficit borrowing. The Temporary Commission on City Finances warned in 1966 that this "might well lead to further deterioration in the City's credit standing."[28] Unfortunately, by that time the City was deeply committed to the practice.

The financing took many forms. First, the City borrowed from itself. It had a "rainy day fund."[29] The City is required by law to contribute to this fund, so that in lean years it has a ready source of cash. From June 30, 1961 to June 30, 1965 the cash balance in the fund decreased from $69.9 million to $155 thousand. Other reserve funds were similarly depleted.[30]

In addition to borrowing from the rainy day fund, the City had local legislation passed relieving it of the duty to make appropriations to the fund for fiscal year 1963.[31] The City Council passed legislation waiving the appropriation requirement again in 1964 and for each fiscal year beginning in 1968.[32] According to the New York City Comptroller, had the rainy day fund been "maintained and replenished as required by the Charter, it would have provided a cushion of over $280 million at the point . . . [in 1975] when the City faced a possible shutdown of operations for lack of cash."[33] The Comptroller also drew a gloomy picture of the Tax Deficiency Account (another of the City's reserve funds) which "at the end of calendar year 1975 had a debit balance of $175.5 million, by far the largest debit balance in the history of this account. This total represents, for the most part, money which the City had expected to obtain in real estate taxes . . . but which never materialized."[34] The debit balance in this account grew to more than $300 million by June 30, 1976.[35]

In addition to depleting its reserve funds, the City issued short-term notes to balance its budget. In fiscal years 1962, 1963, 1964 and 1965 it issued budget notes in the amounts of $10, $27, $30 and $39 million, respectively. In fiscal year 1965, it began to issue revenue anticipation notes (RANs) to balance its budget.[36] It did so pursuant to legislation which permitted the City to issue RANs in a fiscal year in anticipation of revenues attributed to or based on transactions or activities occurring during April, May and June of the fiscal year, but not received or collected until after the close of the fiscal year.[37] In other words, the City could use the following year's revenues to balance the current year's budget. The City's legislative memorandum said the bill would enable the City to borrow approximately $50,000,000 in the 1964–1965 fiscal year, but would "not increase the temporary borrowing power in subsequent fiscal years."[38] In fact, the City continued to use this so-called "June accrual" to provide cash for the City at the end of each fiscal year. This practice resulted in $358 million of the City's cumulative deficit.[39]

The same act which provided for the June accrual amended the Local Finance Law in a manner which was to have an even more serious impact on City finances. Prior to 1965 the total amount of RANs which the City could issue was limited to the amount of revenues actually collected or received during the preceding fiscal year. The legislation removed this limitation and tied the City's power to issue RANs to the amount estimated in the annual budget. The City argued that it would receive approximately $58 million more school aid from the State for fiscal year 1965–1966 than for fiscal 1964–1965, and that its bill would permit the City to borrow in early fiscal 1965–1966 in anticipation of the increase.[40] This had the effect of permitting borrowing against optimistic revenue estimates and the building of a cumulative deficit as notes were rolled over when anticipated revenues did not come in. In 1971 the law was changed again to permit issuance of RANs redeemable from federal and state aid on an "overall basis" rather than from specific types of revenues.[41] This tended to obscure a shortfall in a specific type of revenue.[42]

The issuance of tax anticipation notes (TANs) by the City resulted in more deficit financing. TANs are notes issued in anticipation of real estate

tax revenues. The City had on its tax rolls property which was not subject to taxes, e.g., diplomatic, publicly-owned, Mitchell-Lama, and "in rem" property. This practice tended to increase the estimate of real estate taxes to be collected and the amount against which the City could borrow. The City also made inadequate provision for taxes uncollectible because of defaulting taxpayers or tax cancellations or remissions. Nevertheless, the City issued TANs against these revenue estimates. Notes were rolled over when anticipated taxes were not collected. Most of the TANs outstanding at the time of the fiscal crisis were issued against such revenues, reflecting a deficit of hundreds of millions of dollars. Indeed, the State Comptroller has estimated "that the $502 million of real estate taxes receivable on the City's books at June 30, 1975 were overstated by approximately $408 million."[43]

The City's deficit financing was not confined to short-term borrowing. In 1965, the City sponsored a bill to permit it to issue five-year serial bonds in the amount of $255.8 million to finance the cost of the City's pension retirement liabilities during the fiscal year 1965–1966.[44] The City argued that it needed the money to meet the automatic increase in pension liabilities mandated by Art. 5, §7 of the Constitution and that the bill was necessary to prevent economic hardship.[45] Although the constitutionality of the law was upheld in *Bugeja v. City of New York* on the grounds that the pension and retirement payments involved were not of "purely transient usefulness," the City did concede that the true purpose of the bond issue was to bridge a gap in the current ordinary expense budget.[46]

Since the pension borrowing occurred only once, it was not to have a lasting effect on the City's finances. The practice of borrowing for items which would, under generally accepted accounting principles, be treated as ordinary expenses had more significance in the long run. The Temporary Commission on City Finances in 1966 condemned this practice as unsound and recommended that current expenses be removed from the capital budget and that perhaps the City should "be compelled to do this by amendments to the Local Finance Law."[47]

The contrary occurred. The City sponsored legislation in the 1960's and the early 1970's amending the Local Finance Law to permit all sorts of borrowing for current expenses. A period of probable usefulness was added to permit borrowing for "job and business opportunity expansion programs of municipalities."[48] It was justified as an investment in human capital as opposed to bricks and mortar. It was eventually used to support the financing of the operations of the City's vocational high schools through the issuance of bonds, even though vocational education is a recurring ordinary expense of government. A period of probable usefulness authorized the issuance of bonds to pay rent.[49] It seemed as if the City could borrow for anything.

In 1974, the Court of Appeals in *Hurd v. City of Buffalo*[50] held unconstitutional a statute which established a period of probable usefulness for the costs of the pension and retirement liabilities of the cities of Buffalo, Rochester and Yonkers. It distinguished the *Bugeja* case, *supra*, on the ground that the statute in *Bugeja* involved a one-time funding of pensions and retirement obligations, whereas the statute in *Hurd* involved an ongoing

funding of such contributions. The *Hurd* case put into question other periods of probable usefulness of a similar nature and their application to the City. By the time the *Hurd* case was decided, however, the City was issuing hundreds of millions of dollars of bonds for capitalized expenses each year.

A Temporary Commission on City Finances noted in 1977:

> In fiscal year 1965, $26 million of operating expenses was capitalized; by fiscal 1975, when the City's financial structure almost collapsed, $724 million of capital funds, over one-half of the entire capital budget, was used to finance operations.[51]

It was not until the fiscal crisis that the law was changed to require a ten year phaseout of this practice by the City.[52]

For the City to issue bonds for capitalized expenses, it had to make room for them within its legal debt incurring capacity. One way it did so was by excluding other debt from its debt limits. An amendment to the Local Finance Law, sponsored by the City in 1968,[53] enabled a municipality to elect whether to charge housing and urban renewal debt to the 2% housing debt limit,[54] or the 10% general debt limit.[55] Because the standards for exclusion of bonds for revenue producing projects are stricter under the 2% limit[56] than under the 10% limit,[57] this option allowed the City to expand its debt incurring power.

Even if the City had retained its credit standing in 1975 the sheer volume of its financing would have proved difficult for the market to absorb. The Municipal Assistance Corporation for the City of New York (MAC) has calculated that in 1975 the City had long-term financing needs of $500 million quarterly for capital and operating expenses, and short-term financing needs of $750 million monthly, and that the City's short-term debt had grown to $4.5 billion and its long-term debt had increased to $6.8 billion, a total City debt of more than $11 billion.[58] Significantly, between 1966 and 1975, the City's short-term debt grew from 8.5% to 36.9% of its total debt.[59] It is short-term debt that must be paid or renewed annually.

In 1976 over $1.2 billion, or more than one quarter of the City's outstanding short-term debt, was in the form of bond anticipation notes (BANs) related to limited profit (Mitchell-Lama) housing.[60] If the City had not had Mitchell-Lama BANs to renew in 1975 its financing burden would have been eased considerably. The statute requires that BANs issued to make loans to limited profit housing companies or their renewals "may extend not more than five years beyond the original date of issue of such notes."[61] Starting in 1969, however, when a proviso was added extending the period to six years for BANs issued prior to 1965,[62] the period was routinely extended with the result that the BANs were not converted into bonds.

The City also has statutory and/or contractual arrangements with certain public benefit corporations (PBCs), which in many ways have served as the equivalent of issuing City bonds and notes. Some of the PBCs, like the N.Y.C. Housing Authority and the N.Y.C. Transit Authority, had been in existence for a long time, but some were created in the 1965–1975 period by the Legislature at the urging of the City. Some of the new PBCs were created for

highly esoteric financing schemes which did not materialize.[63] Other PBCs, however, issued hundreds of millions of dollars worth of their bonds and notes to finance, operate and construct hospitals, schools, housing and other facilities on behalf of the City, supported directly or indirectly by City credit or revenues on a contingent or non-contingent basis. The arrangements with the PBCs fell into four categories: guarantees, executory lease arrangements, capital reserve fund arrangements, and executed leases.[64] This vast array of statutory and contractual arrangements enabled the City to minimize or avoid debt limit charges and tended to dilute the City's credit.

By the Spring of 1974, New York City was in serious financial difficulty. At the request of the City the Legislature created the New York City Stabilization Reserve Corporation (SRC).[65] The SRC differed from other PBCs in that it did not construct facilities or provide services. Its sole function was to sell $520 million of its bonds and notes and to turn the proceeds over to the City. In the SRC Act the Legislative findings and declaration of purposes stated that:

> . . . the City of New York is faced with a *grave and unprecedented fiscal crisis* which threatens the city's ability to provide essential services and thereby endangers the welfare of all the inhabitants of such city. . . . Accordingly, . . . it is necessary for a corporation to be created to assist such city to enable it *to provide such essential services* during the nineteen hundred seventy-three—nineteen hundred seventy-four and nineteen hundred seventy-four—nineteen hundred seventy-five fiscal years of such city on *a sound financial basis*.[66] (emphasis supplied)

In accordance with the SRC Act,[67] the Mayor certified to the corporation $150 million as the amount required by the City for the 1973–1974 fiscal year, and $370 million as the amount required by the City for the 1974–1975 fiscal year, and he included the latter amount as a revenue in his proposed budget for the 1974–1975 fiscal year.[68]

A few days before the scheduled sale of SRC debt in 1975, a lawsuit was filed against the City demanding that the SRC Act be declared unconstitutional as a loan of the City's credit and that the defendants be enjoined from issuing SRC bonds and notes. The suit also claimed that SRC debt and the debt issued by certain other PBCs were, in reality, City debt, and that the City was therefore in excess of its Constitutional debt limits. The City postponed the sale of the SRC notes while the case was in the Courts. In May 1975 the Court of Appeals affirmed the validity of the SRC Act by a 4 to 3 decision,[69] but by that time the City was out of the public credit market. SRC never issued any of its obligations, but the decision upholding it paved the way for the creation of MAC.

The foregoing is a brief and by no means exhaustive review of the many ways the City borrowed directly or indirectly to meet its annual deficits, or managed to avoid debt limit charges. A large portion of the deficits were not funded or were paid for by unfunded short-term debt, leaving the City with a huge cumulative unfunded deficit. The City's deficient accounting system tended to conceal the actual amount of these unfunded liabilities.

For example, the City incurred huge pension liabilities and accounted for them on a cash basis rather than on an accrual basis, so that the true cost of its annual pension liabilities was not reflected in its annual budget.[70] The City Actuary has estimated that the unfunded accrual liability of the five major N.Y.C. actuarial pension systems was $6.95 billion as of June 30, 1975, and that there was approximately $1.2 billion of unfunded liability on account of the non-actuarial pension systems.[71]

Additionally, the precise amount of the City's cumulative deficit was in doubt for a long time after 1975 because, according to the SEC, the City's internal accounting controls "significantly hindered the City's capacity to generate financial data which was reliable and accurate."[72]

Finally, there was only limited disclosure of information, in a form useful to investors, regarding the City's deficits and liabilities. The City did not issue an Official Statement until 1976 when it was out of the public market, though it did issue a statement of essential facts in March, 1975, in connection with its last note sale to the public.

The accounting practices, the poor internal controls and the lack of disclosure not only affected the investing public's ability to evaluate the City's finances, it also affected the decisions of public officials. Had the true condition of the City's affairs been common knowledge prior to the fiscal crisis, there might have been some fiscal retrenchment. Indeed the program of disclosure and independent auditing which the City has been pursuing since 1975 has no doubt increased public understanding of the need for fiscal restraints.

But even had there been a good early warning system to alert City officials and the public that a financial storm was brewing, the City might not have been saved from the agonies of fiscal crisis and default on its short-term debt. There were inadequate controls over the issuance of short-term debt. That made possible the accumulation of unfunded debt and at the same time made the City vulnerable to market conditions. There were insufficient expenditure control mechanisms and little external pressure to cut expenditures or increase revenues to respond to changing economic conditions or to avoid foreseeable deficits during the fiscal year. The checks and balances within state and local governmental structures were inadequate to prevent deficits.

Many economic, social and political factors have been cited as the causes of the City's fiscal crisis. These include inflation, slow economic growth, shifting populations, militant unions, increased reliance on variable intergovernmental assistance, loss of jobs, unemployment, crime, urban decay, and unsound allocation of expenditure burdens as between the City and higher levels of government.[73] These issues are beyond our scope. Others have documented these underlying causes of the fiscal crisis and done it well.[74] Our concern is deficit financing, which was the governmental response to the City's problem. This practice proved to be destructive and self-defeating.

C. *Deficit Financing in Other Localities*

The City of New York is not the only local government in this State which

has engaged in deficit financing during the past ten years. Although local governments have the power to issue budget notes to cure short-term deficits, many of them have had to issue bonds or BANs for a five to ten year period to fund their deficits. For example, the City of Long Beach was authorized to issue ten-year serial bonds in the amount of $1,700,000 for the specific purposes of funding deficits incurred before December 1, 1971. The statute states that the deficits occurred through the failure to receive revenues estimated in its budget, expenditures in excess of budgetary appropriations and the inability to collect the full amount each year of the taxes levied upon real property.[76] On approving the bill, former Governor Rockefeller stated:

> . . . I have repeatedly expressed my strong opposition in principle to bond financing operating deficits . . . The present city government has indicated that steps are being taken to help insure that similar deficits will not be allowed to occur in the future, and under these special circumstances, the bill should be approved. I am deeply distressed, however, that despite my strong statements against this practice in the past, some municipalities continue to incur substantial deficits without regard to their future consequences.[76]

Deficits did occur again, and in 1975 the City of Long Beach was authorized to issue its serial bonds in the amount of $750,000 to fund deficits which resulted prior to December 1, 1974.[77]

It is significant that the municipalities which had to issue deficit bonds or notes pursuant to legislation fashioned on the Long Beach model cannot be distinguished by their size, geographic location or form of government. They include: The City of Troy ($684,000),[78] the City of Albany ($14,156,868.01),[79] Central School District No. 4—Town of Brookhaven ($1,100,000),[80] Village of Herkimer ($359,118.90),[81] City of Utica ($745,000),[82] Wyandanch Union Free School District ($750,000)[83] Salmon River Central School District ($325,000),[84] Deer Park Union Free School District ($2,215,000),[85] Village of Portchester ($550,000),[86] Town of Yorktown ($897,000),[87] Town of Charleston ($77,000),[88] and Village of Monticello ($361,633).[89]

The deficit financing of certain other municipalities is worthy of more detailed examination.

The Village of Keeseville is an example of a small municipality which got itself into difficulty. In 1977 it had outstanding a RAN in the amount of $193,900 in anticipation of the collection of revenues to be received from the State and the federal government in connection with the construction of a sewer system for the Village. Unfortunately, it had spent for other purposes the revenues against which the note had been issued and could no longer reasonably expect the balance of the revenues to be received. It obtained legislation which "in all respects legalized, validated, ratified and confirmed . . . [the note] notwithstanding the fact that such note was issued in violation of certain provisions of the local finance law. . . ." [90] The statute declared that the specific object or purpose of funding all or a portion of the note to be a public purpose for which the Village may issue its bonds or BANs. It assigned a period of probable usefulness of 10 years to $76,200 of the principal

amount of the note and 40 years to the balance, representing respectively the portion of the note for which revenues had been received and misspent and that portion for which revenues would not be received.

In Yonkers there have been four authorizations to fund deficits in recent years: in 1969 ($11,800,000),[91] in 1971 ($3,625,000)[92] in 1975 ($15,000,000),[93] and finally in 1976 ($37,750,000 Current Account Bonds issued to fund "various items of deficits attributable to the fiscal year ending June 30, 1976 and unaccounted for deficits of prior fiscal years, including outstanding short term borrowings issued to fund certain of such deficits. . . ."). [94] The State has created the New York State Emergency Financial Control Board for the City of Yonkers[95] and enacted a Special Finance and Budget Act.[96] Recently the State has authorized the advance of $10,000,000 to Yonkers.[97]

In 1976 the Roosevelt Union Free School District was authorized by the Legislature to issue 10 year bonds to fund a $2,383,000 deficit.[98] Because of "the serious emergency created by such deficits" the Commissioner of Education has been authorized and directed by the authorizing act to appoint a special administrator for the school district. This administrator acts, in effect, as an emergency financial control board. The Board of Education of the school district cannot approve current or future estimates of school district revenues without the concurrence of the special administrator nor can it authorize items of expenditure or the contents of budget appropriations without his concurrence based upon his findings that the budget or items of expenditure are consistent with the requirements of a balanced budget. Thus the device of a fiscal monitor has been used by the Legislature in a place other than New York City and Yonkers in connection with authorization to fund deficits over a long period.

Recently a bill was passed by the Legislature which authorizes a $3,000,000 advance of public school aid to the city school district of Buffalo because the school district "anticipates a cash deficit prior to the close of the current school year which will prevent the district from meeting its payroll obligations." [99] A similar bill was passed which authorized as an advance the sum of $52,000,000 for eligible city school districts and eligible cities having populations in excess of 125,000.[100] These "advances" are loans by the State and are also a form of deficit financing.

The point need not be belabored. These examples support a conclusion that reform is needed in the basic local finance laws of this State which apply to all local governments.

CHAPTER TWO

PROPOSED LOCAL FINANCE ARTICLE

A. *Introduction*

A constitutional system of checks and balances is particularly important where normal legislative processes are not likely to prevent abuse. This is the case in matters of local finance since improvident borrowing may post-

pone the need for elected officials to take unpopular steps such as increasing taxes or curtailing public programs.

The existing Article VIII of the New York State Constitution sets specific and detailed rules and limits for local finances. It contemplates that the courts will enforce these rules and from time to time the courts have done so.

Chapter One shows, however, that filling the Constitution with percentages and limits and exclusions and exceptions has not worked to prevent massive deficit financing, uncontrolled incurrence of long-term obligations and even, for a period, default on over a billion dollars in municipal obligations.

Our proposal for a new Article VIII (the text of which is set forth in Appendix A) is intended to address this problem in several ways.

First, the proposal sets forth a number of fundamental principles in place of the existing detailed but far from comprehensive specifications. These include, 1) the requirement of a pledge of faith and credit, 2) the requirement of a balanced budget, 3) the requirement that tax and revenue anticipation notes be issued in anticipation of taxes and revenues and not deficits, 4) the requirement of a legislatively fixed period of probable usefulness, 5) the requirement that local borrowing not exceed limits fixed by the Legislature and subject to further restriction either by the Comptroller or by a Local Finance Board established by the Legislature and 6) a constitutional limit on real property taxes. By requiring courts to apply basic principles rather than detailed language which may not cover all contingencies, there will be a better prospect for effective enforcement.

Second, the proposal eliminates the need to resort to extra-constitutional financing mechanisms such as lease-purchase arrangements, guarantees, debt service reserve fund make-up provisions and the like. It does this by permitting the Legislature to authorize loans of credit for a public purpose. Rigid restrictions on cooperation between public and private sectors are undesirable since they may impede necessary programs such as programs to promote job opportunities.

Third, the proposal is intended to make debt limits more effective. Tighter regulation of local debt issuing authority will be achieved by requiring the Legislature to fix a general debt limit as a percentage of a local government's revenues. Only self supporting debt and debt approved by referendum would be excluded. Any increase in this general debt limit must be approved by two sessions of the Legislator. There is provision for additional restrictions on all long- and short-term debt based on a technical evaluation of a local government's financial condition by the Comptroller or a Local Finance Board. We believe that this approach will lead to more conservative borrowing restraints than the existing system of voter approved exclusions and limits based on real property values alone.

Fourth, the proposal seeks to increase the incentive to contain the cost of government. Governments will have to live within their means, within a constitutionally mandated balanced budget. Because the choice between decreased expenditures or increased taxes will be unavoidable, elected officials will be called on to make greater efforts to keep expenses as low as possible.

B. *Detailed Discussion*

1. *Section 1*

Section 1 contains two limitations on the power of local governments to make gifts and loans of their money, property or credit: all gifts and loans must be authorized by State law, and they must be for a public purpose which includes the provision of assistance necessary for the betterment of a locality or its economy.

Paragraph (b) of Section 1 authorizes joint or cooperative undertakings by two or more local governments.

Section 1 represents a basic change from New York's traditional prohibition against gifts and loans now contained in Section 1 of Article VIII. The proposal substitutes a broad "public purpose" standard for the more detailed prohibitions, with equally detailed exceptions, which now govern local finances in New York. If authorized by the Legislature, a local government would be constitutionally free to carry out a greater range of activities —including loans and guarantees of loans to public and private corporations —than is now permissible.

The proposal contains other provisions, however, which would further restrict local government indebtedness: all local debt would be full faith and credit debt (§2); all local debt would be within limitations on the amount of indebtedness (§5); no local debt could be issued for a term longer than the expected useful life of the project or program being financed (§3).

Taken together, the provisions of this proposal would give local governments the ability to finance public purpose activities, within program and quantitative limitations established by law, from which they are now constitutionally barred.

To depart from the traditional "gift and loan" restrictions on local government finances requires justification; a hundred-year-old precedent is not lightly to be discarded.

The reason the Committee has decided to recommend this new approach is that the present constitutional provision is unsatisfactory. Created to protect the public purse from buccaneering railroads, it does not provide an adequate legal basis for many current local programs, which are perceived as necessary and have in fact been operative for decades. The constitutional history of New York is replete with artifices of questionable legality designed to overcome the restraints of Article VIII, §1. The courts have been given the awkward task of reconciling urgent public needs with a rigid constitutional prohibition. The result has been a series of decisions upholding governmental action on a weak and equivocal basis. (*See, e.g., Comereski v. City of Elmira*, 308 N.Y. 218 (1955); *Wein v. City of New York*, 36 N.Y.2d 610 (1975)).

This result is unsatisfactory because it creates disrespect for the law, encourages elaborate (and expensive) devices to circumvent the Constitution, and promotes litigation with attendant expense and uncertainty.

One response is that elected officials should stop doing what is not clearly authorized by the Constitution. That is as obvious as it is desirable. But the

history of the State and its municipalities (and of many other states and municipalities) indicates the tendency of rigid restriction to lead to "gimmicks" and abuse. Moreover, neither the Legislature, local officials nor the public have a very clear idea of what is constitutionally permissible in New York. As lawyers, the Committee's task is to help structure a Constitution which will reflect societal needs and permit rational decision-making.

The proposal would do this. It would permit localities to act directly, with attention focused on real fiscal consequences and based on a clear determination that local assistance to public or private entities serves a public purpose. It would permit matters of policy to be clearly resolved and honestly implemented.

Contrast the current means of resolving important fiscal questions. Either an elaborate device is created to overcome a constitutional problem (*see, e.g., Wein v. City of New York, supra*) or a small, incremental exception is made to the constitutional prohibition itself. The original gift and loan provision contained only one exception permitting aid to the poor. (See Constitution of 1846, Art. VIII, §11, as added in 1874.) The current version contains a long list of exceptions, which is still being added to on a piecemeal basis. The latest exception, approved in 1965, permits the City of New York to increase pension benefits to survivors of members of its department of street cleaning. No useful purpose is served by enshrining such a provision in the State Constitution, nor by requiring it to be submitted to the people of, say, Buffalo for approval. If it is an important governmental purpose, it should be capable of achievement through legislative authorization.

Moreover, New York's nineteenth century prohibitions are ill-suited to the demands of contemporary society and the closer relationship between the public and private sectors. In particular, we believe that localities should be more free to act in order to generate private investment and economic and job development activities. New York State and its municipalities have been disadvantaged in the competition among the states to attract new industrial and commercial activity. One of the difficulties with the existing gift and loan restriction is that it does not permit public and private enterprise to combine in order to capitalize on the strengths of each. Too often, the only alternative to abandonment of a privately provided service is complete government ownership and operation. Since there is a possibility of new Federal incentives for urban investment, it is extremely important that local government be able to respond to these programs in an effective and flexible manner.

The problem of reconciling constitutional tradition with the contemporary needs of local government is not unique to New York. Other states similarly situated have wrestled with the same questions. Illinois, which had a provision much like New York's present gift and loan restriction (Ill. Const. of 1870, Art. IV, §20), recently scrapped the traditional formulation and substituted this simple principle: "Public funds, property or credit shall be used only for public purposes." (Ill. Const. of 1970, Art. VIII, §1). Pennsylvania, which for over a century has had restrictions substantially similar to our Article VIII, §1, in 1968 added the following language: "The General

Assembly may provide standards by which municipalities or school districts may give financial assistance . . . to public service, industrial or commercial enterprises if it shall find that such assistance . . . is necessary to the health, safety or welfare of the Commonwealth or any municipality or school district." (Pa. Const., Article 9, §9). Michigan's Constitution of 1963 provides simply: "Except as otherwise provided in this constitution, no city or village shall have the power to loan its credit for any private purpose or, except as provided by law, for any public purpose." (Art. 7, §26).

The proposed draft for New York seeks to achieve substantially the same result as Illinois, Pennsylvania and Michigan—all states with similar histories and similar problems—have sought and achieved through recent constitutional reform.

When the matter was last fully considered in New York—at the Constitutional Convention of 1967—the Convention concluded that the financing powers of local governments should be greatly broadened. The Constitution it proposed would have enabled local governments to make gifts and loans (including gifts and loans to private corporations), "for economic and community development purposes" (Article X, §12.b.); to make such gifts and loans "for public purposes" (Art. X, §18.a); and to guarantee the obligations of any public corporation "for economic and community development purposes" (Art. X, §18.b.). The 1967 proposed Constitution defined "economic and community development purposes" very broadly, to ". . . include the renewal and rebuilding of communities, the development of new communities, and programs and facilities to enhance the physical environmental, health and social well-being of, and to encourage the expansion of economic opportunity for, the people of the state." (Art. X, §12.a). Of course, the entire 1967 proposed Constitution was defeated.

Again in 1971 an effort was made to broaden the constitutional basis for local government action in the area of community development. This amendment was defeated after double passage by the Legislature. Since then, the need for change—and the gap between express constitutional authority and actual governmental activity—has widened.

The present provisions of Article VIII, section 1, do not give clear authorization for what elected officials have for decades perceived as necessary government initiatives in community and economic development and other areas. Rather, they lead to contrived and ingenious solutions to pressing public concerns, which are then upheld by divided and troubled courts. Other states have made constitutional changes which permit more straightforward direction for these activities. New York should do the same.

The Committee also believes that it is desirable to permit units of local government to act together and with the private sector for mutually agreed upon projects or functions. Steps in this direction were taken when the very restrictive provisions of the 1938 Constitution were eased by a series of amendments adopted in the 1950s. In the future such inter-governmental ventures should not need specific constitutional authorization, but should be authorized by the Legislature, subject only to the basic limitations on debt and taxes. Thus, the Committee recommends the general language of

paragraph (b) of section 1 of the draft, in place of the detailed provisions of existing sections 1 and 2a, which would be eliminated. Also modified would be the provisions of existing Article VIII, §3 and §9, and Article X, §5, dealing with the liability of political subdivisions for the payment of the obligations of certain public corporations.

2. *Section 2*

The first sentence of proposed Section 2 repeats without substantive change the first sentence of the second paragraph of existing section 2 and continues the existing constitutional requirement that no local government contract indebtedness unless it shall have pledged its faith and credit for the payment of principal and interest of such indebtedness. While the Committee has considered changing these provisions to permit the issuance of bonds backed solely by particular revenues, it has not done so. The Committee believes that even self-liquidating debt should in addition be secured by the general revenue powers of a local government through a pledge of its faith and credit.

The pledge of faith and credit is particularly important since it has been given added force by the Court of Appeals in its recent decision in *Flushing National Bank* v. *Municipal Assistance Corporation*, 40 N.Y.2d 731 (1976). The Court placed central reliance on the faith and credit requirement in declaring unconstitutional the moratorium on suits to enforce short-term obligations of the City of New York. It stated at pp. 734–736:

> "The State Constitution regulates closely the debt-incurring power of local governments. Key to this case is that a city may not contract indebtedness unless it has 'pledged its faith and credit for the payment of the principal thereof and the interest thereon' (NY Const., Art. VIII, §2).
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> * * *
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> "A pledge of the city's faith and credit is both a commitment to pay and a commitment of the city's revenue generating powers to produce the funds to pay. Hence, an obligation containing a pledge of the city's 'faith and credit' is secured by a promise both to pay and to use in good faith the city's general revenue powers to produce sufficient funds to pay the principal and interest of the obligation as it becomes due.
>
> * * *
>
> "The constitutional requirement of a pledge of the city's faith and credit is not satisfied merely by engraving a statement of the pledge in the text of the obligation. The last is a strange argument made by respondents. It is difficult to understand the financial value of such a commitment as contrasted with a 'moral' obligation, wisely prohibited by the Constitution for municipalities (NY Const., Art. VIII, §2). Instead, by any test, whether based on realism or sensibility, the city is constitutionally obliged to pay and to use in good faith its revenue powers to produce funds to pay the principal of the notes when due. . . ."

In order for local governments to have the power to raise needed funds in

time of difficulty as well as in times of prosperity, there should be no doubt that debt will be paid when due. This principle is consistent with the existing Article VIII and the *Flushing Bank* cause quoted above. See also *Weir* v. *Carey*, 41 N.Y. 2d 498 (1977).

The so-called "first revenues" provision of existing section 2, paragraph 2, like the "faith and credit" provision, is designed to afford the investor in municipal obligations with such assurance. However, it is not sufficiently restrictive and some of its language is ambiguous.

Under the existing provision every local government is required to provide annually by appropriation for the payment of interest on all indebtedness and for the payment of principal on bonds and certain, but not all, notes. The proposed section would require that provision be made for the payment of interest on all indebtedness and for the amounts required for payment of all principal maturing or otherwise coming due during the fiscal year, including the principal due on notes not covered by the existing provision. It would also provide, however, that provision for payment may be made by means other than by appropriation. For example, provision for the payment of bond anticipation notes could be made through the sale of bonds and provision for the payment of tax and revenue anticipation notes could be made by the anticipated receipt of the taxes and revenue in anticipation of which the notes have been issued.

The proposed section 2 clarifies current law by providing that upon failure to make provision for payment of indebtedness or upon the failure to make such payment, a sufficient sum shall be set aside from first revenues thereafter received and shall be applied to such purposes. The existing provision might be read to require the setting aside of first revenues only if there is a failure to appropriate.

The use of the words "may be required" in the last sentence of the section, relating to the setting aside of revenues at the suit of a holder of obligations, has been continued. Because the judicial relief contemplated by this sentence is equitable in nature, it would be inappropriate to deprive the Court of all discretion by substituting the words "shall be required."

3. *Section 3*

Paragraph (a) of section 3 continues the existing requirement that the issuance of debt be authorized by state law for a public purpose. The existing Article VIII specifies limitations on local indebtedness; the proposed section would require the Legislature to fix such limitations by general law as a percentage of a local government's revenues, subject to the power of the Comptroller or a Local Finance Board established by the Legislature to impose additional restrictions. Any law providing for an increase in such limitations would have to be passed by two consecutive sessions of the Legislature. Because the limitations fixed under the proposed Article VIII would apply to debt issued for all purposes, the special two percent limitation for housing purposes under Article XVIII would be repealed.

Paragraph (b) continues existing law requiring the Legislature to fix a period of probable usefulness. This provision, in addition to fixing the maxi-

mum maturity of bonds, has also been construed to limit the power of the Legislature to authorize the issuance of bonds to finance recurring operating expenses. See *Hurd* v. *City of Buffalo*, 34 N.ad 628 (1974). The section does not specify the maximum period of probable usefulness or the schedule of debt service payments (*e.g.*, equal installments, level debt service, the existing 50% rule, sinking fund amortization). Existing provisions on these subjects are detailed, and the Committee believes that the potential for abuse on these matters is not sufficient to justify constitutional restriction.

Paragraph (c) adds restrictions on the issuance of short-term debt not found in the present Article VIII but which are applicable to the State under Article VII. The comparable Article VII provisions have been construed by the Court of Appeals in *Wein* v. *Carey*, 41 N.Y.ad 498 (1977) and *Wein* v. *State*, 39 N.Y.ad 136 (1976) to preclude the issuance of short-term debt in anticipation of a deficit.

Paragraph (d) imposes new restrictions on the issuance of bond anticipation notes. Under the existing Constitution, the Legislature may permit bond anticipation notes to be rolled over for the full period of probable usefulness. Under Article VII, the State is subject to a five year limit on the rollover of bond anticipation notes. The proposal would impose the five year limit on localities but permit an additional one year extension if an appropriation was made to retire the notes.

The principal change effected by Section 3 is to remove the lengthy and detailed restrictions on local debt from the Constitution itself and, instead, to require that the Legislature impose such restrictions subject to further restriction by the Comptroller, or if the Legislature so provides, a Local Finance Board. This change is recommended for several reasons.

The existing debt limits relate to the value of taxable real property within each locality. It is likely that real property taxes will constitute an ever-declining proportion of local government revenues, and accordingly be less useful as a measure of the debt repayment capacities of local governments. In requiring that debt limits be based on revenues, the proposal looks toward a community's overall ability to repay debt.

Current constitutional debt limits restrict only actual, direct indebtedness of localities. They do not restrict such obligations as long-term leases and moral obligation debts. However, these obligations create actual or contingent liabilities which may impair a localities ability to repay its debts just as surely as any direct obligation. In fixing debt limits under the proposal, account will be taken of all such obligations and their impact on debt repayment capacity.

Because the proposal looks to total repayment capacity as well as total repayment obligations, it should lead to more effective and more sensitive restrictions on local indebtedness.

Another reason for removing debt limits from the Constitution is to end the piecemeal, exception-ridden pattern of restriction which has evolved in New York. Instead of a rational plan for local debt management, we have a series of exceptions and special cases to handle special problems on an ad hoc basis. Moreover, each of these has to be approved by voters throughout

the State, although they may concern only a particular locality or group of localities. The current system lacks both a rational fiscal strategy and a necessary degree of flexibility.

The Committee's proposal is similar to the Constitutional provisions adopted in Pennsylvania in 1968 for local governments other than the City of Philadelphia. (Penn. Const., Art. 9, §10). Under its constitutional provisions the Pennsylvania General Assembly has fixed debt limits of 100% of the borrowing base (average of total revenues for the three full fiscal years preceding incurrence of debt) in the case of a school district of the first class, 300% of the borrowing base in the case of a county and 250% in the case of any other local government. ("Local Government Unit Debt Act" contituting 53 P.S. §§6780 *et seq*, as amended by P.L. 1978, No. 52). Counties are permitted an additional 100% under certain circumstances and all local governments are permitted an additional 50% if required to replace assets as a result of fire, flood, war or other catastrophe upon application to the Commonwealth Court. An additional limit is fixed for lease rental debt based upon a percentage of the borrowing base and debt outstanding. We contemplate that after a careful and professional study of existing debt and revenue patterns in New York State, the Legislature would fix comparable limits appropriate to New York.

Our proposal contains additional restrictions not found in the Pennsylvania Constitution, namely the requirement that increases in debt limits be approved by two consecutive sessions of the Legislature and provision for further restriction by the Comptroller or, if the Legislature provides, by a Local Finance Board. Since the Comptroller or Local Finance Board would have the power to limit the amount of voter approved debt that a local government may issue, there will be further assurance that the ability of a local government to pay debt will be taken into account. At the same time provision for voter approved debt permits the Legislature to establish more conservative general debt limits.

Section 3 also tightens constitutional restrictions on the issuance of short-term debt. Recent experience has shown the damage that the imprudent issuance of short-term debt can do to the financial health of a community—even one with very substantial resources. Short-term borrowing is necessary and proper as a cash management device. It is abused when it is used to finance deficits accumulating year to year.

The Committee recognizes that unanticipated deficits cannot always be avoided since the budgetary process is dependent on estimates. When a deficit occurs, short-term borrowing may be necessary. Such borrowing should be repaid in the following fiscal year within the framework of a balanced budget for the fiscal year of repayment. The proposal would require this result. It is based on the constitutional language which now controls short-term borrowing by the State and under which the State has successfully raised substantial amounts for its short-term needs. As the Court of Appeals has stated in construing these provisions:

> "Thus, the device of issuing tax and revenue anticipation notes was designed to permit the State to borrow temporarily to meet expenses for which

appropriations under a balanced budget have been made, but for which revenues, both committed and anticipated, have not yet come in, thus adjusting the cash flow of taxes and revenues to expenditures. Put another way, these short-term obligations may be used to raise funds to offset deficits in the fiscal year of issuance and payable not later than in some early portion of the next fiscal year." *Wein v. State*, 39 N.Y.2d 136, 148 (1976).

4. *Section 4*

This section continues existing limits on real property taxes imposed by localities for purposes other than the payment of debt service. It repeats nearly verbatim the wording of the existing constitution. Paragraph (e) permits pay-as-you-go financing outside the tax limit for objects or purposes for which a local government could borrow. Existing law limits New York City to pay-as-you-go financing of capital improvements and requires the City to charge its debt limit for capital improvements financed on a pay-as-you-go basis even though no bonds are issued (so-called phantom debt). These requirements do not apply to other local governments. The proposed Article eliminates this special treatment for New York City in order to encourage the financing from current revenues of objects or purposes for which the City is authorized to borrow.

5. *Section 5*

This section is new. The existing Article VIII does not require local governments to adopt or maintain balanced budgets. Under the proposed Article the Legislature would itself or through its designee fix the criteria for determining whether a budget is balanced, including such matters as the treatment of deferred payments, reserves for contingencies and the use of bond proceeds to support expenditures.

The obligation to "maintain" a balanced budget would not of course preclude the possibility of a deficit. Indeed appropriation for an unanticipated but necessary expenditure toward the end of a fiscal year may well put a budget out of balance. The Legislature would have authority to determine what constitutes maintenance of a balanced budget—a power which under our statutory proposals would be delegated to the Comptroller. The Constitution, however, would make clear that local officials are under a duty to control expenditures and that any short-term deficit financing must be repaid in the following year under a balanced budget. Under this proposal, as under existing law, bonds could be issued to finance deficits or expenditures which would otherwise give rise to deficits to the extent that the Legislature could properly establish a period of probable usefulness for such purpose.

The chief drawback to a balanced budget requirement is that localities may be required to curtail public programs during periods of economic recession. To a degree, the recent expansion of federal programs has lessened this difficulty and localities may in any event establish "rainy day" funds to meet expenditures when revenue growth declines. More fundamentally, however, the Committee believes that to permit deficit financing would remove needed incentive to contain the cost of local government.

The proposal does not mandate the use of generally accepted accounting principles in connection with local accounting and budgeting. These principles may be a useful guide to the Legislature or to such officer as may be authorized by the Legislature to establish regulations on local budgeting and accounting.

6. *Other Sections*

Section 5 contains transition provisions intended to protect the rights of holders of existing debt. Section 6 makes it the duty of the Legislature to restrict the power of taxation, assessment, borrowing money, contracting indebtedness, and loaning the credit of local governments so as to assure sound fiscal practices and prevent abuses. It continues existing law with added emphasis on the duty to assure sound fiscal practices. Sections 7 and 8 should be read together. The definition of "local government" in section 8 includes existing local units and any public corporation with the power both to levy taxes and to incur indebtedness. The existing Article VIII prohibits the creation of new public entities with these powers. Over time the Legislature may want to provide for local government on a more regional basis. Section 7 of the proposed Article VIII would not permit the Legislature to create new units of local government unless those exercising the authority to impose taxes and contract indebtedness are elected. The finances of such entities would be subject to the same restrictions as apply to existing units.

CHAPTER THREE

PROPOSED DISCLOSURE LEGISLATION

A. *Introduction*

Between 1962 and 1975, the amount of local debt outstanding nationwide (excluding state debt) increased by more than 250%, climbing to almost $150 billion.[101] In 1976 alone, state and local governments issued over $55 billion worth of obligations, well over twice the amount issued in 1967.[102] These increases reveal a continuing dependence by local governments on the public market for credit through the issuance of both long and short-term obligations.

New York surpasses all other states in terms of the dollar amount of debt obligations outstanding. New York local governments (excluding the state government) had over $25 billion of debt outstanding at the end of fiscal 1975.[103] This total figure, well above the level of any other state, represented almost 17% of the debt outstanding of local governments nationwide. In the short-term debt market, New York local government obligations represent over 45% of the national figure.[104] During the 12-month period ending in November of 1977, local government entities and state agencies came to the market almost 500 times, issuing debt in an aggregate amount over $10 billion.[105]

These statistics highlight the obvious fact that New York local governments have a strong interest in protecting their access to the market and

creating confidence on the part of investors who provide this vital credit source. New York State already has legislation on the books regulating in certain respects the issuance of debt. For example, a Notice of Sale is required in connection with the public sale of debt obligations, specifying data relevant to the obligation being sold.[106] The filing of a Debt Statement (a statement as to debt-contracting power) is required prior to the public sale of bonds by certain local government entities.[107] A system of annual reports is also prescribed by New York statutes, providing a detailed analysis of operations in a format fixed by the Comptroller.[108] The Comptroller's Office, through its Bureau of Examinations, performs periodic audits of local government accounts based on the uniform system of accounts set by the Comptroller.[109]

While these State mechanisms are designed to perform a disclosure function, the form and content of the filings are such that, in many instances, they do not adequately inform the taxpayers of these localities as to the fiscal condition of the communities, and they are seldom relied upon by investors contemplating a purchase or sale decision. The pressures of the marketplace have forced many local government entities to issue official statements even though no requirement to do so exists by law.

The existing framework of federal securities regulation does not add to the particular disclosure requirements of the State, but stands as a potent sanction against fraud in the marketplace. While the Securities Act of 1933 and the Securities Exchange Act of 1934 provide a broad set of disclosure requirements in connection with the public distribution of securities and subsequent security transactions, specific exemptions for municipal securities transactions have left local governments free from registration requirements. However, the broad prohibitions against fraud, material omissions, and material misstatements in the offering or sale of securities have been broadly construed by the courts both in general and in the municipal securities area specifically. These provisions apply to voluntary disclosure presently made by local governments in connection with the sale of obligations and would be equally applicable to any proposals to augment New York's statutory disclosure requirements.

B. *Need for More Complete Information*

In connection with the study of disclosure practices of issuers in New York State, interviews were conducted with various representatives of the investor community. These discussions have revealed a general dissatisfaction with the availability of usable information with respect to the finances of local governments in New York. The principal concerns are (i) the form of disclosure, and (ii) the general absence of reliable post-issuance reporting.

It was the general observation of those interviewed that present disclosure practices by New York issuers do not permit easy comparison of issuances or provide investors with information in a manageable form sufficient to base a decision to purchase a new offering or to hold or sell an obligation presently in their portfolio. As a result, although New York State government entities annually undertake to compile extensive schedules relating to their

financial operations, that information has not been presented in a form useful to investors. Similarly, the segments of the public which need access to financial information concerning the reporting entities cannot readily process the volume and detail of information filed with the Comptroller's Office under the existing system of reporting.

The volume of disclosure by local government issuers has increased substantially in the aftermath of New York City's fiscal crisis in late 1975. Despite this dramatic improvement in response to the demands of the marketplace for more information, it is the general consensus of the Committee that many deficiencies remain in the scope, quality and presentation of information by local governments in New York State.[110] These deficiencies have severely limited the usefulness of the disclosure documents to investors.

C. *Drawbacks of Federal Regulation*

The major proposal for federal regulation of state and local government disclosure is the Williams Bill, introduced in 1976[111] and again in 1977[112] in a revised form. Under the proposal, disclosure would be effected primarily through the preparation and public availability of two types of documents based in large part on the voluntary disclosure guidelines suggested in 1976 by the Municipal Finance Officers Association. By the amendment of section 13A(b)(1) of the Securities Exchange Act of 1934, any issuer of municipal securities that has outstanding, during any portion of a fiscal year, an aggregate principal amount of municipal securities exceeding $50 million would be required to prepare an annual report and reports of events of default.

Notwithstanding the size of the issue, any issuer of municipal securities would be additionally required, under another proposed amendment to the Securities Exchange Act, to prepare a municipal securities distribution document including the types of information outlined in the annual report requirements. While the bill does not require pre-issuance registration or filing of disclosure documents with the SEC, that federal agency would have considerable discretion over the scope and form of disclosure for both the annual report and distribution documents. The absence of the pre-issuance registration or filing requirements would not, we believe, eliminate the involvement of the SEC with the content and form of distribution documents.

As a means of minimizing federal regulation of local government issuers, the bill exempts from the annual report and disclosure document requirements any issuer of municipal securities that is required by the law of the state in which the issuer is organized to make disclosures that are "substantially similar" to those required by the bill. The SEC, as the ultimate arbiter of the content and form of disclosure documents required by the bill, would indirectly establish the criteria upon which state-mandated disclosure documents would be judged to determine if they were "substantially similar" to federal requirements.

The Committee believes that the approach outlined herein is clearly preferable to the adoption of mandatory disclosure legislation at the federal level for the following reasons:

(a) Not only are local government entities themselves the creatures of the states, but also the entire authority for municipal debt issuances derives from state statutes. Such fundamental elements of the debt issuance framework as debt limitations, tax resources available to service the debt and the procedures for debt issuance are all state created.

(b) The administration of a disclosure system can best be done at the state level, since state officials in most states, as in New York, already have considerable responsibilities and experience in relation to local financing and reporting.

(c) State disclosure proposals can be integrated into existing state reporting mechanisms, thereby providing investors and the general public with needed information while imposing a lesser administrative and cost burden on issuing entities.

(d) Disclosure documents prescribed by state officials can be designed to take account of the practical realities and state statutory requirements faced by local governments within one state, but not necessarily applicable to other states.

(e) Numerous distinctions exist between the *corporate* securities market and the *municipal* securities market. The procedures for corporate securities transactions are too detailed and expensive to apply to the typically smaller and more numerous municipal securities transactions. Many of these differences can best be recognized through legislation and regulations adopted at the state level, where there is greater knowledge of the local issuers. Given the potential for an expanded role by the corporation-oriented SEC under the Williams Bill, the differences between the municipal and corporate securities markets might be ignored under that proposal.

(f) There are constitutional uncertainties involved in federal legislation requiring the pre-filing of municipal disclosure documents.

D. *Proposals*

The recommended revisions to New York's Local Finance Law and General Municipal Law (the proposed text is set forth in Appendix B) attempt to construct a comprehensive system of financial disclosure by local governmental entities within the basic framework of existing State reporting mechanisms. The proposal relies on three elements to achieve this goal: (i) a disclosure document (the "official statement"), to provide investor information in connection with the issuance of obligations by a local entity, (ii) summarized periodic reporting (the "summary annual report"), and (iii) timely independent examination of financial practices and accounts. While present State requirements and the voluntary practices of localities already perform, to differing degrees, many of these functions, the accompanying proposals are designed to standardize practices of New York localities in a manner least likely to disrupt or burden local governmental operations.

1. *Official Statement*

Having opted for a system of State regulation of disclosure, the Committee viewed the 1976 bill, sponsored by Governor Carey (S. 4871, A. 7126) as a sound approach and used it as a point of departure for its proposals. That 1976 Program Bill proposed adding to Sections 57.00 and 60.00 of New York Local Finance Law (relating to the sale of bonds and notes, respectively) new paragraphs with four basic elements:

1. Requiring that a "disclosure document" be filed with the State Comptroller at least 10 days prior to the date fixed for the public sale of bonds or notes.

2. Establishing the Comptroller as the administering officer of disclosure practice and requiring him to specify, by rule or order, the kinds of information to be included in disclosure documents.

3. Requiring disclosure documents be certified as to completeness and accuracy by the "chief fiscal officer or such other person or persons as may be designated by the finance board of such municipality, school district or district corporation."

4. Permitting the Comptroller, by rule or order, to exempt any issue of bonds or notes from filing requirements if he determined that such filing was not necessary or appropriate in the public interest or for the protection of investors by reason of (i) the aggregate principal amount of the bonds or notes involved in the particular issue, or (ii) the limited character of the public offering.

Substantially similar bills were introduced in 1978 with the sponsorship of the State Comptroller (S. 8688, A. 10213).

The amendments to Local Finance Law, §§57.00 and 60.00 which are proposed herein follow the pattern of the Governor's 1976 Program Bill and the recent Comptroller's bill by requiring that an "official statement" be filed prior to the sale of bonds or notes, thereby insuring that material information necessary to make an informed investment decision will be available in a utilizable format. However, the proposal omits the requirement of the earlier bills that the filing be made at least 10 days prior to the public sale date, and the imposition of any such time period would require a rule or order of the Comptroller.

The proposal does not attempt to fix by statute a detailed listing of the information which would be required to be covered in the official statement. Given (i) the varied nature of the issuing entities subject to the Local Finance Law, (ii) the alternate forms of debt regularly issued, and (iii) the constantly evolving needs for specific types of financial information and disclosure, it seemed advisable to establish a flexible format, under the supervision of the State's chief fiscal officer, the Comptroller. Such flexibility has been assured by requiring the Comptroller, by regulation, to specify the categories of information to be elicited from localities issuing obligations.

The proposal directs the Comptroller to consider "voluntary disclosure standards promulgated by national organizations of local governments" in

developing regulations which enunciate the types of information to be included in official statements. At the present time, the set of standards meeting this description is the Municipal Finance Officers Association's *Disclosure Guidelines for Offerings of Securities by State and Local Governments* (December, 1976) (the "MFOA Guidelines"). The proposal permits but does not require adoption of the MFOA Guidelines *in toto* since a statute that required adoption in full might unnecessarily restrict the flexibility of the State Comptroller in designing an appropriate disclosure document tailored to the needs and practices of New York governmental entities. We comment below on the format of the financial statements to be included in the official statement.

In order to facilitate the preparation by issuers of the prescribed official statement, the proposal provides that any summary annual report filed with the Comptroller's Office under newly proposed §31-a of the General Municipal Law may be incorporated by reference in an issuing entity's official statement. To insure that the official statement will present an integrated statement of the issuing entity's fiscal condition, the proposal requires that any portion of a summary annual report incorporated by reference be attached to or included in such official statement. Once a system of annual summarized reporting is in effect, the parallelism of the disclosure required in the annual report and the official statement, together with this provision allowing for incorporation, will reduce the burden of preparing an official statement in connection with a new offering to essentially an updating of summary reports already on file at the Comptroller's Office.

The burden of preparing the official statement required by these proposals should be significantly offset by the proposed requirement that the Comptroller provide forms of prototype official statements keyed to the type and size of the entity. This practice is presently employed with the annual reports required by General Municipal Law, §§30 and 31.

The Committee's proposals differ from Governor Carey's 1976 Program Bill by requiring that the official statement merely be signed on behalf of the issuing entity, rather than "certified . . . as to completeness and accuracy." The reason for the change is the concern that certification might carry with it an implied right of private action based upon the contents of the official statement, without there being assurance of appropriate indemnification for the certifying official. In providing for the informational needs of investors and the general public, the Committee did not want to risk discouraging qualified individuals from seeking public office because of the threat of potentially staggering liability which might arise from the sale of public obligations. The proposed statutory revisions make clear that no new State rights of action are created by the requirement of an official statement, though it is recognized that, based on existing judicial precedents, the anti-fraud provisions of existing federal securities law are applicable to State and local official statements.

The proposed amendments do not contemplate that the Comptroller will review the official statement, and he would be precluded from delaying the

sale of the bonds or notes on the basis of alleged deficiencies in the official statement.

While no specific provision has been made for the indemnification of public officials who sign a disclosure document, a proposal drafted by the New York State Law Revision Commission, which would have a broad impact on all public officers, is under consideration by the State Legislature (A. 8091-S. 6603). Should the Legislature act favorably on the proposal of the Law Revision Commission, indemnification could afford added protection to public officials.

The proposal empowers the Comptroller to waive the normal disclosure procedure in those instances where an official statement is not appropriate or where it would impose a disproportionate burden on the issuing entity (*e.g.*, a limited private sale to institutions or a sale of short-term notes of minor aggregate amount compared to the issuer's resources). Exemption also might be appropriate in many of those instances which qualify as "private" sales of bonds under Local Finance Law, §57.00: *e.g.*, bonds sold to the United States government, the New York Municipal Bond Agency, the New York Environmental Facilities Corporation, pollution control bonds.

The Committee believes that in those instances where the cost of preparing an official statement disproportionately outweighs the informational benefits which might be afforded a limited group of investors in a short-term or limited size offering, the Comptroller should waive the normal disclosure requirements. Although these proposals do enunciate the factors to be considered in granting an exemption, no fixed statutory standard (such as a minimum dollar amount of the issue) is incorporated. Instead, the Comptroller is vested with the power to grant exemptions by rules or orders of general or particular applicability, allowing him to consider factors such as the size of the issuing entity or the financial sophistication of debt purchasers.

2. *Summary Annual Report*

Having provided for the requirement of an official statement in connection with the initial sale of bonds and notes, the proposed amendments to the General Municipal Law seek to complete the disclosure process by requiring a system of ongoing financial disclosure which is subject to regular independent review. Three questions were given primary consideration in evaluating alternative forms of continuous reporting: (i) what information do investors need, (ii) where does the existing system of reporting fail, and (iii) what solution would pose the least hardship to governmental units already burdened with considerable paperwork demands?

The New York General Municipal Law presently requires local governmental entities to file an annual report in a form prescribed by the Comptroller. Although this report includes extensive financial data designed to reflect a governmental entity's financial transactions and status, it fails to meet the informational needs of investors as well as the taxpaying public for several reasons: (i) it is unaudited when filed and is typically not subject to audit by the Comptroller's Office for two to three years, (ii) it consists largely

of detailed financial schedules which do not facilitate quick analysis of the entity's overall financial picture or comparison to the fiscal performance of other entities, (iii) it fails to contain any narrative disclosure of significant developments, material to the financial health and operations of the entity, and (iv) it fails to present figures in a format which permits easy comparison to prior years' performance. Each of these deficiencies is addressed in the Committee's proposals.

In order to meet the needs of investors and the general public for concise periodic reporting by local governments, the proposals supplement the present annual report format with a "summary annual report." This new document would summarize significant aspects of the financial information which is already contained in the more exhaustive annual reports presently filed.

Consistent with the approach taken in establishing the content of official statements, the Committee's proposals for summary annual reports would create a flexible format to be prescribed by the Comptroller, upon having given consideration to "voluntary disclosure standards promulgated by national organizations of local governments." At the present time, the set of standards meeting this description is the Municipal Finance Officers Association's *Guidelines for Use by State and Local Governments in the Preparation of Yearly Information Statements and Other Current Information* (May 1978). Again, the proposal does not mandate the Comptroller to adopt these MFOA Guidelines *in toto* but authorizes the Comptroller to do so.

The financial statements to be included in the summary annual report might, in large part, be drawn from the annual reports presently filed. Disclosure of changes in fund balances, a schedule of indebtedness and an analysis of tax receipts and expenses (with budget figures contrasted to actual amounts received and expended), are presently part of the annual reports filed with the Comptroller's Office. It is understood that the Comptroller's Office is now undertaking the regular computerization of annual reports as filed. By making maximum use of data processing capabilities, it may be possible for the State to undertake the mechanics of summarizing financial accounts for local government entities, thereby reducing their administrative burdens and reducing the likelihood of statistical error.

The present system of annual reporting does not indicate any material changes in the operation or condition of the reporting entity or the economics of the geographical area covered by the reporting entity. The categories of information contained in the summary annual report, on the other hand, would conform (to the extent deemed appropriate by the Comptroller) to the types of information in the official statement. The effect of this approach would be to provide a regular updating of the kinds of information originally furnished in the official statement. As in the case of financial statements, the Comptroller's Office would be able to assist local governments in developing demographic and economic data. Moreover, the administrative burden of preparing the proposed summary annual report would be balanced by the fact that it would have been preceded by an official statement and would constitute, in many respects, merely an updating of that official statement.

The requirement of a summary annual report would be applicable only

to those local government units which (i) have issued bonds or notes after the effective date of the proposals, (ii) have obligations outstanding at the close of their fiscal year, and (iii) have not been exempted from such requirement by the Comptroller. As in the case of the official statement, the Committee proposes that the Comptroller should be empowered to grant exemptions in those cases where the burden of preparing a summary annual report is not justified by significant investor or public need (*e.g.*, where an insignificant aggregate amount of the governmental unit's obligations remain outstanding).

The State presently performs a broad scale audit function as an external monitor of the accounts of local governmental units and public authorities. The Comptroller's Office, employing a uniform system of accounts prescribed pursuant to General Municipal Law, §36, is empowered to conduct periodic examinations of the accounts of local entities. As the general hiring freeze has shrunk the ranks of the Comptroller's audit staff, the frequency of these State conducted examinations has dropped to once every two to three years. Given this length of time between examinations, investment analysts have been deprived of current audit information and have discounted the value of State audit reports as too outdated to aid investment decisions. Similarly, under present practices taxpayers and members of the public at large typically learn of fiscal or administrative deficiencies in their respective jurisdictions only after such practices have been allowed to continue unnoticed for several years. The frequency of the Comptroller's audits, rather than their adequacy or scope, has been the most commonly cited failing of the present system of local financial audit.

In addressing the need for current audited financial statements, the proposals offer local government units alternative means of securing independent examination of accounts presented in summary annual reports. In those instances in which a government unit elects to file a summary annual report which includes unaudited financial statements, the present statutory requirement that the annual report be filed within sixty days after the close of the fiscal year (four months after in the case of New York City) would apply also to the summary annual report, and the Comptroller would be required to perform an examination of such summary annual report within six months of its being filed. As an alternative, a local government subject to the requirement of a summary annual report would be permitted up to one hundred fifty days after the close of its fiscal year to file the report if the financial statements presented therein had already been examined by and were accompanied by an opinion thereon of independent certified public accountants. This latter method would avoid the public filing of financial data which might later be subject to revision upon audit examination. While not provided for expressly in the proposed statute, the State might conclude that it is desirable to reimburse local government units for at least part of the expense incurred by hiring independent certified public accountants, thereby encouraging the use of that alternate form of audit.

In considering the audit principles and standards which should govern the preparation and presentation of financial statements contained in both official statements and summary annual reports, the Committee has been advised

that, at present, compliance by local government units with the State Uniform System of Accounts will also provide financial statements which follow national generally accepted accounting principals (as reflected in GAAFR's Blue Book and the AICPA Audit Guide). The Committee has been further advised that national governmental accounting principles are now in a state of evolution. Since there could from time to time be differences between the State Uniform System of Accounts and generally accepted accounting principles as they are applied to local government units, the Committee's bill proposes to accept financial statements presented in accordance with either set of accounting principles. However, if the financial statements in either an official statement or a summary annual report are prepared in accordance with the State Uniform System of Accounts, there must also be an explanation (which may be in terms prescribed in rules of the Comptroller) as to any material differences between such system of keeping accounts and generally accepted accounting principles as are in effect at the date of the official statement or the summary annual report, as the case may be.

In those instances where local governments obtain independent examination of financial statements presented in summary annual reports, the nature of the audit to be performed would be defined by the requirement that it be in accordance with generally accepted auditing standards.

Provision has also been made to assure public availability of both official statements and summary annual reports, although the proposed statute would not prescribe any requirements as to distribution to purchasers of the securities. The statute proceeds on the theory that distribution patterns will be established by the underwriters and dealers, and that the statute's function is to assure the existence of the official statement. The proposed amendment of §30 of the General Municipal Law would require local governments to provide upon request the most recent summary annual report filed with the Comptroller, together with any report of examination of financial accounts presented in that report which may have been performed. The availability of summary annual reports would be made known to the holders of obligations by a statement on the face of bonds and notes pursuant to the proposed revision to N.Y. Local Finance Law, §51.

CHAPTER FOUR

PROPOSED FISCAL MONITOR LEGISLATION

A. *Introduction*

Integral to the reforms proposed by the Committee is the question of how to insure that they will be effectively monitored. The Committee has focused on how existing statutory requirements for the supervision of the fiscal affairs of the state's local governments might be developed to complement the Project's other proposals.

The Committee's point of departure is the proposed constitutional requirement that each local government adopt a balanced budget. The legislation proposed by the Committee mandates that such budgets be balanced in accordance with standards promulgated by the Comptroller and that local governments conduct their financial affairs to realize that objective.

To insure compliance with this requirement, particularly by local governments that issue debt, the legislation empowers the Comptroller to review budgets, to monitor budgets of local governments which evidence some form of fiscal difficulty (*e.g.*, substantial or successive budget deficits), to issue reports on compliance with the balanced budget requirement, and to bring legal actions against local governments to enforce this requirement and certain others dealing with fiscal discipline.

The Committee gave consideration to the establishment of a permanent fiscal monitor to supervise the fiscal affairs of local government experiencing fiscal trouble. It was argued that the existing Emergency Financial Control Boards for New York City and Yonkers were developed in response to specific difficulties existing at particular times. Since it was acknowledged that each Control Board reflects a variety of political compromises effected in response to specific problems and circumstances, it was felt that the experience with these Control Boards should not form the basis for legislation of general application. Instead, the discretion and responsibility for fashioning an appropriate response to possible future fiscal difficulties of other local governments should be left to future legislatures. The proposed legislation (the text of which is set forth in Appendix C) follows this approach.

B. *Detailed Discussion*

1. *Balanced Budget Requirement*

The proposed legislation codifies the proposed constitutional requirement that local governments adopt budgets which are balanced in that, under accounting principles specified by the State Comptroller, total expenditures are equal to or less than total revenues for each fiscal year. It further requires local governments to conduct their financial affairs so that their results of operations are consistent with this objective.

Under the proposed statute, the balanced budget requirement would not be applicable where an entity had advised the Comptroller, prior to the end of its fiscal year, that as a result of unforeseen circumstances it was likely to incur a deficit for that fiscal year and that compliance with the balanced budget requirement would have a material adverse effect on the delivery of essential governmental services.

2. *Deputy Comptroller, Division of Municipal Affairs*

Since both the Committee's disclosure and fiscal monitor proposals substantially increase the responsibilities of the Comptroller with respect to local governments that issue debt, the Committee proposes that the Deputy Comptroller, Division of Municipal Affairs, be elevated to statutory prominence

comparable to that of the Special Deputy Comptroller for New York City. Such statutory recognition would emphasize the importance of this function and facilitate the appropriation of necessary funds for the proper execution of these responsibilities.

3. Submission of Budgets

Expanding on the requirement under Section 54-a of the State Finance Law that counties, cities and villages file certified copies of their budgets with the Comptroller, the proposed legislation would require all municipal and district corporations to file their budgets and material budget modifications with the Comptroller. Budgets would be due within thirty days of adoption; material changes would be due within ten days. Such submissions would be accompanied by such other information as the Comptroller may determine is necessary or appropriate to enable that officer to determine whether the budget or the budget modification is in accordance with law.

In order to avoid placing unnecessary burdens on either the Comptroller or municipal or district corporations that do not issue debt, the legislation permits the Comptroller to exempt such entities from this filing requirement under certain specified circumstances. The legislation contemplates that the exemption would only extend to entities that had not issued debt during any of the three fiscal years preceding the budget year and did not propose to issue debt during the fiscal year covered by the budget. In addition, in order to qualify for the exemption the entity could not have incurred deficits during the three fiscal years preceding the budget year which amounted, in the aggregate, to more than three percent of the revenues projected for the budget year.

4. Review of Local Government Fiscal Affairs

The Comptroller would be required to review that government's compliance with the balanced budget requirement within one year following receipt of its budget. In the case of budget modifications filed after such review, the Comptroller would be required to review them following their filing. Thus the Comptroller would be able to establish an annual review cycle which gives earliest attention to local government showing signs of difficulty yet establishes a performance record for all local government.

In addition to his review function, it is anticipated that the Comptroller would issue reports based on such reviews where he deemed it appropriate. Such reviews and reports, if any, should provide an early warning of fiscal difficulties which might affect a local government's credit-worthiness and should prompt local officials to take appropriate remedial action at the earliest opportunity.

Local governments that have operated with budget deficits in any one or more of the three fiscal years preceding a budget year will be subject to increased reporting requirements if the deficits amount, in the aggregate, to 3% or more of the total revenues projected for the budget year. In addition, the Comptroller is authorized to impose additional reporting requirements

on local governments where he determines that the credit-worthiness of the local government has been threatened by circumstances such as a default in a scheduled payment of principal or interest.

Under the increased reporting requirements, local governments would submit quarterly reports of operations, in such detail as the Comptroller may deem necessary, for prompt review by the Comptroller to monitor compliance with the balanced budget requirement and with requirements relating to the issuance of debt. The Comptroller is also given discretion to require such additional reports as he may deem necessary. For example, it is anticipated that he would require four year financial plans from such local governments to insure that adequate attention is given to the budgetary planning efforts necessary to restore a local government to fiscal health.

Quarterly reporting requirements which have been imposed as a result of budget deficits will terminate when the locality has operated without a deficit for three successive fiscal years. Where the requirements have been imposed at the discretion of the Comptroller, they will terminate upon a finding by the Comptroller that the problems or circumstances which warranted their imposition no longer exist.

Although the proposed legislation does not empower the Comptroller to mandate specific remedial actions by local governments, the findings in these reports and any proposals for remedial action are to be reviewed with the appropriate local officials. Presumably, these reports will prompt corrective action and, as a practical matter, should restrict the market for the local government's debt until the difficulties have been addressed. If they are not sufficient to prompt remedial action, the legislation, as noted below, would permit the Comptroller to bring suit to compel compliance with the balanced budget requirement.

The Comptroller is also required to prepare, annually, a report for the Governor concerning local governments under his supervision. This report is to be delivered to the Legislature, as well, for its consideration. The report would set forth the problems encountered by such local governments in their fiscal operations and the progress being made towards the resolution of these problems.

Where circumstances warrant the imposition of additional fiscal controls, it is anticipated that the Comptroller's reports would prompt the Legislature and the Governor to consider proposals for control mechanisms and other appropriate fiscal disciplines. As noted, the Committee thinks that such proposals can be developed best within the context of the local government's economic and political situation at the time it is experiencing fiscal difficulty.

5. Comptroller's Legal Remedies

In a situation where a local government is found not to be in compliance with the balanced budget or other legal requirements relating to its fiscal condition, the Comptroller would be specifically authorized to bring suit to compel compliance. The power to bring such a suit, with its probable impact on the marketability of the local government's obligations, is intended to

provide the Comptroller with leverage with which to enforce his newly granted statutory responsibilities.

Respectfully submitted,

THE COMMITTEE ON MUNICIPAL AFFAIRS

GEORGE H. P. DWIGHT, Chairman	EVAN A. DAVIS,† Chairman,
JAY W. WAKS, Secretary	Subcommittee on Local Finance
HOWARD J. AIBEL	JOHN M. ALLEN, JR.*
FREDERIC S. BERMAN**	JOHN BENDER*
JAMES S. BOYNTON	ALBERT L. BESWICK*
JOHN V. CONNORTON, JR.	EILEEN EVERS CARLSON
PAUL A. CROTTY	EDWARD N. COSTIKYAN
PATRICK J. FALVEY	GORDON J. DAVIS
GARY W. GARSON	MARILYN F. FRIEDMAN
THEODORE P. HALPERIN	PETER R. HAJE*
STEPHEN A. LEFKOWITZ	ROBERT A. KANDEL
JON J. MASTERS	BURTON HAROLD MARKS
CHARLES G. MOERDLER	MARK A. MEYER
ROSWELL B. PERKINS*	MILTON MOLLEN**
DONALD J. ROBINSON	ROBERT PRICE
JAMES P. SULLIVAN	EDITH L. SPIVACK
JEFFREY L. ZUKERMAN	CLARENCE J. SUNDRAM

KENNETH F. HARTMAN, Project Director

* Adjunct Member.

** The Judicial members of the Committee, Milton Mollen and Frederic S. Berman, have participated in the Committee's deliberations but have taken no position with respect to the contents of the Report.

† Mr. Davis succeeded Mr. Dwight as Chairman on October 1, 1978.

FOOTNOTES

1 Official Statement relating to $105,995,000 General Obligation Bonds of the City of New York dated August 25, 1978, pp. 78, 86–87 (hereafter N.Y.C. official Statement 1978).

2 Donald J. Robinson believes that the Constitution should not contain debt limits, but if debt limits are to be included, he favors the Committee's proposal for debt limits based on revenues and percentage limitations to be specified by statute.

3 Including: Report of the Special Committee on the Constitutional Convention, April, 1967, the Association of the Bar of the City of New York; Report to the Governor N.Y.S. Moreland Act Commission on the Urban Development Corporation, et al., "Restoring Credit and Confidence . . . A reform program for New York State and its Public Authorities," March 21, 1976.

4 Edward Dana Durand, *The Finances of New York City*, 1898, p 33.

5 L. 1812, ch. 99.

6 Frank LeRoy Spangler, Special Report of the State Tax Commission No. 5, *Operation of Debt and Tax Rate Limits in the State of New York*, Albany, 1932, p. 43.

7 Charles Z. Lincoln, *The Constitutional History of New York*, Vol. II, Rochester, 1906, pp. 198–199.

8 1846 Constitution, Art. VIII, §9.

9 Lincoln, *op. cit.* Vol. II, p. 358; New York Constitutional Convention, 1867–8, Proceedings and Debates, Vol. 5, p. 3606.

10 Spangler, *op. cit.*, p. 45.

11 In later years the Court of Appeals in *Sun Printing and Publishing Assoc. v. The Mayor*, 152 N.Y. 257, 268–269 (1897) said:

> Under . . . [the Town Bonding Act] numerous railroads had been built upon the bonds procured from towns through which they were constructed in return for stock issued by the corporation . . . So great was the evil and so heavy the burden upon the towns that relief was sought through a constitutional provision . . . The towns had subscribed for the stock in private corporations and in most instances they had lost.

12 *State of New York, Messages from the Governors*, ed. Charles Z. Lincoln, Vol. VI, p. 402.

13 New York Constitutional Commission, 1872–73, Journal—Appendix No. 1, p. 5.

14 Spangler, *op. cit.*, p. 50.

15 N.Y.S. Temporary Commission on the Revision and Simplification of the Constitution—Staff Report No. 32, *Constitutional Debt Limits for Local Governments* (unpublished draft) April 1960, pp. 28–31.

16 *Id.* at 33.

17 N.Y.S. Constitutional Convention, 1938, *Revised Record*, Vol. II, p. 1076.

18 Stephen M. Lounsberry, *The Scope and Basis of the Local Finance Law*, 1945, McKinney's Local Finance Law, pp. xiv-xv.

19 L. 1939, ch. 958. Officially known as the Temporary State Commission for Codification and Revision of the Laws Relating to Municipal Finances, the Municipal Finance Commission was empowered to study existing laws and to codify, revise and make uniform as far as possible the state statutes pertaining to finances of state municipal subdivisions and districts.

20 L. 1942, ch. 424; constituting c.33-A of the Consolidated Laws; effective September 1, 1945.

21 L. 1946, ch. 228.

22 N.Y.S. Constitutional Convention, 1938, *op. cit.*, Vol. II, pp. 1076, 1081.

23 N.Y.S. Temporary Commission on the Revision and Simplification of the Constitution (Staff Report No. 32, *op. cit.*, pp. 63–66).

24 See 1949, 1951 and 1953 McKinney's Session Laws of New York for Constitutional proposals. Also see First, Second and Third Report of the State Comptroller's Committee on Constitutional Tax and Debt Limitation and City-School Fiscal Relations for discussion of proposals (1948, 1949, 1950 respectively).

25 According to the N.Y.S. Temporary Commission on the Revision and Simplification of the Constitution (*op. cit.*, p. 76), the introduction of so much transitory material "lengthened the text of the provisions from about 1,000 words to about 6,000, making it correspondingly more complicated . . . Most of the changes made . . . were based on conjecture, rather than on tested data . . . with the wholly unexpected result of making the debt limits completely meaningless for most localities."

26 Among the provisions adopted were an exception to the gifts and loans provisions to permit increased pension payable to retired members of police or fire departments or their dependents; and an exclusion for indebtedness contracted by a municipality for sewage facilities on or after January 1, 1962 and prior to January 1, 1983.

27 Temporary Commission on City Finances, Final Report, *Better Financing for New York City*, August, 1966, Introduction, p. 3, Table 1.

28 *Id.* at 79.

29 N.Y.C. Charter, §128. Tax appropriation and general fund stabilization reserve fund.

[30] Temporary Commission on City Finances, 1966, *op. cit.*, p. 57, Table 3— Decline in Major City Reserves June 30, 1961 to June 30, 1965.

[31] N.Y.C. Charter, §128, subd. g as added by L.L. 1963, No. 31.

[32] L.L. 1964, No. 15; L.L. 1968, No. 58; L.L. 1969, No. 42; L.L. 1970, No. 24; L.L. 1971, No. 47; L.L. 1972, No. 49; L.L. 1973, No. 30; L.L. 1974, No. 25; L.L. 1975, No. 34; L.L. 1976, No. 34; L.L. 1977, No. 44.

[33] Office of the Comptroller, City of New York, "Report of the Comptroller Pursuant to Section 113 of the Charter With Respect to the Proposed Expense Budget for 1976–1977," February 14, 1976 as quoted in the *City Record*, February 24, 1976, p. 500.

[34] *Id.* The Tax Deficiency Account is established pursuant to N.Y.C. Charter, §127.

[35] Annual Report of the Comptroller of the City of New York for the Fiscal Year 1975–1976, p. 157.

[36] Temporary Commission on City Finances, 1966 *op. cit.*, p. 229—Appendix Table 1—Funds to Finance Annual Deficits—Reserve Depletion and Borrowing to Balance Expense Budgets City of New York, 1961–1962 to 1966–1967.

[37] L. 1965, ch. 441.

[38] McKinney's Session Laws of New York, 1965, p. 2065, Memorandum of Legislative Representative of City of New York.

[39] Securities and Exchange Commission Staff Report on Transactions in Securities of the City of New York, (hereafter SEC Staff Report), August, 1977, Ch. 2, p. 10.

[40] McKinney's Session Laws of New York, 1965, p. 2064, Memorandum of Legislative Representative of City of New York.

[41] L. 1971, ch. 957.

[42] A state audit report gives some indication of the extent to which the City had been overstating its state and federal aid receivables:

> We examined $373.3 million out of $434.2 million of fiscal 1973 and 1974 State and Federal aid receivables as of March 31, 1975 and found them to be overstated by $324.8 million (Report NYC-3-76). This gross overstatement meant that the City had similarly overstated its prior years revenues; borrowed against these overstated receivables, and; reported better year-end results than actually experienced.

Office of the State Comptroller, Division of Audits and Accounts, *Summary of Audit Reports Relative to Central Budgetary, Accounting and Finance Systems and Reporting Practices of New York City*, Audit Report NYC-63-78, April 19, 1978, p. 6.

[43] *Id.* at 8. See also SEC Staff Report, *op. cit.*, Ch. 2, pp. 27–34 for further discussion of the City's real estate tax practices.

[44] L. 1965, ch. 440.

[45] McKinney's Session Laws of New York, 1965, p. 2063, Memorandum of Legislative Representative of City of New York.

[46] 24 A.D. 2d 151 at 154, aff'd 17 N.Y. 2d 628 (1966).

[47] Temporary Commission on City Finances, 1966, *op. cit.*, p. 79-80.

[48] Local Finance Law, §11.00, par. a subd. 73 as added by L. 1968, ch. 1080.

[49] Local Finance Law, §11.00, par. a, subd. 78 set out second, as added by L. 1973, ch. 898.

[50] 34 N.Y. 2d 628 (1974).

[51] The Final Report of the Temporary Commission on City Finances, June, 1977, (hereafter TCCF Report 1977), *The City in Transition: Prospects and Policies for New York*, p. 5.

[52] Subdivision 5 of Section 3038 of the Municipal Assistance Corporation for the City of New York Act, as added by L. 1975, ch. 169, §1. Subdivision 5 was recently amended by L. 1978, ch. 201, §59 to provide that for the fiscal year ending June 30, 1982 and thereafter, no expense items shall be included in the city's capital budget, thus shortening the ten year period to six years. See also N.Y.C. Charter, §225, subd. c.

[53] Local Finance Law, §150.00, subd. d as added by L. 1968, ch. 1089, §10.

[54] Constitution, Art. XVIII, §4.

[55] Constitution, Art. VIII, §4.

[56] Local Finance Law, §152.00

[57] Local Finance Law, §136.00, subd. 3.

[58] Municipal Assistance Corporation for the City of New York—Annual Report 1976 (hereafter MAC Annual Report 1976), p. 7.

[59] TCCF Report 1977, *op. cit.*, p. 5.

[60] MAC Annual Report 1976, *op. cit.*, p. 7.

[61] Local Finance Law, §25.00, par. b.

[62] L. 1969, ch. 12.

[63] E.g., Transit Construction Fund, Public Authorities Law §§1225-a *et. seq.* as added by L. 1972, ch. 576; and N.Y.C. Sports Authority, Public Authorities Law, §§2500 *et. seq.* as added by L. 1973, ch. 816

[64] See N.Y.C. Official Statement 1978, *op. cit.*, "Public Benefit Corporation Indebtedness," pp. 97–102 for full discussion of N.Y.C. liabilities under financing arrangements with PBCs.

[65] Public Authorities Law, §§2530 *et. seq.* as added by L. 1974, ch. 594.

[66] Public Authorities Law, §2533.

[67] Public Authorities Law, §2538.

[68] New York City Stabilization Reserve Corporation, Official Statement and Notice of Sale dated January 31, 1975 Relating to $260,000,000 NYCSRC Bond Anticipation Notes, First Issue, p. 2.

[69] *Wein* v. *The City of New York*, 36 N.Y. 2d 610 (1975).

[70] "If the City were to account for pension costs on an accrual basis, the City Actuary has estimated that the additional cost would amount to $100 million in the 1978 fiscal year and $140 million in the 1979 fiscal year . . . GAAP requires that pension costs be accounted for on an accrual basis. Accordingly, the Four Year Financial Plan calls for the City to account for pension costs on an accrual basis by its 1982 fiscal year." N.Y.C. Official Statement, 1978, *op. cit.*, p. 30.

[71] N.Y.C. Official Statement 1978, *op. cit.*, "Unfunded Accrual Liability," p. 74. Furthermore, the "City Actuary has recently determined that the unfunded accrual liability of the five major actuarial systems as of June 30, 1976 was approximately $9.40 billion using the revised actuarial assumptions that have recently been adopted . . ."

[72] SEC Staff Report, *op. cit.*, Ch. 2, p. 80.

[73] Indeed, the central finding of the Temporary Commission on City Finances in 1977 is that:

> . . . The City's problems are not essentially fiscal but manifestations of deep-seated problems stemming from highly interactive developments in the socioeconomic structure of the city, inter-governmental relations and the local governmental process.

TCCF Report 1977, *op. cit.*, p. 2.

[74] See TCCF Report 1977, *op. cit.*, MAC Annual Report 1976 *op. cit.*; *New York City and the Urban Fiscal Predicament* by J. Ward Wright (Municipal Finance

Officers Association, Study No. 2, April 1976); U.S. Congress, Congressional Budget Office, *New York City's Fiscal Problem: Its Origins, Potential Repercussions and Some Alternative Policy Responses*, Background Paper No. 1 (Washington, D.C., October 10, 1975).

76 L. 1972, ch. 430.

77 McKinney's 1972 Session Laws of New York, Vol. II, p. 3393.

78 L. 1975, ch. 419.

79 L. 1969, ch. 1039.

80 L. 1970, ch. 1008.

81 L. 1972, ch. 365.

82 L. 1972, ch. 756.

83 L. 1972, ch. 759.

84 L. 1974, ch. 154.

85 L. 1975, ch. 376.

86 L. 1975, ch. 304.

87 L. 1975, ch. 30.

88 L. 1976, ch. 432.

89 L. 1977, ch. 390.

90 L. 1977, ch. 954.

91 L. 1969, ch. 124 as amended by L. 1973, ch. 305.

92 L. 1971, ch. 1200, as amended by L. 1973, ch. 304.

93 L. 1975, ch. 871, §8.

94 Official Statement relating to $83,680,000 City of Yonkers, N.Y. General Obligation Serial Bonds—1976 (Special Finance and Budget Act Issue) dated October 15, 1976, p. 3; L. 1976, ch. 488 and ch. 489.

95 Section 5 of the New York State Financial Emergency Act for the City of Yonkers, as added by L. 1975, ch. 871, §2.

96 L. 1976, ch. 488 and ch. 489.

97 L. 1978, ch. 457.

98 L. 1976, ch. 3.

99 L. 1978, ch. 279.

100 L. 1978, ch. 280.

101 The Bond Buyer's 1976 Municipal Finance Statistics Vol. 15 (June 1977), at p. 25.

102 *Id.* at 5.

103 *Id.* at 35.

104 *Id.*

105 Preliminary data compiled by Comptroller's Office Division of Municipal Affairs.

106 Local Finance Law, §§50.00, 60.00(c).

107 Local Finance Law, §109.00.

108 General Municipal Law, Article 3.

109 General Municipal Law, §§33–38.

110 Donald J. Robinson does not believe that there is sufficient evidence to sustain a finding that information supplied in connection with the offer and sale of obligations of such local governments is inadequate.

111 The Municipal Securities Full Disclosure Act of 1976 (S. 2969).

112 The Municipal Securities Full Disclosure Act of 1977 (S. 2339).

APPENDIX A

TEXT OF PROPOSED LOCAL FINANCE ARTICLE

CONCURRENT RESOLUTION OF THE SENATE AND ASSEMBLY

Proposing a new article eight and amendments of articles ten and eighteen of the constitution, in relation to local finances, and repealing article eight and section four of article eighteen of the constitution relating thereto

Section 1. Resolved (if the Senate concur), That article eight of the constitution be hereby REPEALED and a new article, to be article eight, be inserted therein, in lieu thereof, to read as follows:

ARTICLE VIII—LOCAL FINANCES

Sec.

1. Gift or loan of money, property or credit prohibited; when permitted.

2. Provision for payment of local indebtedness.

3. Limitations on local indebtedness.

4. Limitations on local taxation.

5. Local governments to have balanced budgets.

6. Indebtedness not to be invalidated by operation of this article.

7. Duties of the legislature.

8. Restrictions on the creation of certain corporations.

9. Definition.

§1. Gift or loan of money, property or credit prohibited; when permitted.

(a) No local government shall give or loan its money, property or credit, except as authorized by law for a public purpose, including provision of assistance necessary to promote the betterment of a local government or its economy.

(b) The legislature may authorize cooperation between local governments to provide jointly any service or facility which each of such units has power to provide independently; to contract joint or several indebtedness therefor; and to contract with each other for use of such service or facility.

§2. Provision for payment of local indebtedness

No indebtedness shall be contracted by any local government unless such local government shall have pledged its faith and credit for the payment of the principal thereof and the interest thereon. Provision shall be made in each fiscal year by every local government for the payment of interest on all indebtedness and for the amounts required for repayment of all principal thereof maturing or otherwise coming due during such fiscal year. If at any time the respective authorities shall fail to make such provision for payment or shall fail to make payment, 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 such local government 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.

§3. Limitations on local indebtedness

(a) No local government shall contract indebtedness except as authorized by law. No county wholly contained within a city shall contract indebtedness. The amount

of indebtedness which each local government may contract shall be limited by law. In the case of indebtedness other than indebtedness contracted in anticipation of the receipt of taxes and revenues, or the renewal or refunding thereof, the legislature shall by general law prescribe limitations on the amount of indebtedness which each local government may contract which shall be an amount equal to a percentage of the revenues, as defined by law, of the local government computed over a specific period immediately preceding the year of the contracting of such indebtedness. No local government may contract indebtedness for any purpose or in any manner which, including existing indebtedness, shall exceed such limitation. The limitations so prescribed shall exclude all indebtedness (1) for any project that is self-liquidating or self-supporting or (2) which has been approved by referendum held in such manner as shall be provided by law. No act providing for an increase in such limitations shall become law until passed by two consecutive sessions of the legislature. The comptroller, or if the legislature so provides, a board over which the comptroller shall preside, shall have the power and duty further to limit the amount of indebtedness which may be contracted by any local government and the terms upon which such indebtedness may be contracted so as to preserve credit and avoid deficits. The legislature shall determine the method for the allocation or apportionment of any indebtedness arising out of joint undertakings.

(b) No indebtedness, other than indebtedness contracted in anticipation of the receipt of taxes and revenues, shall be contracted for longer than the period of probable usefulness of the object or purpose for which such indebtedness is to be contracted, to be determined by law, which determination shall be conclusive. No such indebtedness heretofore or hereafter contracted or any portion thereof shall be refunded beyond such period of probable usefulness computed from the date such refunded indebtedness was originally issued.

(c) No local government shall contract indebtedness in anticipation of the receipt of taxes and revenues, direct or indirect, except for the purposes of and within the amounts of appropriations theretofore made. No such obligations or any renewal thereof shall be issued unless it is reasonably anticipated that such taxes and revenues will be received in an amount sufficient to provide for the payment thereof. Such obligations shall mature within one year and unless such obligations and any renewals thereof shall mature within the fiscal year of issuance, appropriation shall be made for their payment with interest thereon. In no event shall such obligations and any renewals thereof mature later than the end of the fiscal year following the fiscal year of original issuance.

(d) No local government shall contract indebtedness in anticipation of the receipt of the proceeds of the sale of bonds theretofore authorized except for the purposes and within the amounts of the bonds so authorized. Such obligations and renewals thereof shall, with interest thereon, be paid within the period fixed by law which period shall not exceed five years from the date of original issue. At the end of such period such obligations may be renewed for an additional period not to exceed one year provided that appropriation shall be made for their payment, with interest thereon.

§4. Limitations on Local Taxation

(a) No local government shall levy taxes except as authorized by law, provided, however that the legislature shall not restrict the power of any local government to levy taxes on real estate without limit for the payment of interest on or principal of indebtedness.

(b) In any county, city, village or school district, the amount to be raised by tax

on real estate in any fiscal year, in addition to providing for the interest on and principal of all indebtedness, shall not exceed an amount equal to the following percentages of the average full valuation of taxable real estate of such county, city, village or school district, less the amount to be raised by tax on real estate in such year for the payment of interest on and redemption of notes issued in anticipation of the receipt of taxes or revenues or renewals thereof and less a portion, determined in manner fixed by law, of any tax on real estate authorized to be imposed other than for the payment of interest on and principal of indebtedness by any other local government hereafter created which is coterminous with or wholly or partly within such county, city, village or school district.

(1) any county, for county purposes, one and one-half per centum; provided, however, that the legislature may prescribe a method by which such limitation may be increased not to exceed two per centum;

(2) any city of one hundred twenty-five thousand or more inhabitants according to the latest federal census, for city purposes, two per centum;

(3) any city having less than one hundred twenty-five thousand inhabitants according to the latest federal census, for city purposes, two per centum;

(4) any village, for village purposes, two per centum;

(5) any school district which is coterminous with or partly within or wholly within, a city having less than one hundred twenty-five thousand inhabitants according to the latest federal census, for school district purposes, one and one-quarter per centum; provided, however, that if the taxes subject to this limitation levied for any such school district for its first fiscal year beginning on or after July first, nineteen hundred forty-seven, were in excess of one and one-quarter per centum but not greater than one and one-half per centum, then for such school district the limitation shall be one and one-half per centum; or if such taxes were in excess of one and one-half per centum but not greater than one and three-quarters per centum for such fiscal year, then for such school district the limitation shall be one and three-quarters per centum; or if such taxes were in excess of one and three-quarters per centum for such fiscal year, then for such school district the limitation shall be two per centum. The limitation herein imposed for any such school district may be increased by the approving vote of sixty per centum or more of the duly qualified voters of such school district voting on a proposition therefor submitted at a general or special election. Any such proposition shall provide only for an additional one-quarter of one per centum in excess of the limitation applicable to such school district at the time of submission of such proposition. When such a proposition has been submitted and approved by the voters of the school district as herein provided, no proposition for a further increase in such limitation shall be submitted for a period of one year computed from the date of submission of the approved proposition, provided that where a proposition for an increase is submitted and approved at a general election or an annual school election, a proposition for a further increase may be submitted at the corresponding election in the following year. The legislature shall prescribe by law the qualifications for voting at any such election. In the event any such school district shall be consolidated with any one or more school districts, the legislature shall prescribe a limitation, not exceeding two per centum, for such consolidated district. Thereafter, such limitation may be increased as provided in this subparagraph (5). In no event shall the limitation for any school district or consolidated school district described in this subparagraph (5) exceed two per centum.

(6) Notwithstanding the provisions of subparagraphs (1) and (2) of this section, the city of New York and the counties therein, for city and county purposes, a combined total of two and one-half per centum.

(c) The average full valuation of taxable real estate of such county, city, village or school district shall be determined by taking the assessed valuation of taxable real estate on the last completed assessment rolls and the four preceding roles of such county, city, village or school district, and applying thereto the ratio which such assessed valuation on each of such rolls bears to the full valuation, as determined by the state tax commission or by such other state officer or agency as the legislature shall by law direct. The legislature shall prescribe the manner by which such ratio shall be determined by the state tax commission or by such other state officer or agency.

(d) For the purpose of determining the amount of taxes which may be raised on real estate pursuant to paragraphs (b) and (c) of this section, the revenues received in each fiscal year by any county, city or village from a public improvement or part thereof, or service, owned or rendered by such county, city or village for which bonds or capital notes are issued after January first, nineteen hundred fifty, shall be applied first to the payment of all costs of operation, maintenance and repairs thereof, and then to the payment of the amounts required in such fiscal year to pay the interest on and the amortization of, or payment of, indebtedness contracted for such public improvement or part thereof, or service. The provisions of this paragraph shall not prohibit the use of excess revenues for any lawful county, city or village purpose. The provisions of this paragraph shall not be applicable to a public improvement or part thereof constructed to provide for the supply of water.

(e) Whenever any county, city, village or school district provides by direct budgetary appropriation for any fiscal year for the payment in such fiscal year or in any future fiscal year or years of all or any part of the cost of an object or purpose for which a period of probableness usefulness has been determined by law, the taxes required for such appropriation shall be excluded from the tax limitation prescribed by this section unless the legislature otherwise provides.

(f) Nothing contained in this section shall be deemed to restrict the powers granted to the legislature by other provisions of this constitution to further restrict the powers of any local government to levy taxes on real estate.

§5. Local governments to have balanced budgets.

Every local government shall for each fiscal year adopt and maintain a balanced budget, as defined by law.

§6. Indebtedness not to be invalidated by operation of this article.

No indebtedness of a local government valid at the time of its inception shall thereafter become invalid or the rights of holders thereof be impaired by reason of the operation of any of the provisions of this article.

§7. Duties of the legislature.

It shall be the duty of the legislature, subject to the provisions of this article, to restrict the power of taxation, assessment, borrowing money, contracting indebtedness, and loaning the credit of local governments so as to assure sound fiscal practices and prevent abuses in taxation and assessments and in the contracting of indebtedness by them.

§8. Restrictions on the creation of certain corporations.

No public corporation having both the power to levy taxes and contract indebtedness shall hereafter be established or created unless the authority to exercise such powers shall be vested in persons elected as may be provided by law by the voters of the region within which such corporation conducts its operations.

§9. Definition

Whenever used in this article the term "local government" shall mean or include a county, city, town, village or school district, or other public corporation having both the power to levy taxes and contract indebtedness.

§2. Resolved (If the Senate concur), That the fourth unnumbered paragraph of section five of article ten of the constitution be amended to read as follows:

[Neither] *Except as otherwise provided in this constitution, neither* the state nor any political subdivision thereof shall at any time be liable for the payment of any obligations issued by such a public corporation heretofore or hereafter created, nor may the legislature accept, authorize acceptance of or impose such liability upon the state or a political subdivision thereof; but the state or a political subdivision thereof may, if authorized by the legislature, acquire the properties of any such corporation and pay the indebtedness thereof.

§3. Resolved (If the Senate concur), That section four of article eighteen of the constitution be hereby REPEALED.

§4. Resolved (If the Senate concur), That section five of article eighteen of the constitution be amended to read as follows:

§5. Any city, town or village shall be liable for the repayment of any loans and interest thereon made by the state to any public corporation, acting as an instrumentality of such city, town or village. [Such liability of a city, town or village shall be excluded in ascertaining the power of such city, town or village to become indebted pursuant to the provisions of this article, except that in the event of a default in payment under the terms of any such loan, the unpaid balance thereof shall be included in ascertaining the power of such city, town or village to become so indebted.] No subsidy, in addition to any capital or periodic subsidy originally contracted for in aid of any project or projects authorized under this article, shall be paid by the state to a city, town, village or public corporation, acting as an instrumentality thereof, for the purpose of enabling such city, town, village or corporation to remedy an actual default or avoid an impending default in the payment of principal or interest on a loan which has been theretofore made by the state to such city, town, village or corporation pursuant to this article.

§5. Resolved (If the Senate concur), That the foregoing amendments be referred to the first regular legislative session convening after the next succeeding general election of members of the assembly, and, in conformance with section one of article nineteen of the constitution, be published for three months previous to the time of such election.

APPENDIX B

TEXT OF PROPOSED DISCLOSURE LEGISLATION

AN ACT to amend the local finance law and the general municipal law, in relation to the filing by a municipal corporation, school district or district corporation of an official statement and a summary annual report with the state comptroller

The People of the State of New York, represented in Senate and Assembly, do enact as follows:

Section 1. Section 51.00 of the local finance law is hereby amended by adding thereto a new paragraph, to be paragraph eleven, to read as follows:

11. If an official statement was filed in connection with the sale of the obligation, pursuant to section 57.00 or 60.00 of this chapter, a statement to the effect that (a) New York statutes in effect at the date of original issuance of the bond or note

required (subject to certain qualifications) the filing with the state comptroller of a summary annual report by the municipality, school district or district corporation issuing the obligation after the end of each fiscal year, and (b) upon request, a copy of the most recent summary annual report of such municipality, school district or district corporation on file with the state comptroller, together with a copy of any report of examination by the state comptroller of the accounts of such municipality, school district or district corporation which are presented in such summary annual report, will be furnished by such municipality, school district or district corporation (upon payment of such charge, if any, as the state comptroller may prescribe).

§2. Section 57.00 of such law is hereby amended by adding thereto, a new paragraph, to be paragraph e, to read as follows:

e.1. Filing of official statement. Each sale of bonds pursuant to this section shall be preceded by the filing with the state comptroller of an official statement by the municipality, school district or district corporation which proposes to issue such bonds.

2. Content of official Statement. The state comptroller shall adopt a rule or order, which he may amend from time to time, prescribing (a) the information to be included in such official statement, relevant to purchasers of the bonds, and (b) such other requirements as he may deem reasonable relating to the use of such an official statement. In developing such rule or order the state comptroller shall give consideration to (and may adopt in their entirety) voluntary disclosure standards promulgated by national organizations of local governments.

3. Form of financial statements. All financial statements presented in such official statement shall be prepared either (a) in accordance with such system of keeping accounts as may be formulated and prescribed by the state comptroller pursuant to section thirty-six of the general municipal law or (b) in accordance with generally accepted accounting principles as are in effect at the date of the official statement, but need not be audited. If the financial statements have been prepared as provided in the foregoing clause (a), such official statement shall also contain an explanation (which may be prescribed in rules of the state comptroller) as to any material differences between such system of keeping accounts and generally accepted accounting principles as are in effect at the date of the official statement.

4. Incorporation of summary annual report by reference. Subject to the rules of the state comptroller, such official statement may incorporate by reference any portion of the most recent summary annual report, if any, of the municipality, school district or district corporation, which has been filed pursuant to section thirty-one-a of the general municipal law, provided that the portion so incorporated by reference shall be attached to or included in such official statement.

5. Time of filing. Except as otherwise provided by rule or order of the state comptroller of general or particular applicability, the official statement required by this paragraph shall be filed at any time prior to the date fixed for the receipt of bids, or, in the case of a private sale, at any time prior to the sale of bonds. When so filed, such official statement shall be a public record open to inspection by any interested person. The state comptroller shall not be required to make any review of such official statement and shall not be empowered to delay the sale of bonds based upon the failure of such official statement to meet the information requirements prescribed by the state comptroller.

6. Signing of official statement. Such official statement shall be signed on behalf of the municipality, school district or district corporation offering bonds for sale (a) as to all financial statements, by the chief fiscal officer, (b) as to other portions

of the official statement, by the chief fiscal officer or such other person or persons as may be designated by the finance board of such municipality, school district or district corporation.

7. Liability. Nothing contained in this section shall create any right or cause of action against the municipality, school district or district corporation offering bonds for sale or against the individuals signing such official statement on its behalf which did not exist prior to the effective date of this section.

8. No effect on validity of bonds. Neither the failure to file such official statement nor the failure of such official statement to meet the information requirements prescribed by the state comptroller shall affect the validity of the bonds relating thereto.

9. Exemptions. The state comptroller, by rules or orders of general or particular applicability, may exempt any offering and sale of bonds (whether a single issue or sold as a single issue pursuant to paragraph c of this section and whether or not the sale is public within the meaning of paragraph a of this section) from the filing requirements of this paragraph if he determines that such filing is not necessary or appropriate in the public interest or for the protection of investors by reason of: (a) the aggregate principal amount of the bonds to be issued; or (b) the nature of the offerees and the number and nature of the purchasers of such bonds.

10. Filing of state comptroller's rules and orders. Any rule or order and amendments thereto adopted by the state comptroller under this paragraph shall be filed in the office of the secretary of state and in such other offices as the state comptroller may designate.

11. Furnishing copies of official statement. Copies of any official statement required to be filed pursuant to this paragraph will be furnished by the municipality, school district or district corporation filing such official statement to any person upon request, upon payment of such charge, if any, as the state comptroller may prescribe.

12. State comptroller to furnish sample forms. The state comptroller shall furnish to any municipality, school district or district corporation upon request sample forms of official statements together with copies of the pertinent rules of the state comptroller and supplementary instructions for the preparation of an official statement.

§3. Section 60.00 of such law is hereby amended by adding thereto, a new paragraph, to be paragraph f, to read as follows:

f.1. Filing of official statement. Each sale of notes pursuant to this section shall be preceded by the filing with the state comptroller of an official statement by the municipality, school district or district corporation which proposes to issue such notes.

2. Content of official statement. The state comptroller shall adopt a rule or order, which he may amend from time to time, prescribing (a) the information to be included in such official statement, relevant to purchasers of the notes, and (b) such other requirements as he may deem reasonable relating to the use of such an official statement. In developing such rule or order the state comptroller shall give consideration to (and may adopt in their entirety) voluntary disclosure standards promulgated by national organizations of local governments.

3. Form of financial statements. All financial statements presented in such official statement shall be prepared either (a) in accordance with such system of keeping accounts as may be formulated and prescribed by the state comptroller pursuant to section thirty-six of the general municipal law, or (b) in accordance with generally accepted accounting principles as are in effect at the date of the official statement, but need not be audited. If the financial statements have been prepared

as provided in the foregoing clause (a), such official statement shall also contain an explanation (which may be prescribed in rules of the state comptroller) as to any material differences between such system of keeping accounts and generally accepted accounting principles as are in effect at the date of the official statement.

4. Incorporation of summary annual report by reference. Subject to the rules of the state comptroller, such official statement may incorporate by reference any portion of the most recent summary annual report, if any, of the municipality, school district or district corporation, which has been filed pursuant to section thirty-one-a of the general municipal law, provided that the portion so incorporated by reference shall be attached to or included in such official statement.

5. Time of filing. Except as otherwise provided by rule or order of the state comptroller of general or particular applicability, the official statement required by this paragraph shall be filed at any time prior to the date fixed for the receipt of bids, or, in the case of a private sale, at any time prior to the sale of notes. When so filed, such official statement shall be a public record open to inspection by any interested person. The state comptroller shall not be required to make any review of such official statement and shall not be empowered to delay the sale of notes based upon the failure of such official statement to meet the information requirements prescribed by the state comptroller.

6. Signing of official statement. Such official statement shall be signed on behalf of the municipality, school district or district corporation offering notes for sale (a) as to all financial statements, by the chief fiscal officer, (b) as to other portions of the official statement, by the chief fiscal officer or such other person or persons as may be designated by the finance board of such municipality, school district or district corporation.

7. Liability. Nothing contained in this section shall create any right or cause of action against the municipality, school district or district corporation offering notes for sale or against the individuals signing such official statement on its behalf which did not exist prior to the effective date of this section.

8. No effect on validity of notes. Neither the failure to file such official statement nor the failure of such official statement to meet the information requirements prescribed by the state comptroller shall affect the validity of the notes relating thereto.

9. Exemptions. The state comptroller, by rules or orders of general or particular applicability, may exempt any offering and sale of notes (whether a single issue or sold as a single issue pursuant to paragraph c of this section and whether or not the sale is public within the meaning of paragraph a of this section) from the filing requirements of this paragraph if he determines that such filing is not necessary or appropriate in the public interest or for the protection of investor by reason of: (a) the aggregate principal amount of the notes to be issued; or (b) the nature of the offerees and the number and nature of the purchasers of such notes.

10. Filing of state comptroller's rules and orders. Any rule or order and amendments thereto adopted by the state comptroller under this paragraph shall be filed in the office of the secretary of state and in such other offices as the state comptroller may designate.

11. Furnishing copies of official statement Copies of any official statement required to be filed pursuant to this paragraph will be furnished by the municipality, school district or district corporation filing such official statement to any person upon request upon payment of such charge, if any, as the state comptroller may prescribe.

12. State comptroller to furnish sample forms. The state comptroller shall furnish to any municipality, school district or district corporation upon request

sample forms of official statements together with copies of the pertinent rules of the state comptroller and supplementary instruction for the preparation of an official statement.

§4. Section thirty of the general municipal law is hereby amended by adding thereto, a new subdivision, to be subdivision six, to read as follows:

6. All reports filed pursuant to this section or section thirty-one-a of this chapter shall be a public record open to inspection by any interested person. Upon request, any municipality, school district or district corporation required to file a summary annual report, pursuant to section thirty-one-a of this chapter, shall supply to any interested person (upon payment of such charge, if any, as the comptroller may prescribe) a copy of the most recent summary annual report of such municipality, school district or district corporation on file with the comptroller, together with a copy of any report of examination by the comptroller of the accounts of such municipality, school district or district corporation which are presented in such summary annual report.

§5. Such law is hereby amended by adding thereto, a new section, to be section thirty-one-a, to read as follows:

§31-a. Summary Annual Report

1. Applicability of this section. This section shall apply only to a municipality, school district or district corporation which (a) has issued bonds or notes after the effective date of this section, (b) has bonds outstanding at the close of its fiscal year, and (c) has not been exempted from the requirements of this section pursuant to subdivision eight of this section.

2. Filing of summary annual report. All reports filed with the comptroller pursuant to subdivision one of section thirty of this chapter by each municipality, school district or district corporation to which this section applies shall be accompanied by a summary annual report of information relevant to the holders of obligations of such municipality, school district or district corporation. Except as provided in subdivision five of this section, the summary annual report shall be filed within the applicable time period prescribed in subdivision five of section thirty of this chapter.

3. Content of summary annual report. The comptroller shall adopt a rule or order, which he may amend from time to time, prescribing the information to be included in such summary annual report. In developing such rule or order the comptroller shall give consideration to (and may adopt in their entirety) voluntary disclosure standards promulgated by national organizations of local governments. In prescribing the information to be included, the comptroller shall seek to conform, as nearly as may be practicable and appropriate, the requirements of this section with the requirements of paragraph e of section 57.00 of the local finance law and paragraph f of section 60.00 of the local finance law.

4. Form of Financial Statements. All financial statements presented in such summary annual report shall be prepared either (a) in accordance with such system of keeping accounts as may be formulated and prescribed by the comptroller pursuant to section thirty-six of this chapter, or (b) in accordance with generally accepted accounting principles as are in effect at the date of the summary annual report. If the financial statements have been prepared as provided in the foregoing clause (a), such summary annual report shall also contain an explanation (which may be prescribed in rules of that state comptroller) as to any material differences between such system of keeping accounts and generally accepted accounting principles as are in effect at the date of the summary annual report.

5. Extension for time of filing if financial statements are audited. If the financial

fiscal year covered by such budget, (ii) shall not propose to issue debt during the fiscal year covered by such budget, and (iii) shall not have incurred deficits during any of the three fiscal years preceding the fiscal year covered by such budget which amount, in the aggregate, to three per cent or more of the total revenues projected for such fiscal year.

1-c. If, on the basis of documents required to be filed with him pursuant to the provisions of this chapter or otherwise, the comptroller shall determine that a municipal corporation or a district corporation shall have incurred deficits during any of the three fiscal years preceding the fiscal year covered by its current budget which amount, in the aggregate, to three per cent or more of the total revenues projected for such year, or that any such corporation shall have taken actions, or suffered circumstances, which have affected such corporation adversely, or which threaten to affect adversely, the creditworthiness of the obligations of such corporation, the comptroller may require that such corporation deliver to the comptroller within thirty days after the end of each fiscal quarter a report of its financial condition at the end of such quarter, an operations report reflecting results of operations for such quarter and such other reports as the comptroller may determine would be necessary or desirable.

1-d. The obligation of a municipal corporation or of a district corporation to deliver reports to the comptroller pursuant to subdivision one-c of this section shall terminate upon the comptroller's determination that such corporation shall not have incurred a deficit for three successive fiscal years or, where the requirement to deliver such reports shall have been imposed at the discretion of the comptroller, upon a finding by the comptroller that the circumstances which warranted such reports no longer exist.

2. An annual financial report for each municipal urban renewal agency shall be made by the treasurer of the agency.

3. An annual report of the financial transactions shall be made by the treasurer of each public library and library service system established pursuant to section two hundred fifty-five of the education law, each county vocational education board established pursuant to section eleven hundred one of the education law and each board of cooperative educational services established pursuant to section nineteen hundred fifty-eight of the education law.

4. If for any reason, the comptroller shall deem it necessary that additional information be furnished by any other officer, he may require such additional information from such other officer in such form as he may deem necessary to carry into effect the purposes of this article.

5. All reports shall be certified by the officer making the same and shall be filed with the comptroller within sixty days after the close of the fiscal year of such municipal corporation, district, agency or activity. It shall be the duty of the incumbent officer at the time such reports are required to be filed with the comptroller to file such report. The refusal or wilful neglect of such officer to file a report as herein prescribed shall be a misdemeanor and subject the financial officer so refusing or neglecting to a penalty of five dollars per day for each day's delay beyond the sixty days to be paid on demand of the comptroller. Notwithstanding any of the provisions contained in this section, the city of New York shall file its report with the comptroller within four months after the close of its fiscal year.

§3. Such law is hereby amended by adding thereto, a new section, to be section thirty-one-a, to read as follows:

§31-a. Form of certain reports and documents to be filed with Comptroller. The annual budgets, and the material changes thereto, required to be filed with the comptroller pursuant to subdivision one-b of section thirty of this chapter, and the

reports required to be filed pursuant to subdivision one-c of section thirty of this chapter, shall be in the form to be prescribed by the comptroller.

§4. Section thirty-three of such law, as last amended by chapter six hundred ninety-six of the laws of nineteen hundred sixty-four, is hereby amended to read as follows:

§33. Accounts of officers to be examined

1. The comptroller shall cause the accounts of all officers of each such municipal corporation, district, agency and activity to be inspected and examined by one or more examiners of municipal affairs for such periods as the comptroller shall deem necessary. On every such examination inquiry shall be made as to the financial condition and resources of the municipal corporation, district, agency or activity, and into the method and accuracy of its accounts.

2. In the case of every municipal corporation and every district corporation which has filed a copy of its annual budget and any material modifications thereto pursuant to subdivision one-b of section thirty of this chapter, the comptroller shall cause a review of such budget and any material modifications thereto to be made within one year of the filing of such budget. With respect to any material modification to such budget submitted after such review, the comptroller shall cause a review of such modification to be made following the filing thereof.

3. In the case of each municipal corporation or district corporation which has filed with the comptroller such reports as may be required pursuant to subdivision one-c of section thirty of this chapter, the comptroller shall cause any such reports to be reviewed promptly. If the comptroller shall determine that a violation of law relating to the adoption and maintenance of balanced budgets or the issuance of debt exists which effects adversely or threatens to affect adversely the creditworthiness of the obligations of such corporation, he shall so notify and shall review with officials of such corporation such remedial action as may be appropriate for such corporation to effect compliance with law.

4. In the case of each municipal corporation or district corporation which is under the supervision of the comptroller pursuant to subdivisions one-c of section thirty of this chapter, the comptroller shall prepare for the governor and deliver to the legislature an annual report describing the financial condition of such corporations, including the difficulties encountered by them in complying with laws relating to the adoption and maintenance of balanced budgets and the issuance of debt and the progress being made by such corporations towards the resolution of such difficulties.

§5. Section thirty-four of such law, as last amended by chapter six hundred ninety-six of the laws of nineteen hundred sixty-four, is hereby amended to read as follows:

§34. Powers and duties of examiners

1. The comptroller and each examiner of municipal affairs shall have power to examine into the financial affairs of every such municipal corporation, district, agency and activity and to administer an oath to any person whose testimony may be required, and to compel the appearance and attendance of such person for the purpose of any such examination and investigation, and the production of books and papers. In the case of a municipal corporation or school district, no such person shall be compelled to appear or be examined elsewhere than within such municipal corporation or school district. In the case of any district other than a school district, no such person may be compelled to appear or be examined elsewhere