Note: New York - A City in Crisis: Fiscal Emergency Legislation and the Constitutional Attacks

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NEW YORK — A CITY IN CRISIS: FISCAL EMERGENCY LEGISLATION AND THE CONSTITUTIONAL ATTACKS

I. Introduction

Generous spending and, some would add, fiscal mismanagement have been a New York City tradition, putting tremendous pressures on both the City and State budgets. To forestall the deterioration of the City's financial condition and the subsequent collapse of the City itself, the New York State Legislature enacted a series of laws, many of which were feverishly incorporated into the body of State law in extraordinary session. With the creation of public authorities, the authorization of State funds to aid these authorities, and State hindrance of the payment of municipal debt service obligations, came inevitable claims in the courts that the State had attempted to circumvent constitutional debt limitations. The New York Court of Appeals responded to the constitutional attacks on the emergency legislation by manifesting, in a series of critical

1. E.g., in May, 1974, the New York State Legislature created the New York City Stabilization Reserve Corporation (SRC), a public benefit corporation authorized to sell bonds, the proceeds of which were to go directly to the City. N.Y. Pub. Auth. Law §§ 2530-51 (McKinney Supps. 1975 & 1976). In June, 1975, the Legislature created the Municipal Assistance Corporation for the City of New York (MAC), authorized to issue bonds, the proceeds of which were to be used to purchase City obligations. N.Y. Pub. Auth. Law §§ 3030-40 (McKinney Supps. 1975 & 1976). Also in June, 1975, the Legislature provided the administrative skeleton upon which to flesh out a municipal assistance corporation for any other city requiring one. N.Y. Pub. Auth. Law §§ 3001-21 (McKinney Supps. 1975 & 1976).


cases, a pragmatic, public policy attitude aimed at both the bond market and the individual investor. An examination of these decisions\(^5\) and the legislation which spawned the suits\(^6\) evinces the court's result-oriented approach toward what is in effect a bridling of legislative and municipal power.

II. The Legislation

A. The Stabilization Reserve Corporation

With the declaration "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,"\(^7\) the State Legislature created the Stabilization Reserve Corporation (SRC) to take effect May 30, 1974.\(^8\) This was the first of the legislative devices designed to generate much needed capital for New York City through the sale of bonds to the public. Its sole corporate purpose was to finance the delivery of essential services by the City during its economic distress\(^9\) by funneling proceeds of SRC bonds into the City's general fund.\(^10\)

The SRC was to establish a capital reserve fund\(^11\) out of which it was to pay the principal and interest on the bonds it issued. Income for the fund would be derived from the sale of corporate notes or bonds, appropriations from the City, and any other sources made available for this purpose.\(^12\) However, the statute did not compel the City to make these contributions; the relevant language shows they

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6. See notes 1-3 supra.
8. Id. §§ 2530-51 (McKinney Supps. 1975 & 1976). The full title of this enactment is the New York City Stabilization Reserve Corporation Act. Id. § 2530.
9. Id. § 2533.
10. Id. § 2538.
11. Id. § 2537.
12. Id. § 2537(1).
were purely discretionary. If the City were unable or unwilling to provide the SRC with enough money to maintain the capital reserve fund at an acceptable level, the statute authorized the State comptroller to make up the difference by diverting the City's share of the proceeds from the stock transfer tax directly to the SRC. If the fund were still deficient, the comptroller could channel to the corporation incoming per capita state and federal monies designated for the City. Any appropriations diverted from the City to the SRC would be credited to the City's share. Thus, directing incoming funds away from the City per se would not entitle the City to additional aid. Nonetheless, the SRC was the exclusive obligor on any debt it incurred: the Legislature absolved both the State and City from any liability thereon.

The mayor of New York was to certify to the SRC the amount which the City would need to deliver essential services to its citizens. The corporation was then permitted to issue its bonds or notes to obtain the required funds and deliver them to the City's general fund. Finally, the act provides for the corporation to be extinguished if 520 million dollars in aggregate bonds or notes are outstanding, issued by either the SRC itself, the City's Municipal Assistance Corporation (a public benefit corporation created subse-

13. Section 2537(1)(c) provides:
In order further to assure such maintenance of the capital reserve fund, there shall be paid by the city to the corporation for deposit in the capital reserve fund . . . such amount, if any, needed for the purpose of maintaining the . . . fund at the capital reserve fund requirement . . . ; provided that any such amount shall have been first appropriated by or on behalf of the city for such purpose or shall have been otherwise made available.

(emphasis added).

Section 2540(a) provides: "Since the corporation's continued discharge of its public and governmental purpose is of benefit to the city, the city shall pay, within the appropriations available therefor, the expenses of the establishment and continued operation of the corporation." (emphasis added).

14. The capital reserve fund requirement is defined in the act as that amount needed, as of a particular date, to pay interest on all of the corporation's outstanding bonds, the principal on all corporate bonds coming due on that date, and the sinking fund payments due as of that date on all outstanding corporate bonds. Id. § 2531(10).

15. Id. § 2540(b).
16. Id. § 2540(c).
17. Id. § 2542.
18. Id. § 2538.
quent to the SRC), or both together.

The lack of any absolutely committed source of capital made the bond market apprehensive about purchasing SRC bonds and notes. SRC obligations could not be sold. Ironically, a New York Court of Appeals decision upholding the State constitutionality of the corporate scheme extinguished any possibility of the obligations being saleable. The court held that "in no way can the city become indebted" on the debt service; rather, City appropriations were a permissible gift to a public corporation. In light of the overwhelming risk involved in purchasing SRC bonds, the SRC could not fulfill its corporate purpose by selling these securities, and thus, dissolved by its own terms.

B. The Municipal Assistance Corporations

In June, 1975 the Legislature authorized the creation of a City municipal assistance corporation, and passed enabling legislation (the State Act) to provide a model for similar public benefit corporations, partly in response to New York City’s fiscal crisis and partly in anticipation of similar situations occurring in other

22. Id. at 618, 331 N.E.2d 518, 370 N.Y.S.2d 556.
23. Id. at 618, 331 N.E.2d 518, 370 N.Y.S.2d 557.
24. N.Y. Pub. Auth. Law § 2542. The City municipal assistance corporation subsequently issued the full complement of bonds allowed to both the SRC and it together. In its first offering it noted that “[i]t is anticipated that, upon the completion of this offering, the Stabilization Reserve Corporation will not have issued any bonds or notes and that its existence will terminate.” Municipal Assistance Corporation for the City of New York 1975 Series A Bonds Official Statement, July 1, 1975, at 5.
27. Governor Carey, upon approval of the City Act stated that New York City . . . is facing a grave fiscal emergency with potentially far-reaching economic and social consequences for not only its own inhabitants, but for all residents of the Empire State. The approval of these bills represents a significant first step towards alleviating the fiscal problems of New York City while at the same time requiring the City to institute long-range corrective measures. Governor’s Memoranda, 1975 N.Y. Sess. Laws 1745 (McKinney).
The City Act creates a New York City municipal assistance corporation (MAC) specifically tailored to the exigencies of the City during its emergency period. The State Act delineates a general framework upon which to structure a municipal assistance corporation for any locality which the Legislature finds cannot meet payment on its municipal securities without interrupting essential services.

The State Act provides inter alia for a municipal assistance corporation administered by nine directors appointed by the Governor with the approval of the State Senate. The corporation's notes or bonds are not, according to the statute's term, the obligations of the state or municipality; rather, they are payable from corporate funds alone. Moreover, the State Act declares these notes or bonds to be legal securities for public investment purposes. To finance the corporation, the statute allows the establishment of both a municipal assistance tax fund, comprised of revenues from municipal assistance sales and compensating use taxes, and a per capita State aid fund.

The capital structure of MAC is based on three funds: (1) the capital reserve fund used to pay the principal on the corporation's bonds; (2) the debt service fund used to pay interest on principal and redemption of MAC's bonds and notes; and (3) the operating fund which covers operating expenses and administrative costs. Money for these funds is derived from State appropriations, the proceeds from the sale of MAC bonds or notes, and any other ac-

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32. Id. § 3016. Section 3012(c) provides that every note and bond issued is a general obligation of the corporation.
33. Id. § 3018.
37. Id. § 3036(1) (McKinney Supp. 1975).
38. Id.
ceptable source. The primary sources of State contributions are the sales and compensating use tax, the per capita State aid, and the stock transfer tax. The effect of these State appropriations is to divert revenues originally designated for City use to MAC's coffers. Thus, the City's total State aid is diminished by what MAC has received.

39. See notes 39-41 supra.
40. The State has established funds of its own to collect and keep revenues until they are requested by a municipal assistance corporation: the stock transfer tax fund, consisting mainly of the proceeds of the stock transfer tax (N.Y. STATE FIN. LAW § 92-b (McKinney 1974), as amended by chapter 878, § 8, 1977 N.Y. Sess. Laws 1770 (McKinney)); the municipal assistance tax fund consisting of revenues from sales and compensating use taxes and some per capita aid (Id. § 92-d (McKinney Supp. 1976), as amended by chapter 878, § 9, 1977 N.Y. Sess. Laws 1772 (McKinney)); and the municipal assistance State aid fund, comprised of per capita State aid appropriated thereto (Id. § 92-e (McKinney Supp. 1976)).
41. N.Y. TAX LAW §§ 1107, 1108 (McKinney Supp. 1976). The sales tax secures both the First Resolution (see RESOLUTION I, art. II, § 201) and the Second Resolution MAC bonds (see MUNICIPAL ASSISTANCE CORPORATION FOR THE CITY OF NEW YORK SECOND GENERAL BOND RESOLUTION (RESOLUTION II), art. II, § 201 (adopted Nov. 25, 1975)).
42. N.Y. STATE FIN. LAW § 54 (McKinney 1974). The per capita State aid secures Resolution II bonds only. See RESOLUTION II, art. II, § 201.
43. N.Y. TAX LAW § 270 (McKinney 1966). The stock transfer tax secures both First Resolution (see RESOLUTION I, art. II, § 201) and Second Resolution MAC bonds (see RESOLUTION II, art. II, § 201).

In Boston Stock Exchange v. State Tax Comm'n, 429 U.S. 318 (1977), the Supreme Court ruled that New York's stock transfer tax was unconstitutional as written. The tax law, as amended in 1968, gave a distinct advantage to non-residents participating in New York stock sales. To encourage the sale of securities within the state, the amendment afforded non-residents a 50 per cent stock transfer tax reduction on sales occurring in New York. Furthermore, the statute limited the total tax liability on a single New York sale to 350 dollars. N.Y. TAX LAW § 270-a (McKinney Supp. 1976). The Supreme Court found that by imposing a greater tax liability on out-of-state than on in-state sales of securities, the law fell "short of the substantially even-handed treatment demanded by the Commerce Clause." 429 U.S. at 332.

As a result of this decision, New York repealed the 50 per cent advantage. Chapter 878, §§ 2, 3, 1977 N.Y. Sess. Laws 1762 (McKinney). It also provided for the complete phase out of the tax by 1981 through a series of gradually increased rebates to the taxpayer. Id. § 6. Mindful, however, that the stock transfer tax proceeds were designated for MAC, the Legislature fashioned a system whereby MAC would receive such funds only up to the amount needed. Id. § 8. Presumably MAC must first turn to the sales tax and, where applicable, the per capita State aid before tapping the stock transfer tax.

The effect of this diminution of MAC's resources is yet unclear. Nonetheless, commentators seem untroubled. Arthur Hausker, vice president of municipal securities at Reynolds Securities, Inc., pointed out that the stock transfer tax is a reserve source available only "to the extent necessary." Moreover, he projected that both the First and Second Resolution bonds will be amply secured by the other taxes on which the corporation has a "first lien." Weekly Bond Buyer, Feb. 14, 1977, at 10, cols. 1 and 2.
44. N.Y. PUB. AUTH. LAW § 3036(1) (McKinney Supp. 1975).
Both municipal assistance corporation acts reduced the risk on bonds sold by such corporations by requiring that the State covenant to appropriate particular revenues only to the corporations. While this commitment of funds is not as tenuous as that to SRC, it still does not commit particular revenues absolutely. Each year the Legislature must recertify and redesignate these funds to the municipal assistance corporation; no constitutional guarantee exists that the Legislature will not eliminate these taxes from which the funds are derived. Therefore, if the State does not renew the appropriations, it has at most breached a covenant. Therein remains the risk to the investor.

The keynote provision in the City Act permits MAC to issue its own bonds or notes in exchange for the City's short-term obligations, provided the value of MAC obligations does not exceed that of the City's which it receives. MAC thereupon may deliver these City securities back to the City, which cancels them without paying the principal and interest. Thus, the statute in effect shifts the liability of these short-term debts from the City to MAC.

Furthermore, the mayor may certify to MAC that amount needed to pay the City's operating expenses or the principal, on maturity, of any of its short-term obligations (within statutory limits). MAC in turn may pay the City such amount, which would be held in trust for payment of the City's short-term debt service, or applied toward

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45. This covenant takes the form of a general pledge that the State will not limit or alter the bondholders' rights vested in the corporation "to fulfill the terms of any agreements made with" them. Id. § 3015.
47. The first MAC general bond resolution provides that the corporation will default if "the State Comptroller shall fail to pay to the Corporation . . . for deposit in the Capital Reserve Fund, the Debt Service Fund or the Operating Fund any amounts . . . as shall be certified by the Chairman . . . ." MUNICIPAL ASSISTANCE CORPORATION FOR THE CITY OF NEW YORK GENERAL BOND RESOLUTION (RESOLUTION I), art. XII, § 1202(c) (adopted July 2, 1975). Furthermore, the resolution provides that if the State fails or refuses to impose the sales or stock transfer taxes, or maintain the funds designed as receptacles for these taxes, the corporation will default. Id. §§ 1202(f), 1202(g).
48. Id. § 3035(1).
49. Id. § 3035(2). Such cancellation and delivery does not apply to notes issued in anticipation of bond proceeds (BANs). If MAC delivers these notes to the City, the City must pay the principal and accrued interest or pay the accrued interest and exchange City BANs of equal principal and interest rate. Id.
its operating expenses. Alternatively, MAC may buy City obligations up to the amount of the City's certified requirement.\textsuperscript{50}

Finally, in order to ascertain whether the City is complying with its statutory duties regarding its relationship with the corporation, MAC may "conduct a review of the records, accounts, budgets, forecasts, projections and other relevant materials of the city." The City is obligated to extend its cooperation to MAC investigators, and must inform MAC of the corrective measures it has taken in response to MAC directives.\textsuperscript{51}

\section{C. The Financial Emergency Act}

By September, 1975 New York City's financial collapse seemed imminent. The State Legislature was deeply concerned that the City would be unable to meet its debt service obligations and thus be foreclosed from seeking funds in the public markets. In an attempt to bring the City's finances under strict control and assure continuity of government operations,\textsuperscript{52} the Legislature enacted the New York State Financial Emergency Act for the City of New York (Emergency Act).\textsuperscript{53} The Emergency Act provides for a State Emergency Financial Control Board which wields review power over City operations and control over City funds to ensure that payment of debt service obligations receives highest priority.\textsuperscript{54} The Board is charged with the duty of reporting on the operations, management and productivity of the City, recommending corrective measures to be made in this regard, and obtaining information as to the City's financial needs and condition.\textsuperscript{55} MAC, too, has similar input into the City's management.\textsuperscript{56} Neither "review" statute, however, distinguishes the Board's functions in this regard from those of MAC, and a reading of both suggests a duplication of efforts.

The Emergency Act also requires the City to develop a plan, subject to the Board's review, to confront and alleviate its fiscal problems.\textsuperscript{57} The act further mandates that the public employees'
pension and retirement systems purchase specified sums of MAC obligations. Finally, the Legislature invoked the State police power to enable the City to obtain prior notice of a person's enforcing a debt against it, to obtain a stay against creditors until the City has developed a plan to prevent default (which plan could be approved by a State court), and to avail itself of any available federal relief.

D. The Emergency Moratorium Act

By October, 1975 the Board had approved a plan which relied on approximately five billion dollars in anticipated federal aid. However, when it became evident that these funds would not be received in time to permit the December 11, 1975 payment of 400 million dollars in City revenue anticipation notes, the Legislature, in special session, adopted the Emergency Moratorium Act (Moratorium Act).

On November 26, 1975, MAC extended an offer to holders of certain short-term City notes. The terms simply offered to exchange these City obligations, all scheduled to mature from mid-

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58. *Id.* sec. 7, enacting the Investment of Funds by Pension and Retirement Systems for Public Employees Act.

59. *Id.* sec. 19, adding title 6-A to article 2 of the Local Finance Law.


62. These City notes were both revenue anticipation notes (RANs) and bond anticipation notes (BANs). They were due as shown in Table I:

<table>
<thead>
<tr>
<th>Scheduled Maturity</th>
<th>Stated Annual Interest Rate</th>
<th>Type</th>
<th>Total Payable (in millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>12/11/75</td>
<td>9.50% RANs</td>
<td></td>
<td>$339.5</td>
</tr>
<tr>
<td>1/12/76</td>
<td>9.40% RANs</td>
<td></td>
<td>596.7</td>
</tr>
<tr>
<td>2/13/76</td>
<td>7.55% RANs</td>
<td></td>
<td>281.5</td>
</tr>
<tr>
<td>3/12/76</td>
<td>8.75% RANs</td>
<td></td>
<td>382.5</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>$1,600.2</td>
</tr>
</tbody>
</table>

*Exchange Offer To Holders of Certain Short-Term Notes of the City of New York Official Statement (Exchange Offer), Nov. 26, 1975, at 3.*

This offer did not embrace those City notes held by the eleven New York Clearing House Banks, and certain City pension funds. *Id.* at 4. It was scheduled to terminate December 29, 1975. *Extension of Tender Offer at 1.*
December, 1975, to mid-March, 1976, for ten-and-one-half-year, 8 percent MAC bonds, interest to be paid semi-annually. For those who did not avail themselves of this offer, the Moratorium Act allowed the payment of the stated annual interest on City notes only up to the date of scheduled maturity. Thereafter, the interest rate would drop to a flat 6 percent for the duration of the moratorium. Furthermore, noteholders would be foreclosed from enforcing any judgments or liens instituted on account of these short-term City notes.

III. The Constitutional Challenges

A. Wein v. City of New York

Leon Wein, in his status as a New York State taxpayer, brought suit in the State court challenging the SRC, claiming that it lacked conventional corporate purpose in that it had "no visible means of financial support except for what it [could] derive from the city, State or Federal governments." In Wein v. City of New York (Wein I), he contended that the SRC was a "mere 'conduit'" for City monies, implying that the corporation constituted a thinly-veiled attempt to circumvent the faith and credit provision of the State constitution. This section provides that "[n]o indebtedness shall be contracted by . . . city . . . unless such . . . city . . . shall have pledged its faith and credit for the payment of the principal thereon." The court rejected this argument, concluding that "such labeling does not necessarily violate the various aspects of the Constitution . . . all of which . . . rest on the assertion that the city has become indebted or obligated." Inasmuch as the statute did not compel the

63. Exchange Offer at 1.
64. Id. chs. 874, 875, § 5(B).
65. Id. ch. 874, § 3. The suspension of enforcement provision was to last the duration of the moratorium, which was a three-year period, to end November 14, 1978. Id. § 2(3).
68. Id. at 617, 331 N.E.2d at 518, 370 N.Y.S.2d at 555.
69. Id. at 615, 331 N.E.2d at 517, 370 N.Y.S.2d at 554.
70. N.Y. Const. art. 8, § 2, para. 2. This provision was challenged again in Flushing Nat'l Bank v. Municipal Assistance Corp., 40 N.Y.2d 731, 358 N.E.2d 848, 390 N.Y.S.2d 22 (1976). See section III-D infra.
City to pay monies into the SRC capital reserve fund and did not obligate the City on the SRC's bonds, the faith and credit provision could not apply.\textsuperscript{71}

In refuting the argument that the City in fact had loaned its credit to a public corporation, the court in \textit{Wein I} cited as controlling\textsuperscript{72} its decision in \textit{Comereski v. City of Elmira}.\textsuperscript{73} In that case, the State Legislature organized a parking authority in the form of a public benefit corporation, whose purpose was to operate parking facilities.\textsuperscript{74} However, the city of Elmira retained control of parking meters in the facilities. Partial profits from the meters were turned over to the authority to off-set any deficit and enable it to pay its bonds. Until the bonds were paid, the city was required to maintain the parking meters in such a manner as to insure the meters' profitability.\textsuperscript{75}

The court in \textit{Comereski} perceived a clear distinction between the city's giving or loaning \textit{money} and giving or loaning \textit{credit} to a public corporation for public purposes.\textsuperscript{76} Historically, "the Constitution permits the use of its credit by a local unit only for the purposes of that unit . . . ." (emphasis added)\textsuperscript{77} However, in neither judicial precedent nor statutory interpretation was there any sanction against a gift of money to a public corporation for a "proper" public purpose.\textsuperscript{78}

The \textit{Comereski} court concluded "that a city's non-liability on an authority's bonds and the same city's right or duty to assist the authority financially are part of the same conventional statutory

\textsuperscript{71} 36 N.Y.2d at 617, 331 N.E.2d at 518, 370 N.Y.S.2d at 555.
\textsuperscript{72} Id. at 618, 331 N.E.2d at 518, 370 N.Y.S.2d at 556.
\textsuperscript{73} 308 N.Y. 248, 125 N.E.2d 241 (1955).
\textsuperscript{74} Id. at 250, 125 N.E.2d at 242.
\textsuperscript{75} Id. at 251, 125 N.E.2d at 242.
\textsuperscript{76} Id. at 252, 125 N.E.2d at 242-43.
\textsuperscript{78} Id. The Rye town supervisor refused to borrow the money needed by the school district when the funds actually available fell short of the amount appropriated to its use. The New York Court of Appeals held that "[p]ublic monies should be used for public purposes." \textit{Id.}

Board of Educ. v. Van Zandt fashioned a test to discern "city purposes": first, look to legislative intent to find that the purpose of the statute was to insure that public monies would not be used for private purposes, and second, apply the plain meaning rule. 119 Misc. 124, 126 (1922). For a discussion of the "public purpose doctrine," see Note, 45 Fordham L. Rev. 860, 879-82 (1977).
pattern. We should not strain ourselves to find illegality in such programs."

Based on the foregoing reasoning, the court in Wein I held that disbursing a portion of the City's State-aid money to the SRC constituted a statutorily permissible gift "for all purposes." Thus, if the money given to the SRC were a gift, it could not be a debt obligation. Both the specific disclaimer in the SRC Act and simple logic demanded that conclusion.

Judge Matthew Jasen, dissenting, dismissed the technical syllogisms. He reasoned that the SRC's de facto dependence on a continuing flow of government funds to insure its existence belied the voluntariness of the City's involvement. He further agreed with plaintiff's premise that the City, straining its debt ceiling to the constitutional limit, created the SRC to borrow indirectly that which it could not otherwise legally obtain. This circumvention, Judge Jasen concluded, "violate[d] the spirit and tenor" of the constitution.

B. Sgaglione v. Levitt

In September, 1975, the court of appeals in Sgaglione v. Levitt declared unconstitutional that provision in the Financial Emergency Act which compelled the State comptroller, a trustee of the State retirement systems, to use 125 million dollars of the systems' funds to purchase MAC bonds at face value. This enactment was designed to furnish committed investment money to the City in the climate of weakening investor confidence. Chief Judge Charles Breitel, writing for the majority, held the provision to be in violation of the State nonimpairment of pension benefits clause which provides: "After July first, nineteen hundred forty, membership in any

79. 308 N.Y. at 254, 125 N.E.2d at 244.
81. Id. at 621, 331 N.E.2d at 520-21, 370 N.Y.S.2d at 559.
82. Id. at 622, 331 N.E.2d at 521, 370 N.Y.S.2d at 560.
83. Id. at 623, 331 N.E.2d at 522, 370 N.Y.S.2d at 561.
85. Id. at 511, 337 N.E.2d at 594, 375 N.Y.S.2d at 82. See Financial Emergency Act, § 7, creating the Investment of Funds by Pension and Retirements Systems for Public Employees Act. N.Y. RETIRE. & SOC. SEC. LAW § 179 (McKinney Supp. 1976) declares MAC securities to be legal investments for the funds, and further indemnifies all fund investors, trustees, and fiduciaries from liability arising out of such investments.
pension or retirement system of the state or of a civil division thereof shall be a contractual relationship, the benefits of which shall not be diminished or impaired. 87 Judge Breitel found that implicit within the protection offered the retirement benefits is a corresponding protection of the funds which guarantee these benefits. By depriving the trustee of his investment discretion, the FEA section endangered the funds and ultimately impaired the benefits of the retirement contract as a whole. 88

The court in Sgaglione strained to bring its decision within the ambit of the "pecuniary benefits" test, heretofore utilized in determining what constituted a benefit under a State retirement contract. 89 This test appears to require a showing of harm by direct dollar amount as opposed to injury to intangible interests, in order to establish the impairment of a benefit.

The test was developed in a series of cases, notably in Birnbaum v. New York State Teachers Retirement System, 90 wherein the court of appeals declared unconstitutional the adoption of an actuarial table which reduced a member's annuity benefits by nearly 5 percent. The court found that these reduced rates would diminish and impair the amount of the system's benefits. 91 Brown v. New York State Teachers Retirement System 92 reiterated this standard in holding that statutory dilution of teachers' voting strength on the Retirement Board was permissible and did not impair the retirement contract. Inasmuch as the pecuniary benefits were already constitutionally safeguarded, the court concluded that they would

87. N.Y. Const. art. 5, § 7.
88. 37 N.Y.2d at 512, 337 N.E.2d at 595, 375 N.Y.S.2d at 83. Cf. Subway-Surface Supervisors Ass'n v. New York City Transit Auth., 85 Misc. 2d 695 (1976), where a wage freeze was upheld by the New York Supreme Court in the face of an article 5, section 7 State constitutional challenge. The court recognized that the impairments clause could not be applied rigidly. "It has been regarded as a proscription qualified by the power of the States to maintain order and to safeguard the public welfare." Id. at 698.
91. Id. at 9, 152 N.E.2d at 245, 176 N.Y.S.2d at 990.
be unaffected by Board representation.\footnote{93}{Id. at 780, 226 N.E.2d at 319, 279 N.Y.S.2d at 533.}

The benefits in \textit{Sgaglione} were statutorily protected\footnote{94}{N.Y. RETIRE. \& SOC. SEC. L\textsc{aw} ¶§ 16, 316 (McKinney 1971). Section 16 applies to State employees' retirement funds and mandates that the comptroller file an estimate of the anticipated amounts required by the system for the previous year. "Such amounts shall be sufficient to provide for payment in full . . . of all obligations of the state to the retirement system." Id. at ¶ 16(a). Section 316 applies to policemen and firemen retirement funds and similarly guarantees the appropriation of sufficient amounts every year.} and incapable of impairment under the nonimpairment clause. However, the court found that the comptroller's discretion was an additional benefit entitled to constitutional protection. Central to \textit{Sgaglione} and \textit{Brown} was the issue of diminution of control over the pension funds. Yet opposite results were reached in these cases, perhaps suggesting that the \textit{Sgaglione} court, in spite of its disclaimers, was more concerned with the result than the route which it mapped to achieve this result. The majority took pains to emphasize the traditional role of the court. It concluded with a statement, the substance of which has echoed throughout the fiscal crisis decisions:

\begin{quote}
Indeed, it should be said that [neutrality] is the primary role of the courts in the American system in reviewing the constitutional validity of executive and legislative acts even if they bear the guise, and the courts are convinced that the guise reflects a reality, of necessity, distress and emergency. The courts did not make the Constitution; the courts may not unmake the Constitution.\footnote{5}{Id. at 780, 226 N.E.2d at 319, 279 N.Y.S.2d at 533.}
\end{quote}

Judge Cooke, dissenting in \textit{Sgaglione}, relied upon the strong presumption of constitutionality generally afforded legislative acts, an approach which frequently punctuates his decisions. He maintained that only pecuniary benefits were entitled to constitutional protection.\footnote{96}{Id. at 516, 337 N.E.2d at 597, 375 N.Y.S.2d at 86-87.} Inasmuch as there was no indication that investment in MAC bonds would deplete the systems' assets, Judge Cooke asserted that a finding of unconstitutionality was impermissible.\footnote{97}{Id. at 517, 337 N.E.2d at 598, 375 N.Y.S.2d at 87-88.} The dissent suggested that the majority was proceeding on a presumption of unsoundness of the questioned investment, rather than looking to prior interpretative case law, which would support the dissenting opinion.\footnote{98}{Id.}
C. Wein v. State of New York

Six months after Sagglione the court of appeals in Wein v. State of New York (Wein II) upheld sections 22 and 23 of the Emergency Act which required the appropriation of millions in State monies to both the City and MAC. These funds were obtained by short-term State borrowing in the form of tax and revenue anticipation notes. Plaintiff charged that these allotments constituted a gift or loan of the State's credit to a public corporation, in contravention of article VII, section 8, subdivision 1 of the State constitution, which provides:

The money of the state shall not be given or loaned to or in aid of any private corporation or association, or private undertaking; nor shall the credit of the state be given or loaned to or in aid of any individual, or public or private corporation or association, or private undertaking . . . .

Although the court found no constitutional violation, it nevertheless admonished that "the State in avoiding violation has been driven to the brink of valid practice." Both plaintiff Wein and the majority perceived the issue to be the giving or loaning of credit by the State. In its analysis, the court divided the appropriating process into two parts and passed on the constitutionality of each separately. First, the court noted that MAC received the State monies in cash and that it is constitutionally permissible for the State to give or loan money to aid a munici-

100. Id. at 140, 347 N.E.2d at 587, 383 N.Y.S.2d at 226.
101. N.Y. Const. art. 7, § 8, subd. 1.
102. 39 N.Y.2d at 142, 347 N.E.2d at 588, 383 N.Y.S.2d at 227. Plaintiff argued that the State was attempting "to do indirectly what it may not do directly," that is, that in effect the State was giving away money to the City and to MAC. Id. The Wein II court did warn against this as a general proposition by referring to People ex rel Burby v. Howland, 155 N.Y. 270, 280-81 (1898), wherein the court stated:

When the main purpose of a statute . . . is to evade the Constitution by effecting indirectly that which cannot be done directly, the act is to that extent void, because it violates the spirit of the fundamental law. Otherwise the Constitution would furnish frail protection to the citizen, for it would be at the mercy of ingenious efforts to circumvent its object and to defeat its commands.

39 N.Y.2d at 145, 347 N.E.2d at 590, 383 N.Y.S.2d at 229. However, it found no circumvention in the instant case.
103. For a summary of legislative motivation to prohibit the State from giving or loaning its credit to a public or private entity, see Wein v. State of New York, 39 N.Y.2d at 147-48, 347 N.E.2d at 591-92, 383 N.Y.S.2d at 230-31.
pal corporation. 104
Second, the State obtained the funds from constitutionally permissible short-term borrowing. 105 The purpose of the short-term loan was to furnish immediate cash as a temporary replacement for revenues already earmarked but not yet received. Moreover, the borrowing used to fund this assistance is proper when, as here, it is matched by taxes or revenues incoming within the following year, assuring a subsequent balance of the liability with the asset. 106 Thus, if the State could not anticipate adequate revenues and taxes to compensate for the obligations, the debt would be constitutionally impermissible. 107

The court cautioned against “rolling over,” i.e., issuing new bonds to meet the deficit of the prior year caused by a previous bond issue. “[R]ollosers,” Chief Judge Breitel wrote, are “not consonant with constitutional limitations or their spirit.” 108

In the dissent, Judge Jasen took issue with appropriations being made in extraordinary session long after the budget was adopted. 109 He agreed that the constitution permits the State to give money to MAC. However, he noted that it first had to have the money to give.110 Indeed, appropriations are distributed from a finite amount of money which the State anticipates as income each year. It is thus

104. Id. at 145, 347 N.E.2d at 590, 383 N.Y.S.2d at 230.
105. Id. at 140, 347 N.E.2d at 587, 383 N.Y.S.2d at 226. See N.Y. Const. art. 7, § 9.
106. Plaintiff, writing a commentary on the New York municipal bond, had harsh words for this borrowing scheme:

The Constitution intended a minor exception to enable government to deal with cash flow problems without the formalities required for permanent debt.

However, the short-term exception became a loophole of disastrous proportions. . . . The whole New York fiscal disaster was premised upon short-term borrowing.

108. Id. at 149, 347 N.E.2d at 593, 383 N.Y.S.2d at 232. The court observed, however, that the purchase of these RANs authorized by the Emergency Act, although not themselves in violation of the State constitution, could become violative if such temporary legislation were used as a launching point for subsequent “rollosers.” Id. at 151, 347 N.E.2d at 594, 383 N.Y.S.2d at 233.
109. Id. at 156-57, 347 N.E.2d at 597, 383 N.Y.S.2d at 236.
110. Id. at 154, 347 N.E.2d at 596, 383 N.Y.S.2d at 235.
anomalous to appropriate money from outside the budget before there is a source. At that point, the State has only its credit to give.

Judge Jasen characterized the funding as an exchange rather than a money transaction. In the absence of other purchasers, the State accepted MAC bonds and City notes. In anticipation of a yield on these securities, the State issued its own revenue anticipation notes, which it was able to market through the persuasiveness of its still-intact credit. Proceeds from the sale of the revenue anticipation notes constituted the allotments in question.\textsuperscript{111} This, Judge Jasen concluded, was clearly a giving or loaning of State credit, an implied guarantee to the State’s own noteholders that City and MAC securities were solid enough to back their investment.\textsuperscript{112}

The majority concluded, however, that the State did not abuse its borrowing power “because the State’s temporary debt as a part of the device must be exonerated in the ensuing fiscal year. The legalities of the device are present so long as the fiscal prospects are tenable.”\textsuperscript{113}

Despite the admonition that this borrowing is barely constitutional, the State’s scheme may be duplicated. That is, the State may appropriate outside the parameters of the adopted budget, so long as the borrowing to fund it will be repaid within one year, is for the same amount as the appropriation, and in no way interferes with the existing State budget. The danger in such a device lies in its potential for abuse, as suggested in \textit{Wein II}. Nonetheless, this decision has retained short-term borrowing as a viable means of obtaining funds for unanticipated State debt.

\textbf{D. Flushing National Bank v. Municipal Assistance Corporation}

By June, 1976, MAC had made two offers to the general public\textsuperscript{114} to exchange its 8 percent bonds due July 1, 1986,\textsuperscript{115} and July 1, 1991,\textsuperscript{116} for City notes. Flushing National Bank, a City noteholder,

\textsuperscript{111} Id. at 154-55, 347 N.E.2d at 596, 383 N.Y.S.2d at 235.
\textsuperscript{112} Id. at 155, 347 N.E.2d at 596, 383 N.Y.S.2d at 235.
\textsuperscript{113} Id. at 151, 347 N.E.2d at 594, 383 N.Y.S.2d at 233.
\textsuperscript{114} Of the 1.6 million dollars worth of RANs and BANs subject to the Moratorium, approximately 600 million dollars worth were exchanged through both offers. Weekly Bond Buyer, Nov. 29, 1976, at 5, col. 1. \textit{See generally} section II-D \textit{supra}.
\textsuperscript{115} \textit{Exchange Offer}, Nov. 26, 1975.
refused the exchange offers and brought suit in New York State Supreme Court challenging the constitutionality of the Moratorium Act under both the United States and New York State Constitutions.\textsuperscript{117} More specifically, Flushing charged that the Moratorium Act violated, \textit{inter alia}, section 2 of article 8 of the New York State Constitution by relieving the City of its pledge of faith and credit to back the notes.\textsuperscript{118} Flushing further challenged the act on the ground that it impaired the obligation of the noteholders' contract with the City, in contravention of the federal constitutional provision which states that "[n]o State shall . . . pass any . . . Law impairing the Obligation of Contracts . . . ."\textsuperscript{119}

The trial court upheld the constitutionality of the Moratorium Act, emphasizing that the public interest involved outweighed a rigid application of the contracts clause.\textsuperscript{120} In addition, the court noted that the act was passed in an emergency and ultimately did not relieve the City of its faith and credit obligations.\textsuperscript{121}

The appellate division unanimously affirmed,\textsuperscript{122} reiterating that the debts were to be paid, albeit on a revised schedule.\textsuperscript{123} In upholding the extension of the repayment period, the court emphasized the State's right to exercise its inherent police powers which repose in every contract or obligation. It found that these powers were invoked properly in view of the State Legislature's findings that New York City was plummeting rapidly toward financial ruin.\textsuperscript{124} Relying heavily on the United States Supreme Court opinion in \textit{Faitoute Iron \& Steel Co. v. Asbury Park}, the appellate division noted:

\begin{itemize}
  \item 118. This section forbids a city from contracting any indebtedness unless it has pledged its faith and credit on payment of the debt. Article 8, § 2 was first challenged in the fiscal crisis decisions in Wein v. City of New York, 36 N.Y.2d 610, 331 N.E.2d 514, 370 N.Y.S.2d 550 (1975), discussed in section III-A supra.
  \item 119. U.S. CONST. art. I, § 10, cl. 1.
  \item 120. 84 Misc. 2d at 980, 379 N.Y.S.2d at 982.
  \item 121. \textit{Id.} at 982, 379 N.Y.S.2d at 985.
  \item 122. 52 App. Div. 2d 84, 382 N.Y.S.2d 764 (1976).
  \item 123. \textit{Id.} at 87, 382 N.Y.S.2d at 767.
  \item 124. \textit{Id.} at 88, 382 N.Y.S.2d at 767.
\end{itemize}
Impairment of an obligation means refusal to pay an honest debt; it does not mean contriving ways and means for paying it. The necessity compelled by unexpected financial conditions to modify an original arrangement for discharging a city's debt is implied in every such obligation for the very reason that thereby the obligation is discharged, not impaired.\textsuperscript{125}

The decision summarily dismissed the challenges based on the faith and credit clause of the State Constitution whereby the City may not contract a debt without pledging its faith and credit thereon. The court merely noted that the mandate of this section had not been violated by the emergency moratorium legislation.\textsuperscript{126}

In a decision by Chief Judge Charles Breitel, the New York Court of Appeals reversed the appellate division's affirmance of the special term's decision,\textsuperscript{127} noting that "[t]he State Constitution prohibits the city from contracting any indebtedness unless it pledges its 'faith and credit' for the payment of the . . . indebtedness . . . ," and that by foreclosing the short-term noteholders from legal recourse for at least the moratorium period, the full faith and credit pledge was rendered meaningless. Having found a violation of the State constitution the court saw no need to proceed to the federal constitutional questions presented.\textsuperscript{128}

Initially, the court looked to constitutional history in its search for the meaning of faith and credit.\textsuperscript{129} As stated by the New York State Constitutional Convention of 1938, the purpose of adding the faith and credit section was to protect "the soundness of local borrowing policies and to preserve and strengthen local credit."\textsuperscript{130} Attempts to eliminate the pledge in 1967 met with no success.\textsuperscript{131}

\begin{itemize}
  \item \textsuperscript{125} Id. at 89, 382 N.Y.S.2d at 768, quoting Faitoute Iron & Steel Co. v. Asbury Park, 316 U.S. 502, 511 (1942).
  \item \textsuperscript{126} Id. at 89, 382 N.Y.S.2d at 768.
  \item \textsuperscript{127} 40 N.Y.2d 731, 358 N.E.2d 847, 390 N.Y.S.2d 22 (1976).
  \item \textsuperscript{128} Id. at 732-33, 358 N.E.2d at 850, 390 N.Y.S.2d at 24. By not passing on the federal questions, the court effectively prevented any higher review of its decision.
  \item \textsuperscript{129} Id. at 734-35, 358 N.E.2d at 851, 390 N.Y.S.2d at 25. For an excellent discussion of the faith and credit provision as applied to municipal bonds, see Bond, Enhancing the Security Behind Municipal Obligations: Flushing and U.S. Trust Lead the Way, 6 Fordham Urban L.J. 1 (1977).
  \item \textsuperscript{130} Revised Record of the Constitutional Convention of the State of New York, 1076, Vol. II (April 5 to Aug. 26, 1938).
  \item \textsuperscript{131} State of New York Temporary State Commission on the Constitutional Convention — Local Finance, 126-27 (Jan. 12, 1967). The purpose stated for eliminating the faith and credit provision was to permit localities to issue revenue bonds (those issued in anticipa-
ever, in neither record did a discussion of the words' literal meaning appear. In the absence of such commentary, the Flushing court justified its assumption of the burden of interpretation.\textsuperscript{132}

The majority, taking a semantic approach, stated at the outset that the meaning of the phrase "faith and credit" was clearly understood and thus "must be read in accordance with [its] univocal meaning." It distinguished between the meanings of "faith" and "credit" in concluding that the phrase was not careless tautology:

[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.\textsuperscript{133}

Acknowledging that few courts have construed the meaning of faith and credit, the majority borrowed from two Florida State Supreme Court opinions and one California Court of Appeals opinion for its interpretation of the term. In \textit{State v. County of Citrus},\textsuperscript{134} the county commissioners approved a bond issue in order to repay holders on a then-outstanding issue.\textsuperscript{135} Unlike the original issue which pledged ad valorem taxes in repayment, the replacement bonds pledged both the ad valorem taxes and the faith and credit of the county.\textsuperscript{136} The Florida Supreme Court pointed out that the faith and credit pledge is both an acknowledgement of the debt by the obligor and an undertaking to use good faith to repay the liability promptly. Such a pledge expanded the county's obligations on the second bond issue to include a commitment to use other legal sources, in addition to the ad valorem taxes, to pay the bondholders.\textsuperscript{137} As a result the court concluded that Florida law required voter approval of the second bond issue.

Faced with another refunding bond issue similar to the one in

\begin{enumerate}
\item Id. at 125.
\item Id. at 735, 358 N.E.2d at 851, 390 N.Y.S.2d at 25.
\item Id. at 735, 358 N.E.2d at 851, 390 N.Y.S.2d at 25.
\item 116 Fla. 676, 157 So. 4 (1934).
\item Id. at 677, 157 So. at 5.
\item Id. at 679-80, 157 So. at 5-6.
\item Id. at 692-94, 157 So. at 10-11.
\end{enumerate}
Citrus County, the Florida Supreme Court, in *State v. City of Lakeland*,138 reaffirmed its *Citrus County* interpretation of faith and credit.139 Appellee Lakeland had pledged its full faith, credit and resources on both an original issue and the refunding bonds. However, the city sought to add a pledge of "surplus net revenues" to the refunding bonds to supplement the ad valorem taxes used to service the obligation.140 Lakeland argued that these surplus revenues were included implicitly in the faith, credit and resources pledge on the original bonds, and that the refunding issue was thus unchanged.141 The court concluded that a pledge of faith and credit "does not create a specific lien on any particular property," but is instead a general obligation. The new issue, by its surplus revenue addition, differed from the original agreement142 and required voter approval. The "faith and credit" pledge in *Lakeland* did not function as a catch-all to the issue by allowing the pledge of revenues outside the restrictions of the bond agreement. Instead, it served as the city's ultimate payment guarantee to the bondholders to call upon available resources in order to meet its debt service obligations.

The California Court of Appeals in *Sacramento Municipal Utility District v. Spink*143 relied upon the Lakeland decision for its inter-

138. 154 Fla. 137, 16 So. 2d 924 (1943).
139. Id. at 139, 16 So. 2d at 925. Citrus County interpreted faith and credit as constituting an undertaking by the city to be irrevocably obligated on its bonds.
140. Id. at 138, 16 So. 2d at 924-25.

In the first issue only the ad valorem taxes of the city were pledged. The city sought to pledge "surplus net revenues" in addition to the ad valorem taxes in the second refunding issue. These surplus revenues were to come from the operation of the city's water and light systems, and were to supplement the ad valorem taxes in the event these proved insufficient to meet obligations on the bonds.

141. Id. at 138-39, 16 So. 2d at 925. The gravamen of both *Citrus County* and *Lakeland* was that if the faith and credit pledge changed the nature of the refunding bonds and expanded their liabilities, they became new issues subject to new referenda votes. In neither case were the refunding issues submitted to a vote. Fla. Const. art. IX, § 6, as it existed prior to the 1968 revision, construed in *State v. City of Lakeland*, 154 Fla. 137, 139, 16 So. 2d 924, 925 (1943), and *State in County of Citrus*, 116 Fla. 676, 681-82, 157 So. 4, 6 (1934), provided in pertinent part that "[t]he Legislature . . . shall have power to issue bonds only after the same shall have been approved by a majority of the votes cast in an election in which a majority of the free holders who are qualified electors . . . shall participate . . .; but the provisions of this act shall not apply to the refunding of bonds issued exclusively for the purpose of refunding of the bonds of [electors'] Municipalities . . . ."

142. *State v. City of Lakeland*, 154 Fla. 139, 16 So. 2d 925.
interpretation of faith and credit as applied to municipal bonds. 44 Sacramento obtained voter approval for revenue bonds issued to finance the development of hydroelectric generating facilities. These bonds were backed by a full faith and credit pledge of the Municipal Utilities District. In addition, the bonds were secured by a lien against all gross revenues of the District. But the District already carried heavy indebtedness, including over ten million dollars in bonds issued in 1938. 45 Inasmuch as all revenues would be pledged to the second issue, the officials who refused to execute the issue argued that holders of 1938 bonds essentially would be deprived of repayment because of the diversion of funds by the second issue from the original issue. 46 The district court found that the obligations on the 1938 bonds, unlike those on the bonds in question, were not secured by any specific funds, and that the faith and credit pledge did not limit its import solely to specific revenues. Thus, the contract on the 1938 bonds was held not impaired, as their faith and credit pledge expressed only that the city would use good faith to produce the revenues when due. 47

In Cirtus County, Lakeland, and Sacramento, each successive court reinforced its interpretation by reliance upon its immediate predecessor. The court of appeals in Flushing brought these issues together and crystallized the doctrine of faith and credit. Since Flushing, a faith and credit pledge appears to require an entity to pay its obligations absolutely. Moreover, the pledge is not limited to specific revenues or property committed by the entity; but requires the governmental unit to seek beyond its specifically obligated funds on property for the means to pay debts secured by the pledge.

The Flushing majority drew the distinction among revenue obligations (those "limited to a pledge of revenues from a designated source"), moral obligations (those backed by only a moral commitment to pay), and the faith and credit or general obligations. 48 Chief Judge Breitel averred that the faith and credit or general obligations are those supported by an unconditional payment promise made by

144. Id. at 577, 303 P.2d at 54.
145. Id. at 570-71, 303 P.2d at 49-50.
146. Id. at 575, 303 P.2d at 52-53.
147. Id. at 575-76, 303 P.2d at 53.
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a government taxing entity and pledging its full faith and credit, but "not includ[ing] obligations not so supported that they are to be repaid only from specified sources [i.e. revenue obligations] . . . ." Applying this reasoning, the faith and credit obligation emerges as a most solemn constitutional pledge of a municipal entity's fiscal wherewithal, more encompassing than either the revenue or moral obligations.

The majority did not imply that if the notes were not paid out of designated funds, the entire revenues of the City would lie exposed to noteholders. It pointed to the protection of section 2 of article 8 of the State constitution providing that any tax or revenue anticipation obligations not retired within five years must be paid out of special appropriations for that purpose. If the municipality fails to do so, it must allocate a sufficient sum for repayment from the first revenues it thereafter receives. This provision, the court concluded, reinforces the premise that the State constitution compels payment on City indebtedness by demonstrating the existence of a specific remedy on outstanding obligations for the defaulting municipality.

The majority, therefore, declared that the faith and credit pledge requires that the indebtedness in question be paid when due, "even if tax limits be exceeded." By extending the repayment period on


150. N.Y. Const. art. 8 § 2, para. 4. This section provides that:

[p]rovision shall be made annually by appropriation by every . . . city . . . for the payment of interest on all indebtedness and for the amounts required for . . . (b) the redemption of certificates or other evidence of indebtedness . . . contracted to be paid in such year out of the tax levy or other revenues applicable to a reduction thereof, and (c) the redemption of certificates or other evidence of indebtedness issued in anticipation of the collection of taxes or other revenues, or renewals thereof, which are not retired within five years after their date of original issue. If at any time the respective appropriating authorities shall fail to make such appropriations, a sufficient sum shall be set apart from the first revenues thereafter received and shall be applied to such purposes.


152. 40 N.Y.2d at 737, 358 N.E.2d at 852, 390 N.Y.S.2d at 27. New York City is prohibited by the State constitution from contracting "indebtedness for any purpose or in any manner which, including existing indebtedness, shall exceed" 10 percent of the full value of its real estate. N.Y. Const. art. 8, § 4(c). The Legislature may not restrict the City's power to levy taxes on real estate up to the allowable percentage, if the proceeds are to pay for the principal
City notes three years beyond their due date, the Moratorium Act sanctioned the City’s disregard of the pledge. If the Act were left standing, the court continued, the moratorium period could be extended indefinitely “until all the note holders [would] take MAC bonds ‘voluntarily’ in exchange for their notes.”\textsuperscript{153} The court found no support for such a proposition.

Judge Cooke, the sole dissenter in Flushing, argued that the faith and credit pledge was merely one element of the contract, and a reneging on that pledge by the City would give rise to a breach of contract action.\textsuperscript{154} Whereas the majority viewed the faith and credit issue in a vacuum, Judge Cooke integrated it with an impairment of contracts concept. He further reasoned that the strong presumption of constitutionality of a state statute had not been given the proper weight.\textsuperscript{155}

Judge Cooke ostensibly read the Citrus County, Lakeland and Sacramento cases more broadly than did Chief Judge Breitel. He referred to essentially the same passage from Lakeland as did the majority:\textsuperscript{156}

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[t]hat the issuing government agrees to be generally obligated to pay the indebtedness out of all the government’s revenues, rather than restrictively obligated only from specific revenues; [the faith and credit pledge] expresses an undertaking by the government to be irrevocably obligated in good faith to use such of its resources and taxing power as may be authorized or required by law for the full and prompt payment of the obligation according to its terms.\textsuperscript{157}
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However, the dissent focused on the term “undertaking” as implying a good faith attempt to pay, rather than a compelled, absolute

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\textsuperscript{153} Id. at 738, 358 N.E.2d at 853, 390 N.Y.S.2d at 27-28.
\textsuperscript{154} Id. at 747, 358 N.E.2d at 859, 390 N.Y.S.2d at 33.
\textsuperscript{155} Id. at 744, 358 N.E.2d at 859, 390 N.Y.S.2d at 31.
\textsuperscript{156} See 40 N.Y.2d at 735, 358 N.E.2d at 851, 390 N.Y.S.2d at 25, citing State v. City of Lakeland, 154 Fla. 137, 139, 16 So. 2d 924, 925 (1944).
\textsuperscript{157} Id. at 746, 358 N.E.2d at 858, 390 N.Y.S.2d at 32.
payment. He asserted that "[a] faith and credit pledge simply means that the issuing government agrees to be generally obligated . . . ."

The dissent maintained that any failure of the municipality to provide for payment on the obligations gives rise to an action for breach of contract. Such an approach requires, therefore, that the surrounding panoply of contractual terms be considered before a decision on the breach be rendered. Whereas the majority abstracted the faith and credit element as being outside of, and naturally higher than, the contract, the dissent perceived faith and credit as but one term of the contract to be weighed equally with all others. The contravening consideration in this case, according to Judge Cooke, was the legislative finding of a "grave public emergency" in the City. He concluded that the faith and credit "pledge can be honored only if the viability and resources of the city are preserved and that the continuation of essential services is vital . . . ."

Judge Cooke argued that there exists in the police power a constitutionally allowable release from the rigid enforcement of municipal debt contracts. This police power is inherent in every contract; it is the right reserved to the State to maintain the health and welfare of its citizens "notwithstanding interference with contracts." He maintained therefore that "the insertion of the faith and credit pledge into the contract could not possibly, nor did it purport to, immunize or insulate the entire contract, or even a part of it, from a valid exercise of the police power by the State." Although the police power must be wielded constitutionally, "there is no proscription against or limitation of the police power in respect to city indebtednesses which embrace a pledge of faith or credit — in section 2 of article VIII . . . ."

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158. Id.

159. Id. at 747, 358 N.E.2d at 858, 390 N.Y.S.2d at 33.

160. Id. at 754, 358 N.E.2d at 863, 390 N.Y.S.2d at 38. But see Sturge v. Crowninshield, 17 U.S. (4 Wheat.) 122 (1819) wherein Justice Marshall stated that a contract is an agreement to do or not to do something, which agreement is binding in the law. This agreement gives rise to the obligation on the contract. Therefore, any law discharging the agreement must impair it. Id. at 197. See also Emergency Moratorium Act, 1975 N.Y. Laws, ch. 874, sec. 1.

161. Id. at 749, 358 N.E.2d at 860, 390 N.Y.S.2d at 35.

162. Id. at 748, 358 N.E.2d at 860, 390 N.Y.S.2d at 34.

163. Id. at 754, 358 N.E.2d at 863, 390 N.Y.S.2d at 38.
The dissent then discussed the effects of the contract clause. *Home Building & Loan Association v. Blaisdell*¹⁶⁴ is the key case upon which the dissent based this argument. In that case, a Minnesota moratorium law allowed the postponement of sales of foreclosed property and the extension of redemption periods during an economic emergency.¹⁶⁵ Faced with a challenge that the law impaired contractual obligations, the United States Supreme Court upheld the law, declaring that the integrity of the mortgage indebtedness remained untouched. During the moratorium, the Court continued, the mortgagee still had the right to title and could still obtain a deficiency judgment against the mortgagor. However, in light of the financial exigencies of the 1930s, the state could use its "protective powers" and justify interference with contracts.¹⁶⁶ "While emergency does not create power, emergency may furnish occasion for the exercise of power."¹⁶⁷ The Supreme Court concluded that the reservation of state power appropriate to such extraordinary conditions may be deemed to be as much a part of all contracts, as is the reservation of state power to protect the public interest . . . ."¹⁶⁸ Thus *Blaisdell* set forth a test to reconcile the contract clause with the state's police power. It required a court first, to consider the reasonableness of the legislation,¹⁶⁹ and second, to balance individual rights against public welfare.¹⁷⁰

During the 1930s, New York passed a similar law which froze both mortgage foreclosures and any legal remedies to collect thereon, provided that taxes and interest were paid on the property.¹⁷¹ The

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¹⁶⁴. 290 U.S. 398 (1934).
¹⁶⁵. Id. at 416.
¹⁶⁶. Id. at 425.
¹⁶⁷. Id. at 426.
¹⁶⁸. Id. at 439.
¹⁷⁰. 290 U.S. at 442.
¹⁷¹. Act of May 3, 1933, ch. 745, 1933 N.Y. LAWS. In its statement of findings and policy, the State Legislature declared the "existence of a public emergency affecting the health, safety, and comfort of the people requiring the provisions of this act, . . ." In view of the substantial number of defaults on mortgages, and an awareness that immediate liquidation of such mortgages would "demoralize" the real estate market, the Legislature declared it "essential for the public interest to provide a procedure under which such . . . mortgages . . . may be liquidated in an orderly manner and under which the assets of the guaranty corporations may be administered and conserved equally and ratably in the interests of holders of mortgage investments." Id. at Section 1.
New York Court of Appeals upheld this legislation in the face of challenges by security holders, first in *Klinke v. Samuels*¹⁷² "to prevent . . . extensive evils and suffering," and similarly in *Maguire & Co. v. Lent & Lent, Inc.*¹⁷³ In 1945, this law was tested in the United States Supreme Court in *East New York Savings Bank v. Hahn*¹⁷⁴ and emerged unscathed. The bank had attempted to foreclose on a mortgage, the principal on which had become due in 1924. However, under the New York Moratorium Law foreclosure was prohibited on mortgages executed prior to July 1, 1932. This provision was renewed annually.¹⁷⁵ In holding that the law did not violate the contracts clause of the United States Constitution, the Court pointed out that the State's power, when otherwise justified, is not "diminished" simply because a private contract is affected.¹⁷⁶ The Court applied the *Blaisdell* reasoning, giving highest regard to legislative discretion in determining the use of the police power, and concluding that "the police power . . . is an exercise of the sovereign right of the Government to protect the . . . general welfare of the people, and is paramount to any rights under contracts between individuals."¹⁷⁷ Thus, the police power is an element implied in every contract and must be treated as though explicitly written into it.¹⁷⁸

In none of the foregoing cases did the legislation in question deny the obligee's rights on the contract; rather, it merely postponed the remedy to enforce those rights. The *Flushing* majority stated that "denial of remedy is [equivalent to the] denial of the right,"¹⁷⁹

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¹⁷². 264 N.Y. 144, 190 N.E. 324 (1934). The court noted that limitation on the remedy is fixed:

There being no market for real estate of any kind, and the banks refusing to loan money on the best of real estate security, owners were caught . . . in a trap due to conditions over which no one had control and for which no relief was at hand. Value was in the property but the value could not be obtained nor anything like it. To prevent worse and more extensive evils and suffering, the Legislature had asked through these laws, for security holders to wait a reasonable time for universal economic conditions to improve, provided interest and taxes are paid.

*Id.* at 149, 190 N.E. at 326.

¹⁷³. 277 N.Y. 694, 14 N.E.2d 629 (1938).


¹⁷⁵. *Id.* at 230-31.

¹⁷⁶. *Id.* at 233.

¹⁷⁷. *Id.* at 232-33.

¹⁷⁸. *Id.*

citing *W.B. Worthen Co. v. Kavanaugh*180 In *Worthen* the Arkansas legislature extended from sixty-five days to six and one-half years the minimum time before which property securing Municipal Improvement District bonds could effectively be seized. Additionally, if the creditor/mortgagor were to take possession, the law required a two and one-half year postponement of the debt with no requirement that the debtor show inability to pay.181 Moreover, the penalty for nonpayment of interest was reduced, and the statute was not limited to a period of economic emergency.182 The *Worthen* Court noted that while in *Blaisdell* the mortgagor nonetheless was obliged to pay rent on the property possessed, in the case before it the creditor’s right was diminished to virtually nothing. The Court thus concluded that there was no reasonable relation between the terms of the statute and its stated objective.183

Ostensibly, City noteholders are in a situation more closely analogous to *Blaisdell* mortgagees than *Worthen* creditors, in that the noteholders continue to receive interest during the three year redemption moratorium. The purpose of the EMA “suspending” legislation arguably has as legitimate an end as did the moratorium in *Blaisdell*; i.e., the most fundamental and immediate necessity of providing essential services to keep the life blood of New York flowing.

Furthermore, in *Faitoute Iron & Steel Co. v. Asbury Park*,184 the Supreme Court recognized that necessity may compel the revision of a city’s debt discharging arrangements. This modification was held not to constitute an impairment of contracts requiring a refusal to pay, but simply a means of ultimately discharging the obligation. Trying to find an alternative to municipal bankruptcy, the City of Asbury Park, a seashore town which had overexpanded, submitted its management to a state-created Municipal Finance Commission. The Commission formulated a plan of adjustment requiring that city bonds and coupons be transformed into new securities without holders’ consent.185 "The necessity compelled by unexpected finan-
cial conditions to modify an original arrangement for discharging a city's debt is implied in every such obligation . . . .”

The *Flushing* majority realized that its decision could have harsh ramifications for the already beleagured City and thus did not immediately impose the injunction and peremptory mandamus requested by Flushing National Bank. The opinion cautioned the City that the noteholders should be given their remedies in short order, indicating that the Legislature would be in session shortly after the decision was to be handed down. The City was given until the end of March, 1977, to repay the notes held by private citizens. Six months thereafter, the remainder was to be paid to institutional noteholders.

petition for recomposition. *Id.* at 504-05. The New York Moratorium Act, on the other hand, foreclosed the City noteholders from any judicial review of their right to payment.


187. 40 N.Y.2d at 741, 358 N.E.2d at 855, 390 N.Y.S.2d at 29. The court decided that:

[i]n order to minimize market and governmental disruptions which might ensue it would be injudicious at this time to allow the extraordinary remedies in the nature of

injunction and peremptory mandamus sought by plaintiff. Plaintiff and other noteholders of the city are entitled to some judicial relief free of throttling by the moratorium statute, but they are not entitled immediately to extraordinary or any particular judicial measures unnecessarily disruptive of the city's delicate financial and economic balance.

*Id.*

On January 14, 1977, almost two months after *Flushing* was decided, the court of appeals granted an extension on the remittitur to February 3, 1977. Flushing Nat'l Bank v. Municipal Assistance Corp., 40 N.Y.2d 1088, 360 N.E.2d 1075, 392 N.Y.S.2d 392 (1977). On February 8, 1977, the remittitur was signed, and the court of appeals rendered a memorandum decision proposing a timetable for the repayment of the City notes, essentially that within thirty days after the noteholder has submitted proof of present ownership or custodianship of the notes, full payment must be made on those notes. Flushing Nat'l Bank v. Municipal Assistance Corp., 40 N.Y.2d 1094, 360 N.E.2d 1106, 393 N.Y.S.2d 424 (1977).

Shortly thereafter, on February 28, 1977, the New York State Supreme Court Justice, James Gibson, appointed to administer the City noteholders' claims, refused to allow Flushing National Bank and all other noteholders similarly situated to receive interest during the moratorium period at the face value on the notes. The bank wanted to continue to receive the original interest beyond the maturity date, instead of the statutory 6 percent. The court said that forbearance on the higher interest rate is "vital to the rehabilitation of [the City's] critical fiscal situation." Flushing Nat'l Bank v. Municipal Assistance Corp., 88 Misc. 2d 1047, 1049, 391 N.Y.S.2d 969, 970 (1977).

For a concise explication of the rights of the noteholders after the moratorium, see *EXCHANGE OFFER TO HOLDERS OF CERTAIN SHORT-TERM NOTES OF THE CITY OF NEW YORK OFFICIAL STATEMENT*, March 22, 1977, at 10.
The immediate effect of the *Flushing* decision is to require payment to those who were most poignantly injured by the EMA — the small investors. But perhaps the opinion's more crucial significance is its impact on the bond industry. Had the court upheld the moratorium, there would always be lurking the risk that at any moment of financial difficulty, a bond's terms would be subject to alteration, prompted less by economic stringencies than political expediency.

E. *Wein v. Carey*

In *Wein v. Carey* (Wein III), Wein returned to challenge the State's good faith in maintaining a balanced budget during fiscal year 1976-77. This case harkened back to *Wein II*, where the plaintiff challenged the State's issuance of revenue anticipation notes to finance $500 million dollars in appropriations to the City and MAC. Although the *Wein II* court held that such borrowing was constitutionally permissible, its finding was premised upon such borrowing not disrupting the balance of the budget.

In *Wein III*, the plaintiff claimed that in recent years the State had issued similar anticipation notes and had failed to repay them within the year of issue. Rather, the State had included this debt in the subsequent year's budget, thereby creating a deficit carry-

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188. It is arguable whether holders of MAC bonds who exchanged them for City notes are entitled to any redemption of those notes similar to that for MAC bonds. The *Flushing* opinion did not specifically deal with the issue.

Arthur Richenthal, counsel for Flushing National Bank, stated that bondholders made the decision to exchange their notes with full knowledge that they may be waiving their rights and knowing that the constitutionality of the moratorium had been challenged. "It appears at this stage that they voluntarily relinquished their rights," he stated. Wall St. J., Nov. 22, 1976, at 4, col. 3.

However, as early as the first exchange offer, the Official Statement contained the opinion that "if such holder exchanges his City Notes pursuant to this Exchange Offer he would probably be deemed to have relinquished any rights to judgment on or enforcement of the City Notes exchanged." *Exchange Offer* at 12.

189. One commentator, responding to the *Flushing* decision, said: "It seems already to have had a salutary effect on the municipal bond market. More important, it restores one's faith in the inevitability of rational and just solutions. It refutes those who insisted that black is white." Weekly Bond Buyer, Dec. 6, 1976, at 1, col. 1.


191. *Id.* at 500, *362 N.E.2d* at 589, *393 N.Y.S.2d* at 957.


193. *See* section III-C *supra*.
over year after year.\textsuperscript{194} Wein inferred from this apparent pattern of State financing that these deficits were constructively "planned deficits," in violation of the constitution's balanced budget mandate.\textsuperscript{195}

The court first rejected plaintiff's argument that the State should bear the burden of proving its good faith effort to maintain a balanced budget.\textsuperscript{196} The court further noted that in attempting to sustain his burden, plaintiff relied on a succession of budget deficits, which were wholly circumstantial evidence and therefore here inadequate proof.\textsuperscript{197}

In its decision, the court examined the feasibility of New York State proceeding to the end of its fiscal year with its budget still intact. It considered that reasonably unanticipated economic conditions could affect the budget, and concluded that "[t]here must, as a practical matter, in every year be either a deficit or a surplus." Moreover, the court hypothesized that even if the prior deficits were ill-disguised rollovers, they would not \textit{ipso facto} invalidate the current budget because the notes still had to be paid.\textsuperscript{198}

The decision in \textit{Wein III} suggests the futility of a taxpayer questioning the State's budget in a judicial forum for want of ability to obtain sufficient evidence. The court reminded potential challengers that if the State had the burden of justifying its good faith in fiscal matters, the State would be subject to defending frivolous suits at a cost which neither the State nor the taxpayer could afford.\textsuperscript{199}

\textbf{F. Quirk v. Municipal Assistance Corporation}

William Quirk and others who did not exchange their long-term City bonds for short-term MAC notes,\textsuperscript{200} charged that their rights as bondholders were impaired under both the United States\textsuperscript{201} and New

\textsuperscript{194} 41 N.Y.2d at 502-03, 362 N.E.2d at 590, 393 N.Y.S.2d at 958.
\textsuperscript{195} \textit{Id.} at 503, 362 N.E.2d at 590-91, 393 N.Y.S.2d at 958-59. The New York State constitution requires that the State budget be balanced when approved by the Legislature for each new fiscal year. A planned deficit is impermissible; that is, no new budget may be unbalanced at its inception. N.Y. CONST. art. 7, § 2.
\textsuperscript{196} 41 N.Y.2d at 503, 362 N.E.2d at 590-91, 393 N.Y.S.2d at 958-59.
\textsuperscript{197} \textit{Id.} at 504-05, 362 N.E.2d at 591-92, 393 N.Y.S.2d at 959-60.
\textsuperscript{198} \textit{Id.} at 504, 362 N.E.2d at 591, 393 N.Y.S.2d at 959.
\textsuperscript{199} \textit{Id.} at 504-05, 362 N.E.2d at 591-92, 393 N.Y.S.2d at 960.
\textsuperscript{201} Plaintiffs allege that the diversion of the proceeds of certain City taxes from the City
York State constitutions. They alleged that the State, in diverting the proceeds of the stock transfer and City sales taxes from the City to MAC, reduced the revenues available to pay City bondholders and thereby diminished their fiscal position while enhancing that of MAC noteholders.

The court of appeals dismissed these contentions by pointing out that there was no provision in either the State constitution or elsewhere committing these specific taxes to payment of the bonds. Without the commitment, there is no obligation to be impaired under the federal Constitution.

The Quirk decision in no way removed that last vestige of protection which the bondholders still possessed. The court assured plaintiffs that the State constitution provides for the appropriation of funds to pay the bonds “from the first revenues . . . received” by the City. Moreover, the faith and credit pledge functions as additional insurance guaranteeing that the bonds will be backed.

The court reminded the bondholders that their right to be paid does not embrace a right to designate which revenues the City will direct toward payment of the obligation. The court is apparently unwilling at this time to impose any further strictures on the City in its debt service. After the Flushing decision, wherein the court articulated the expansive parameters of the faith and credit obligation, the court seems reluctant to impose its judicial sanctions on the manner in which the City activates the court’s prior mandate.

G. Wein v. Levitt

In a “hold-harmless” provision similar in form and effect to those to MAC impaired their contracts under the United States Constitution, article I, § 10, presumably by diminishing the source of funds available to pay their notes.

See note 188 supra, as to the rights of those who accepted the MAC exchange offers.

202. N.Y. Const. art. 7, § 2, provides for a “first lien” on revenues to pay bonds on which an insufficient amount was originally set aside.

203. 41 N.Y.2d at 646, 363 N.E.2d at 550, 394 N.Y.S.2d at 843.

204. Id.

205. Id. at 647, 363 N.E.2d at 550-51, 394 N.Y.S.2d at 843.

206. Id. The effect of the decision on the bond industry is best reflected in the performance of MAC bonds in the market. “Trading in MACs picked up after the news [of the decision] hit the Street with some bonds gaining more than one point.” Daily Bond Buyer, April 27, 1977, at 1, cols. 2-3. Then-mayor Abraham Beame was quoted as saying that Quirk “removes any lingering shadow of uncertainty concerning this necessary financing mechanism.” Id. at 2, col. 2.
included in the MAC statute, the Legislature indemnified trustees of the State Insurance Fund (the Fund) from liability on investments in certain State public benefit corporations. Just as the Legislature required the public employees’ pension and retirement systems to invest in MAC securities, it mandated a similar investment for the Fund. The Legislature perceived this mandate to be a practicable, viable solution to the need for infusion of capital into MAC. Accordingly, the Legislature further required the Fund to purchase securities from investment-poor public benefit corporations (“buildout authorities”). While the indemnification for MAC investments was to be financed by the Fund itself, indemnification for authorities’ investments was to be paid directly by the State. Plaintiff Wein argued that via the hold-harmless clause, the State in effect contracted a debt in contravention of article 7, section 11 of the State constitution providing that “no debt shall be hereafter contracted by or in behalf of the state, unless such debt be authorized by law, for some single work or purpose, to be distinctly specified therein.” Such law must be submitted to a referendum vote.

In its majority opinion, the court classified State spending in two ways: first, that which is needed to maintain the day-to-day operation of the government; and second, that which is “created by long-term borrowing and bond obligations.” The court reasoned that the indemnification in issue falls into the former category because it is simply a cost of doing business and therefore found no

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208. See section III-B supra, for a discussion of Sgagliione v. Levitt, 37 N.Y.2d 507, 337 N.E.2d 592, 375 N.Y.S.2d 79 (1975), which declared unconstitutional the New York State Financial Emergency Act sections 22 and 23, which required the State Comptroller to invest a specified amount of pension funds in MAC bonds.


212. Id. at 302-03, 366 N.E.2d at 848, 397 N.Y.S.2d at 760.

213. Id. at 304, 366 N.E.2d at 849, 397 N.Y.S.2d at 761.

214. Id.
For procedural reasons, the court did not pass upon plaintiff's claim that the provision constituted a prohibited loan of the State's credit to a public corporation, but it did discuss the issue in dictum. This constitutional section is the same one reviewed in *Wein II*. Unlike the financing scheme in the earlier case, where plaintiff argued that the loan of credit ran to a public corporation, the indemnification provision in *Wein III* creates no obligation to the authority itself. Instead, the State is obligated to only the trustees of the investor Fund. The majority concluded that "[i]f the public corporations default, they will wallow in their own tragedy, without benefit of state credit vis-a-vis the indemnification provision."

Chief Judge Breitel, stepping away from his role as the voice of the majority, dissented. He opened his dissenting opinion with the pronouncement that "[t]his appeal involves another of the fiscal gimmicks used during the state and municipal financial stringency in 1975."

He argued that the indemnification provision was indeed a loan, albeit indirectly, of the State's credit to the authorities. Appreciating the economic effect of the provision, Chief Judge Breitel perceived the loan to occur in two steps: first, the State insured a flow of each into the authorities to buoy them above sinking level; second, the State, through indemnification of the officers of the investor, assumed their liability, which would be measured by the amount of losses sustained by the authority's default. Thus, if the authority fails, the State would ultimately have to pay.

However valid this hypothesis may be, the benefit of the State's credit, if indeed it is characterized as credit at all, still runs to the

215. *Id.* at 305, 366 N.E.2d at 849, 397 N.Y.S.2d at 761.
216. In his complaint, Wein raised only the New York Constitutional article 7, § 11 claim. Inasmuch as the case was before the court on a motion for summary judgment, the court may look only to the pleadings and affidavits for the issues to be decided. *Id.* at 305-06, 366 N.E.2d at 850, 397 N.Y.S.2d at 762.
217.  N.Y. Const. art. 7, § 8.
218. *See* text accompanying notes 99-113 *supra*.
220.  *Id.* at 307, 366 N.E.2d at 851, 397 N.Y.S.2d at 762.
221.  *Id*.
222.  *Id.* at 309, 366 N.E.2d at 852, 397 N.Y.S.2d at 764.
223.  *Id*.
224.  *Id.* at 309-10, 366 N.E.2d at 852, 397 N.Y.S.2d at 764.
Fund and not the authority. If the authority defaults on its bond obligations, and if those having an interest in the Fund successfully sue its officers, then the State will have to pay the losses. One factor influencing the majority in its decision was the unlikelihood of the success of such a suit, due to both the indemnification provision and a legislative declaration that buildout authority securities "are reasonable, prudent and proper" investments. Nonetheless, this scheme can hardly be deemed any more of an indirect loan of State credit than the appropriations financing in Wein II. There, the public purchased State securities in reliance on the State's faith in the integrity of the revenues guaranteeing the public's purchase. The State's faith in the bonds was evidenced by its purchase of them at a time when few others would. If the majority in Wein II perceived the connection between the State and MAC as being too remote to constitute a loan of credit, then it was likewise correct in holding that the relationship between the trustees of the corporation's creditors and the corporation itself as too attenuated to fall within the scope of the constitutional limitation.

IV. Conclusion

Upon a review of the foregoing cases, it is questionable whether a trend in constitutional interpretation can be discerned. In Wein I and II, the court of appeals applied a rule of strict construction to the relevant statutes, even though implying in Wein II that the State had stretched its legislative elasticity to the breaking point. On the other hand, the constitutional reasoning applied in Sgaglione seems attenuated. There the court not only strictly construed the term "benefits," but also went further to conclude, albeit impliedly, that the comptroller's discretion was a benefit.

The court of appeals has taken a result-oriented approach to the City's financial emergency cases. The crucial consideration underlying these decisions seems to be whether the constitutional problems created by the legislation can be remedied without undue hardship to those deriving rights therefrom. Had the court invalidated the SRC, and thus the bonds issued thereunder, the bondholders would have been left holding worthless paper with no governmental back-

225. Id. at 306, 366 N.E.2d at 850, 397 N.Y.S.2d at 762.
226. Id. at 304, 366 N.E.2d at 849, 397 N.Y.S.2d at 760.
ing — a harsh result. In addition, the withdrawal of 750 million dollars of State funds from the City and MAC could have resulted in the calamitous collapse of the City and MAC, leaving the City and MAC securities holders with, at best, an "empty right to litigate" their remedies. Likewise, characterizing the trustee indemnification provision common to public corporations and authorities as an operating expense eliminated the need to submit such a provision to a referendum vote.

On the other hand, the finding that the comptroller could not be compelled to invest retirement funds in the City and MAC securities merely resulted in diversion of this money to other solid investments, thereby ensuring the funds' continued yield. By abrogating the Moratorium Act, the court restored investor confidence in municipal securities and established that a pledge of an entity's faith and credit is its ironclad guarantee that bondholders have a right to be paid and a right to contest any unilateral State interference with these rights. Finally, upholding the right of the State to divert its aid from a governmental entity to a public benefit corporation, the court has retained a flexible financing scheme eminently useful for a city's changing economic status.

The foregoing decisions illustrate the court of appeals' public policy approach to a significant economic problem. The court appears to have rejected an approach grounded in strict adherence to prior case law in favor of one based on an awareness of the current and future fiscal repercussions of its rulings. In these cases, the court has fulfilled a function frequently ignored in comfortable adherence to stare decisis — a function reflected in the maxim that the court is a barometer of change. A court must be flexible enough to administer to the challenges presented by novel legal problems, and such flexibility must be tempered not only with the application of precedent but also with a sensitivity to public attitudes, and economic realities.

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227. Most likely, the upholding of the SRC's validity is an academic exercise. Because of uncertainties inherent in the corporation's structure, the bonds were already encountering great difficulty in the market at the time the decision was rendered. See text accompanying notes 12-17 supra.