The New York Times

Friday, July 26, 2013

When New York teetered on the brink of bankruptcy

By SAM ROBERTS

One by one, guests on the multi-tiered dais of the annual white-tie Alfred E. Smith Memorial Foundation benefit dinner slipped away for secret negotiations to resolve the city's fiscal crisis. Mayor Abraham D. Beame returned to Gracie Mansion early to confer with fellow formally attired city officials, then slept fitfully, knowing the grave decisions he faced the next morning.

By midday that Friday, Oct. 17, 1975, Mr. Beame had signed a formal petition attesting to municipal default. The police commandeered squad cars, poised to serve legal papers on banks that were the city's leading creditors. A court order was pending to preserve the city government's assets, including cash and durable goods, like garbage trucks. A judge with whom the Beames regularly played pinochle was enlisted to order Comptroller Harrison J. Goldin to pay the salaries of city workers before paying the principal and interest due that afternoon on municipal debt.

"I have been advised by the comptroller," a two-and-a-half-page mayoral news release began, "that the City of New York has insufficient cash on hand to meet debt obligations due today. This constitutes the default that we have struggled to avoid." New York City was about to declare bankruptcy.

But that signed petition was never invoked. Today, it hangs framed in the Fifth Avenue office of Ira P. Millstein, one of the city's private lawyers during the fiscal crisis — a testament to the New Yorkers who, after meeting for hours in an Upper East Side apartment that October morning, dodged the financial fate that Detroit suffered last week.

They had come this close to declaring that New York had run out of cash and would default on about $100 million in borrowing due that afternoon. As it was, officials had to persuade the comptroller of the currency to keep Manufacturers Hanover, the city's paying agent, open into the night so the debt payments could be processed.

New York avoided what Detroit did not because, literally at the last minute, all parties agreed to share the pain and avoid the prolonged uncertainty that bankruptcy or receivership promised.

At a key moment, everything depended on Albert Shanker, the teachers' union leader, who, worried about his members, was wary about investing about $150 million of their pension funds in city securities. Just how volatile Mr. Shanker could be had been captured by Woody Allen in "Sleeper," his apocalyptic film. Mr. Allen blamed the end of civilization on the fact that "a man named Albert Shanker got hold of a nuclear device."

Mr. Shanker agreed to meet privately in the apartment of Richard Ravitch, whom Gov. Hugh L. Carey had recruited to rescue the state's overextended Urban Development Corporation. At the meeting were Mr. Ravitch; Mr. Shanker; Mr. Carey; his counsel, Judah Gribetz; former Mayor Robert F. Wagner; Sandra Feldman, Mr. Shanker's deputy and eventual successor; and Harry Van Arsdale, head of the city's Central Labor Council.

Among the other principals who played crucial roles in resolving the crisis: Victor Gotbaum, the municipal union leader who had already agreed to invest in city securities; Felix G. Rohatyn, whom Mr. Carey enlisted from the private sector as a financial adviser; Peter C.

Goldmark Jr., the state budget director; and Stephen Berger, who would become the first director of the Emergency Financial Control Board.

"The one thing that really made a difference was the absolute commitment of a new governor not to put the city into bankruptcy," Mr. Rohatyn recalled. "We were not willing to gamble on something that had never happened before on that scale." (Mr. Carey, his biographer, Seymour P. Lachman, said, had been taught by his father long before that bankruptcy was a deceptively easy solution.)

Few people were advocating bankruptcy because it might abrogate agreements with organized labor and leave financial institutions liable for selling securities that were suspect or even fraudulent. New York bonds and notes were widely held by banks and individuals throughout the United States. World leaders feared the repercussions of a New York bankruptcy. And the city depended on credit, which, had bankruptcy been declared, might have been denied for decades.

"New York was broke, but it wasn't bankrupt," Mr. Berger recalled. "It was an enterprise that had been badly mismanaged, whose finances were uncontrolled and had no real financial systems and was basically run by a history of pushcart peddlers. However, it had a substantial core of political and business leadership, which saw the long-term danger to short-term solution."

"Detroit has none of the inherent characteristics that New York had in its worst financial moments," he added. "In the end, all the stuff we did was to keep the kid from drowning and three years later the economy swept him back on the shore."

Mr. Millstein remembered: "Everyone knew that New York, unlike Detroit, was not a dead city. It just needed some mechanism to get out of the mess."

Municipal bankruptcy was largely untested at the time – how would a judge balance the needs of city employees, poor people, vendors and other creditors? How would it affect the state's credit?

"The fiscal crisis was misnamed," Mr. Rohatyn later recalled. "It was a bankruptcy crisis. We had a much greater sense of potential doom if we went bankrupt.''

Mr. Goldmark said: "Hugh Carey lashed the fate of the state to that of the city. Michigan has done nothing of the kind."

Beyond the financial repercussions, bankruptcy, Mr. Ravitch said, would have been "a failure of democracy to solve its problems and we didn't want to fail. But on the other hand, it was the threat of bankruptcy that got everybody to do things that in the beginning of this process they swore they wouldn't do."