

MEMORANDUM

Date: 26 April 1991

To: Quentin B. Spector

From: Lynnette Kelly

Re: Triggers for the Reimposition of a Control Period and Powers of the Financial Control Board During A Control Period

MUNICIPAL
ASSISTANCE
CORPORATION
FOR THE CITY
OF NEW YORK

This memorandum outlines (i) the five events which would force the Financial Control Board ("FCB") to reimpose a control period on the City, and (ii) the powers of the FCB during a control period.

Events Which Would Trigger the Reimposition of a Control Period

Section 2(12) of the New York State Financial Emergency Act for The City of New York (the "FEA") contains a definition of "Control period." This definition requires that the FCB reimpose a control period upon a determination at any time that any of the five following events has occurred or that there is a "substantial likelihood and imminence" of such occurrence:

- (i) the City shall have failed to pay the principal of or interest on any of its bonds or notes when due or payable;
- (ii) the City shall have incurred a deficit of more than one hundred million dollars, during its fiscal year;
- (iii) the City shall have issued notes in violation of the short-term borrowing limitations of the FEA;
- (iv) the City shall have otherwise violated a provision of the FEA, which violation substantially impairs the ability of the City to pay principal of or interest on its bonds or notes when due and payable or its ability to adopt or adhere to a budget covering all expenditures other than capital items balanced in accordance with the FEA; or
- (v) the comptrollers' joint certification regarding the capital and seasonal financing requirements of the City, and its access to the general public credit markets, could not be made.

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The memorandum dated May 22, 1990, attached hereto as Appendix A, discusses the legal standards by which the phrase "substantial likelihood and imminence" would be analyzed.

In any event, the FEA requires that a control period not extend beyond the earlier of (a) July 1, 2008, or (b) the date (i) when all bonds and notes containing the 1978 State covenant are refunded, redeemed, discharged or defeased, or (ii) when all bonds guaranteed by the federal government are no longer outstanding, whichever of (i) or (ii) shall occur later.

Powers of the Financial Control Board During a Control Period

The legislative history of the 1978 amendments to the FEA outlines the broad powers of the FCB during a control period:

- (i) the FCB has the powers to review, control and supervise the financial management of the City;
- (ii) the FCB must approve the adoption of the City's Four-Year Financial Plans;
- (iii) the FCB has the power to review, control and supervise the disbursement of City funds, under which debt service requirements will be met as a first priority;
- (iv) the FCB must review City operations to assure that sound management practices are observed or restored and that operations are conducted in accordance with the plan; and
- (v) the FCB must review, approve or disapprove City contracts and long-term and short-term borrowing.

Specific elaboration of these broad powers is contained throughout the FEA. These specific powers include:

- (i) the FCB shall consult with the City in the preparation of the financial plan, and certify the revenue estimates approved therein, prescribe the form of the financial

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- plan and exercise the rights of approval disapproval and modification with respect to the financial plan, and in some instances may formulate and promulgate a financial plan;
- (ii) the FCB shall establish and adopt procedures with respect to the maintenance and administration of the board fund;
 - (iii) the FCB shall review the operations, management, efficiency and productivity of City operations and make reports thereon, audit compliance with the financial plan, recommend measures to the City relating to their operations, management, efficiency and productivity and obtain information relating to the financial condition and needs of the City;
 - (iv) the FCB shall receive and review City reports prepared pursuant to the requirements of the FEA, receive and review financial data and shall inspect, copy and audit books and records of the City;
 - (v) the FCB shall approve, modify and approve or promulgate regulations respecting categories and types of categories of contracts required to be reviewed by the FCB, review terms of contracts to determine compliance with the financial plan, disapprove any contract upon a determination that the performance of such contract would be inconsistent with the financial plan;
 - (vi) the FCB shall review and approve the terms of each proposed long-term and short-term borrowing;
 - (vii) the FCB shall issue such orders to the City as it deems necessary to accomplish the purposes of the FEA;
 - (viii) in the event of a default by the City on its outstanding bonds or notes, the FCB may take necessary action to remedy the default and shall direct the City to take such action as the City is authorized to take;

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- (ix) the FCB must approve all agreements and arrangements, whether or not it creates a debt of the City, pursuant to which the revenues or credit of the City may be directly or indirectly pledged, encumbered, committed or promised, contingently or otherwise, for the payment of obligations of a public benefit corporation; and
- (x) the FCB shall have the authority to make and execute agreements and instruments which are necessary for the exercise of its powers and functions.

The memorandum dated September 1986, attached hereto as Appendix B, discusses the powers of the FCB during periods other than a control period.

LK:vrw



State of New York
Financial Control Board

May 22, 1990

M E M O R A N D U M

TO: Allen J. Proctor
FROM: Cathy A. Bell
RE: Substantial Likelihood & Imminence

The City's current fiscal stress raises the obvious question of the potential need for the members of the Financial Control Board ("FCB" or the "Board") to reimpose a control period. The Financial Emergency Act ("FEA" or the "Act") requires the Board to make such a determination at least annually. In recent years, this determination has been made by the Board in July.

The pertinent language of the Act, as set forth in section 2(12), provides that the Board shall reimpose a control period upon a determination at any time that any of five enumerated events (the "events of sunrise") "has occurred" or that there is a "substantial likelihood and imminence" of such occurrence. Given the severity of decline in revenue growth coupled with an explosion in the demand for City services, the most likely event to happen is that the City incurs a deficit in excess of \$100 million. Obviously, after the Comptroller concludes her audit in late October, it will be clear whether a deficit of such magnitude has occurred. Because the Board has of late, however, made its determination in July, the more ambiguous substantial likelihood and imminence criterion is controlling.

This memorandum attempts to set forth parameters within which a determination as to the substantial likelihood and imminence of the occurrence of an event of sunrise can be made. While the FEA itself offers little elaboration on the standards set forth therein, we can be guided by the legislative history of

Act's revision in 1978 (at which time section 2(12) was amended to its present form), and the use of the substantial likelihood and imminence standard in other legal contexts.

I. The Legislative History of FEA Section 2(12)

The legislative history of section 2(12) of the Act suggests that the substantial likelihood and imminence standard was not intended to be highly speculative but rather to be applied under conditions of real probability of occurrence.

The FEA was amended in 1978 to extend the life of the FCB and to revise the powers of the board. Section 2(12) was added to the definitional section of the Act to provide for termination of the control period in accordance with certain statutory prerequisites and to set forth grounds for reimposition. A review of the legislative history of the FEA reveals that the framers of the 1978 amendments realized that the substantial likelihood and imminence language set forth in section 2(12) was "broad"¹ and "open"² but concluded that "such flexibility was appropriate"³. A major law firm involved in drafting the 1978 amendments noted also that a certain amount of subjectivity would be required in making a determination under the substantial likelihood and imminence standard.⁴

The insertion of the word imminence into the relevant language of section 2(12) was made shortly prior to enactment of the FEA as amended⁵. Its insertion indicates an attempt by the framers to decrease the level of speculation required in application of the substantial likelihood criterion. Imminence is a standard necessitating a finding of real probability.

Nevertheless, any assessment of probability, even where based on the most up-to-the-minute analyses of the City's

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= real probability*

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revenues and expenditures, can be labelled mere speculation in the absence of measurable guidelines and parameters within which to make such a determination. Reference to the use of the substantial likelihood and imminence criterion in a legal context can be helpful in this regard.

II. "Likelihood & Imminence" As Used In A Legal Context

The likelihood and imminence standard is utilized by the courts in various areas of the law ranging from determinations of criminal cases under the Fourth Amendment (warrantless entry into private quarters held unjustified based upon finding that DEA agents' assumptions as to the likelihood and imminence of the perceived danger were too speculative)⁶ to decisions on motions for preliminary injunctive relief (requires the finding of a substantial likelihood of success on the merits of the underlying motion coupled with the imminence of irreparable harm resulting from the action sought to be enjoined).⁷ A most insightful analogy can be drawn from the legal analysis applying this standard to First Amendment cases.

The U.S. Supreme Court employs a substantial likelihood and imminence standard in applying the clear and present danger test to cases under the First Amendment involving the freedom of speech.⁸ The test is two-pronged; requiring, first, an assessment of the imminence and magnitude of the danger said to flow from the particular utterance. Secondly, a balancing test is applied, weighing the character of the evil, as well as its likelihood, against the need for free and unfettered expression.⁹ In applying this analysis, the courts begin by asking three questions: is there a danger; if so, is it imminent; and, is it so substantial as to justify action?¹⁰ The answers to these questions require a determination as to the extent to which the danger sought to be avoided is a likely consequence and whether

⁶ U.S. v. Driver, 776 F.2d 807 (9th Cir. 1985)

⁷ United Mine Workers v. Bituminous Coal Operators' Association, 898 F.2d 177 (D.C. Cir. 1990)

⁸ See, e.g., Landmark v. Commonwealth of Virginia, 435 U.S. 829 (1978).

⁹ See, Landmark v. Commonwealth of Virginia, supra at 830; Whitney v. California, 274 U.S. 357, 378-379 (1927).

¹⁰ Whitney v. California, supra.

the degree of likelihood is sufficient to justify action. The ability of reducing the risk of danger by other means is also weighed.¹¹

A working principle that is followed in these type of cases and one that is certainly applicable to our analysis is that the danger must be extremely serious and the degree of imminence extremely high.¹² Indeed, courts have held in this context that, in order to make the requisite showing of imminence, it must be established, by a "solidity of evidence"¹³ that the danger is not remote nor even probable, but immediately imperils.¹⁴

A FCB determination as to whether an event of sunrise is substantially likely and imminent could be made by applying a similar analysis to the City's fiscal situation as constrained by the Act. For purposes of example, let us focus on the most probable of such events to occur, the incurring of a budget deficit in excess of \$100 million. Clearly the nature of the substantial likelihood and imminence analysis presupposes that it will be made prior to October 31st when the City Comptroller issues her audit report for the immediately preceding fiscal year (hereinafter referred to as the "close"). If at close, a deficit in excess of \$100 million is reported, an event of sunrise "has occurred" and the FCB will have no alternative to reimposing a control period.

Reimposition of a control period prior to close, on the other hand, would necessarily entail some speculation, based largely on FCB staff analyses, as to the likelihood and magnitude of such a deficit. Once a conclusion is reached that a deficit is likely with a magnitude somewhere in the range of \$100 million, the next step would require a balancing of two factors:

✓ 1. the impact of such a deficit on the City's fiscal affairs and under the Act, as well as the degree of likelihood that a deficit of the requisite magnitude will occur, and

✓ 2. the obviously negative ramifications that the reimposition of a control period will have in the public eye and, more importantly, the public credit markets.

11 Landmark v. Commonwealth of Virginia, supra.

12 Bridges v. California, 314 U.S. 260, 263 (1941).

13 See, Pennekemp v. Florida, 326 U.S. 331, 347 (1946).

14 Craig v. Harney, 331 U.S. 375, 376 (1962).

In assessing imminence, one must take into account the existence or absence of a realistic and attainable gap-closing program or other available means at the City's disposal to avoid an impending deficit.

The mechanics of a likelihood and imminence analysis utilizing the standards outlined above are best discussed in relation to the several possible scenarios in which the FCB would be called upon to make such a determination. These scenarios reflect hypothetical states of the City's finances at various critical points in time prior to October 31.

III. Scenarios Applying Likelihood and Imminence Standard

In order to illustrate how a similar analysis of substantial likelihood and imminence would work in application to the FCB determination under section 2(12), we provide the following hypothetical scenarios. As will be evident, the determining factors in each case are the proximity in time to the close of the City's fiscal year, the magnitude of the problem, and the measures available to the City to reduce the problem.

Scenario 1. Under this scenario, the relevant assumptions are that at the time the City submits its Executive Budget (April 26, pursuant to the City Charter unless extended by local law) the City projects a deficit in the current fiscal year of less than \$100 million with the budget for the upcoming fiscal year reflecting payment of the preceding year's deficit in accordance with FEA section 8(1)(f) and a reasonable gap-closing program to achieve budget balance in that year.

Applying the judicial likelihood and imminence analysis to this scenario, we begin by posing answers to the following questions. Is a deficit in excess of \$100 million likely to occur in this fiscal year? Is it imminent and so substantial as to warrant reimposition of a control period prior to its actual occurrence? If not this year, is a deficit of such magnitude likely in the next fiscal year?

Assuming that 1) the City's forecast of a current year deficit of less than \$100 million is determined to be based upon reasonable and appropriate assumptions and methods of estimation and 2) barring any unforeseen declines in revenues or increases in mandated or necessary expenditures in excess of funds available in the general reserve, the Board would have to conclude that a deficit in excess of \$100 million is not substantially likely to occur this fiscal year and thus is not imminent. Looking ahead to the next fiscal year, while imminence is an issue, the reasonableness and value of the City's proposed

gap-closing program would be dispositive. If the City can reasonably close its projected gap by taking actions that are measurable and attainable and we concur with its projections, the Board would have to determine that no grounds exist warranting reimposition.

Scenario 2. Same facts as presented in scenario 1 except that the gap-closing program set forth by the City in its Executive Budget for the upcoming fiscal year does not appear reasonable nor likely to result in the level of savings necessary to achieve budget balance in that year.

In such an event, assuming that the FCB staff's evaluation of the City's gap-closing program presents the likelihood of a \$100 million+ deficit for that year, the approximately eighteen months between presentation of the Executive Budget projections and the close of the fiscal year in question significantly reduces the imminence of such an occurrence. In the absence of immediate peril, the Board's most responsible course of action would be to urge to City to modify its gap-closing program in order to avoid reimposition of a control period.

Scenario 3. After budget adoption, the Board meets in July in order to render its annual determination. The FCB report indicates that the Comptroller's audit will reveal a preceding fiscal year deficit in excess of \$100 million. The City's projections for the new fiscal year show a gap, but it has formulated and is taking steps to implement a reasonable gap-closing program. The FCB report has concluded that, if fully implemented, the City's PEG program would result in budget balance for the current year.

The statutory mandate of section 2(12) under this set of facts seems clear; the Board would have no choice under the Act but to reimpose a control period based upon the substantial likelihood and imminence of a deficit in excess of \$100 million being reported. The City's ability to avoid a recurring deficit situation in the current fiscal year would be of little import in reaching this decision.

Under this scenario, however, having reimposed a control period based upon the anticipated negative results of operations for the preceding fiscal year, the Board would be faced with the interesting dilemma of continued control in the face of a favorable prognosis for the current year. Section 2(12) of the Act provides that a control period, once reimposed, shall be lifted when the Board determines that the circumstances warranting its reimposition no longer exist. Under this set of

facts, prudence would dictate that a control period be continued until at least preliminary results of operations for the current year are available that reflect budget balance. Prior to terminating control, inherent fiscal instability should be ruled out as the cause of the preceding year deficit.

Scenario 4. Same point in time as set forth in Scenario 3. It appears that the audit report will reveal that the City incurred a deficit in the preceding fiscal year in an amount somewhat less than \$100 million. Our report takes issue with the projected savings from the City's current PEG program and by our analysis, it appears that, on top of last year's deficit, the City will incur a deficit of greater than \$100 million this year.

Here, the necessity of Board action prior to the fact seems clearer than in scenario 2, where a similar situation is viewed as of April 26. Nevertheless, imminence remains an issue, since at this point the City would still have about twelve months within which to correct its deficit situation. On balance, however, the specter of a \$100 million+ deficit on the heels of a prior year deficit and in the absence of a realistic plan to avert such an occurrence, signals grave fiscal instability. When weighed against the implications that a new control period would have for the City, factors would tend to argue in favor of reimposition which could be viewed as having a stabilizing effect. The determining factor, however, under this set of facts would be the existence and availability of offsetting resources that may or may not be reflected in the City's PEG. Any reasonable possibility that the City could take remedial action in a timely fashion would justify a wait-and-see approach on the part of the Board.

Scenario 5. On October 1, the preliminary runs done by the Comptroller's office reveal a preceding year deficit in excess of \$100 million. The City has recently announced plans to modify its current year budget to close an unforeseen shortfall in anticipated revenues in the amount of \$100 million. The gap-closing program as announced seems questionable.

Reimposition would be warranted -- indeed, necessitated -- by the pendency and expected content of the Comptroller's report. Factors relating to the current year are further justification for reimposition. In their absence, however, reimposition would nonetheless be mandated at this juncture based upon the imminence of a reported deficit in excess of \$100 million.

Scenario 6. Same point in time as in scenario 5 except it appears from preliminary runs that the City achieved budget balance in the preceding fiscal year, however, only after repeatedly revising its revenue estimates and instituting severe service reductions. The City's proposal to close an unforeseen current year budget gap in excess of \$100 million appears incapable of producing the savings necessary to avoid a deficit.

Here, the balancing test becomes crucial. If based upon our assessment of the City's gap-closing program as announced, a deficit in excess of \$100 million seems likely for the current fiscal year, the Board would have to balance the need to reimpose a control period, both under the Act and in order to stabilize the City's fiscal affairs, against the impact of reimposition on the City's credit rating and ongoing viability. Weighing against reimposition would be the existence and availability of other resources which may not be reflected in the City's budget, such as MAC surpluses or other one-shot cash infusions, and the ability of the City to implement service reductions of the magnitude necessary to avoid such a deficit.

The City will, at this juncture, still have some nine months within which to correct any problems the FCB may foresee. Absent a conclusion that the City has completely run out of options in attempting to close its projected gap, a finding of imminence might appear precipitous.

IV. Conclusion

In summary, it appears that while a determination under the substantial likelihood and imminence standard pursuant to section 2(12) of the Act does requires a certain level of speculation, the adherence to the guidelines and parameters followed by the courts in application of such criterion will significantly reduce any attendant element of arbitrariness. While the scenarios presented above do not purport to reflect every possible configuration of events, they clearly show that the Board's discretion in deciding to reimpose a control period under this standard is diminished based upon the magnitude of the problem facing the City, the remedial measures available to the City and the proximity of such determination to the close of the City's fiscal year. Applying this analysis, the following becomes evident:

In April, a Board determination employing the substantial likelihood and imminence criterion will, almost under any conceivable set of facts, tend to indicate that reimposition is not warranted (Scenarios 1 and 2).

In July, reimposition of a control period will be warranted only where it appears that a deficit in excess of \$100 million has been incurred in the immediately preceding fiscal year (Scenario 3). Projected current year imbalance would not at this point in time be sufficiently imminent to warrant reimposition. Such imbalance, however, when coupled with a prior year deficit, irrespective of size, would necessitate close scrutiny and stern direction to the City to take remedial action or face renewed control (Scenario 4).

In October, the availability of preliminary results of operations for the preceding fiscal year will guide any decision to reimpose. As to the current fiscal year, reimposition would be warranted only where sustained, irreversible fiscal instability appears certain (Scenarios 5 and 6).

BEL:slt

September 1986

THE FINANCIAL CONTROL BOARD DURING SUNSET(1) Sunset: What It Means

(A) On June 30, 1986, three statutory conditions were satisfied, ending the Control Period and initiating sunset:

- (a) Federally guaranteed debt paid off,
- (b) three successive budgets balanced according to GAAP, and
- (c) full access to credit markets certified.

As a result, the Financial Emergency Act suspends the FCB's powers to approve City financial plans, borrowings, and contracts.

(B) During sunset, the FCB is required to "review" financial plans, borrowings, and contracts; to re-examine financial plans at least quarterly; and to notify the City if a financial plan or modification to the plan does not conform to the standards set forth in the Act and to take "such other action as it deems appropriate".

In addition, during sunset, one new power is added: each year the FCB must determine whether a new control period, under which the suspended powers are reimposed, should be declared; this responsibility must be carried out in public. ✓

(2) The FCB During Sunset: Mission, Goals, Strategies

(A) Mission: to help preserve the City's fiscal independence by avoiding imposition of a new control period.

(B) Goals

(1) Ensure adherence to the City's multi-year financial planning process as defined in the Financial Emergency Act (development of financial plans, reserve funds, GAAP balanced budgets for covered organizations, etc.) in order to achieve recurring budget balance.

- (2) Undertake analyses of important economic, fiscal, social, and physical developments that have major implications for the City's financial planning process and financial condition.
- (3) Fully inform the Governor of current and anticipated fiscal and economic developments affecting the financial condition of the City; and advise him on their implications for the State and for the City's efforts to maintain recurring budget balance.

(C) Strategies to Achieve Goals

- (1) Maintaining adherence to the financial planning process, by
 - reviewing City financial plans, borrowings, and contracts, including at least quarterly reviews of revenues and expenditures,
 - monitoring the levels of federal and state aid and federal and state legislation having fiscal impacts on the City,
 - consulting with City officials to ensure that City financial plans meet the standards set forth in the Financial Emergency Act (reasonable estimates, reserves, etc.) and that borrowings and contracts are consistent with current financial plans,
 - providing information to the public on the City's financial plans, including, where appropriate, the views and recommendations of the FCB, and
 - making public annually the FCB's determination with respect to imposition of a new control period.
- (2) Undertaking analyses of major developments and trends which may have important long-term fiscal implications for the City's financial planning process and financial condition, such as
 - development of fiscal indicators to provide early warning of major impacts on the City's budget resulting from economic, financial, social, and physical conditions and trends,
 - analysis (and periodic evaluation) of recent federal tax reform legislation to determine its

impact on City revenues and borrowing costs and on various key economic sectors of the City,

- analysis of City expenditure trends in light of anticipated continuing reduced federal aid and growth of uncontrollable (fixed) expenses,
- analysis of major spending demands on the City's budget, including a comparison of spending demands on the City with those on other large city and county governments, and
- short-term analyses, such as how budget gaps are eliminated (over, for example, a 2-3 year period), for the City as a whole and for selected agencies and covered organizations.

(3) General FCB Calendar of Activities

(A) July - August - September

- initiate major studies and analyses (short- and long-term)
- review Office of Special Deputy Comptroller (OSDC) annual report on City contracts and make recommendations, if any, to the FCB
- review Municipal Assistance Corporation (MAC) annual report and make recommendations, if any, to the FCB
- review Mayor's annual management report and make recommendations, if any, to the FCB

(B) October - November - December

- review revenue and spending activities during first quarter of fiscal year under the financial plan; consider modifications, if any, to the plan; and publish report on first quarter results
- review City auditor's report on the City's financial statements and make the annual determination with respect to the amount of deficit, if any, during the preceding fiscal year; and publish that determination
- review OSDC quarterly report on contract volume

(C) January - February - March

- review revenue and spending activities during second quarter of fiscal year under the financial

plan, preliminary budget estimates, and modifications to the financial plan; and publish mid-year report

-review Mayor's mid-year management report and make recommendations, if any, to the FCB

-review OSDC quarterly report on contract volume

-issue FCB annual review of City productivity improvement efforts

(D) April - May - June

-review OSDC quarterly report on contract volume

-review executive budget submitted to City Council, new financial plan, and modifications to the budget and plan resulting from Board of Estimate and City Council action; and publish report on the financial plan

-FCB requests joint certification from State and City Comptrollers concerning market access of City

-FCB issues report on its determination as to whether the City (1) has failed to pay principal or interest on notes or bonds when due; (2) has issued notes in violation of the Act; (3) has violated any provision of the Act which substantially impairs its ability to pay principal or interest on obligations or to adhere to a balanced budget; (4) has access to credit markets, as certified by Comptrollers; and (5) has not incurred a deficit in excess of \$100 million in the current fiscal year

Throughout the year, the FCB staff will continue to carry out a variety of monitoring functions: the revenue unit will monitor changes in economic forecasts and actual revenue results, relate them to the City's revenue projections, and periodically provide new projections, as appropriate; the expenditures unit will monitor actual City spending results and other developments relating to expenditures, relate them to the City's spending projections, and provide new projections, as appropriate; the finance unit will monitor the progress of the City's capital program, relate it to the City's long-term borrowing plans, and provide analyses of debt service costs and the level of outstanding debt; and the legal affairs unit will coordinate FCB review of City contracts and borrowings, provide legal advice on matters arising under the Act, and assure FCB compliance with relevant state laws and regulations.

(4) FCB Meetings

The Control Board is required to hold one public meeting each year: the meeting at which it makes its determination with respect to the conditions that would trigger the end of sunset. This meeting, which would be attended by principals, would be scheduled for late June of each year.

From time to time, other meetings of the Control Board may be required. For example, in June it is not possible to say with certainty that operations for the then-current fiscal year have not resulted in a deficit of greater than \$100 million. That question can be definitively answered only upon release of the report of the City's auditors, which occurs in late October.

Consequently, it will be necessary to hold a meeting thereafter (in November) to reaffirm that this condition did not occur. Other occasions to meet may arise, for example, to revise the FCB's contract review regulations. It is unlikely that these meetings will require the attendance of FCB principals, but rather could be handled by representatives of the public members of the Board.

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State of New York
Financial Control Board

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II. "Likelihood & Imminence" As Used In A Legal Context

The likelihood and imminence standard is utilized by the courts in various areas of the law ranging from determinations of criminal cases under the Fourth Amendment (warrantless entry into private quarters held unjustified based upon finding that DEA agents' assumptions as to the likelihood and imminence of the perceived danger were too speculative)⁶ to decisions on motions for preliminary injunctive relief (requires the finding of a substantial likelihood of success on the merits of the underlying motion coupled with the imminence of irreparable harm resulting from the action sought to be enjoined). A most insightful analogy can be drawn from the legal analysis applying this standard to First Amendment cases.

The U.S. Supreme Court employs a substantial likelihood and imminence standard in applying the clear and present danger test to cases⁸ under the First Amendment involving the freedom of speech. The test is two-pronged; requiring, first, an assessment of the imminence and magnitude of the danger said to flow from the particular utterance. Secondly, a balancing test is applied, weighing the character of the evil, as well as its likelihood, against the need for free and unfettered expression.⁹ In applying this analysis, the courts begin by asking three questions: is there a danger; if so, is it imminent; and, is it so substantial as to justify action?¹⁰ The answers to these questions require a determination as to the extent to which the danger sought to be avoided is a likely consequence and whether

⁶ U.S. v. Driver, 776 F.2d 807 (9th Cir. 1985)

⁷ United Mine Workers v. Bituminous Coal Operators' Association, 898 F.2d 177 (D.C. Cir. 1990)

⁸ See, e.g., Landmark v. Commonwealth of Virginia, 435 U.S. 829 (1978).

⁹ See, Landmark v. Commonwealth of Virginia, supra at 830; Whitney v. California, 274 U.S. 357, 378-379 (1927).

¹⁰ Whitney v. California, supra.

the degree of likelihood is sufficient to justify action. The ability of reducing the risk of danger by other means is also weighed.¹¹

A working principle that is followed in these type of cases and one that is certainly applicable to our analysis is that the danger must be extremely serious and the degree of imminence extremely high.¹² Indeed, courts have held in this context that, in order to make the requisite showing of imminence, it must be established, by a "solidity of evidence"¹³ that the danger is not remote nor even probable, but immediately imperils.¹⁴

A FCB determination as to whether an event of sunrise is substantially likely and imminent could be made by applying a similar analysis to the City's fiscal situation as constrained by the Act. For purposes of example, let us focus on the most probable of such events to occur, the incurring of a budget deficit in excess of \$100 million. Clearly the nature of the substantial likelihood and imminence analysis presupposes that it will be made prior to October 31st when the City Comptroller issues her audit report for the immediately preceding fiscal year (hereinafter referred to as the "close"). If at close, a deficit in excess of \$100 million is reported, an event of sunrise "has occurred" and the FCB will have no alternative to reimposing a control period.

Reimposition of a control period prior to close, on the other hand, would necessarily entail some speculation, based largely on FCB staff analyses, as to the likelihood and magnitude of such a deficit. Once a conclusion is reached that a deficit is likely with a magnitude somewhere in the range of \$100 million, the next step would require a balancing of two factors:

✓ 1. the impact of such a deficit on the City's fiscal affairs and under the Act, as well as the degree of likelihood that a deficit of the requisite magnitude will occur, and

✓ 2. the obviously negative ramifications that the reimposition of a control period will have in the public eye and, more importantly, the public credit markets.

¹¹ Landmark v. Commonwealth of Virginia, supra.

¹² Bridges v. California, 314 U.S. 260, 263 (1941).

¹³ See, Pennekemp v. Florida, 326 U.S. 331, 347 (1946).

¹⁴ Craig v. Harney, 331 U.S. 375, 376 (1962).

In assessing imminence, one must take into account the existence or absence of a realistic and attainable gap-closing program or other available means at the City's disposal to avoid an impending deficit.

The mechanics of a likelihood and imminence analysis utilizing the standards outlined above are best discussed in relation to the several possible scenarios in which the FCB would be called upon to make such a determination. These scenarios reflect hypothetical states of the City's finances at various critical points in time prior to October 31.

III. Scenarios Applying Likelihood and Imminence Standard

In order to illustrate how a similar analysis of substantial likelihood and imminence would work in application to the FCB determination under section 2(12), we provide the following hypothetical scenarios. As will be evident, the determining factors in each case are the proximity in time to the close of the City's fiscal year, the magnitude of the problem, and the measures available to the City to reduce the problem.

Scenario 1. Under this scenario, the relevant assumptions are that at the time the City submits its Executive Budget (April 26, pursuant to the City Charter unless extended by local law) the City projects a deficit in the current fiscal year of less than \$100 million with the budget for the upcoming fiscal year reflecting payment of the preceding year's deficit in accordance with FEA section 8(1)(f) and a reasonable gap-closing program to achieve budget balance in that year.

Applying the judicial likelihood and imminence analysis to this scenario, we begin by posing answers to the following questions. Is a deficit in excess of \$100 million likely to occur in this fiscal year? Is it imminent and so substantial as to warrant reimposition of a control period prior to its actual occurrence? If not this year, is a deficit of such magnitude likely in the next fiscal year?

Assuming that 1) the City's forecast of a current year deficit of less than \$100 million is determined to be based upon reasonable and appropriate assumptions and methods of estimation and 2) barring any unforeseen declines in revenues or increases in mandated or necessary expenditures in excess of funds available in the general reserve, the Board would have to conclude that a deficit in excess of \$100 million is not substantially likely to occur this fiscal year and thus is not imminent. Looking ahead to the next fiscal year, while imminence is an issue, the reasonableness and value of the City's proposed

gap-closing program would be dispositive. If the City can reasonably close its projected gap by taking actions that are measurable and attainable and we concur with its projections, the Board would have to determine that no grounds exist warranting reimposition.

Scenario 2. Same facts as presented in scenario 1 except that the gap-closing program set forth by the City in its Executive Budget for the upcoming fiscal year does not appear reasonable nor likely to result in the level of savings necessary to achieve budget balance in that year.

In such an event, assuming that the FCB staff's evaluation of the City's gap-closing program presents the likelihood of a \$100 million+ deficit for that year, the approximately eighteen months between presentation of the Executive Budget projections and the close of the fiscal year in question significantly reduces the imminence of such an occurrence. In the absence of immediate peril, the Board's most responsible course of action would be to urge to City to modify its gap-closing program in order to avoid reimposition of a control period.

Scenario 3. After budget adoption, the Board meets in July in order to render its annual determination. The FCB report indicates that the Comptroller's audit will reveal a preceding fiscal year deficit in excess of \$100 million. The City's projections for the new fiscal year show a gap, but it has formulated and is taking steps to implement a reasonable gap-closing program. The FCB report has concluded that, if fully implemented, the City's PEG program would result in budget balance for the current year.

The statutory mandate of section 2(12) under this set of facts seems clear; the Board would have no choice under the Act but to reimpose a control period based upon the substantial likelihood and imminence of a deficit in excess of \$100 million being reported. The City's ability to avoid a recurring deficit situation in the current fiscal year would be of little import in reaching this decision.

Under this scenario, however, having reimposed a control period based upon the anticipated negative results of operations for the preceding fiscal year, the Board would be faced with the interesting dilemma of continued control in the face of a favorable prognosis for the current year. Section 2(12) of the Act provides that a control period, once reimposed, shall be lifted when the Board determines that the circumstances warranting its reimposition no longer exist. Under this set of

facts, prudence would dictate that a control period be continued until at least preliminary results of operations for the current year are available that reflect budget balance. Prior to terminating control, inherent fiscal instability should be ruled out as the cause of the preceding year deficit.

Scenario 4. Same point in time as set forth in Scenario 3. It appears that the audit report will reveal that the City incurred a deficit in the preceding fiscal year in an amount somewhat less than \$100 million. Our report takes issue with the projected savings from the City's current PEG program and by our analysis, it appears that, on top of last year's deficit, the City will incur a deficit of greater than \$100 million this year.

Here, the necessity of Board action prior to the fact seems clearer than in scenario 2, where a similar situation is viewed as of April 26. Nevertheless, imminence remains an issue, since at this point the City would still have about twelve months within which to correct its deficit situation. On balance, however, the specter of a \$100 million+ deficit on the heels of a prior year deficit and in the absence of a realistic plan to avert such an occurrence, signals grave fiscal instability. When weighed against the implications that a new control period would have for the City, factors would tend to argue in favor of reimposition which could be viewed as having a stabilizing effect. The determining factor, however, under this set of facts would be the existence and availability of offsetting resources that may or may not be reflected in the City's PEG. Any reasonable possibility that the City could take remedial action in a timely fashion would justify a wait-and-see approach on the part of the Board.

Scenario 5. On October 1, the preliminary runs done by the Comptroller's office reveal a preceding year deficit in excess of \$100 million. The City has recently announced plans to modify its current year budget to close an unforeseen shortfall in anticipated revenues in the amount of \$100 million. The gap-closing program as announced seems questionable.

Reimposition would be warranted -- indeed, necessitated -- by the pendency and expected content of the Comptroller's report. Factors relating to the current year are further justification for reimposition. In their absence, however, reimposition would nonetheless be mandated at this juncture based upon the imminence of a reported deficit in excess of \$100 million.

Scenario 6. Same point in time as in scenario 5 except it appears from preliminary runs that the City achieved budget balance in the preceding fiscal year, however, only after repeatedly revising its revenue estimates and instituting severe service reductions. The City's proposal to close an unforeseen current year budget gap in excess of \$100 million appears incapable of producing the savings necessary to avoid a deficit.

Here, the balancing test becomes crucial. If based upon our assessment of the City's gap-closing program as announced, a deficit in excess of \$100 million seems likely for the current fiscal year, the Board would have to balance the need to reimpose a control period, both under the Act and in order to stabilize the City's fiscal affairs, against the impact of reimposition on the City's credit rating and ongoing viability. Weighing against reimposition would be the existence and availability of other resources which may not be reflected in the City's budget, such as MAC surpluses or other one-shot cash infusions, and the ability of the City to implement service reductions of the magnitude necessary to avoid such a deficit.

The City will, at this juncture, still have some nine months within which to correct any problems the FCB may foresee. Absent a conclusion that the City has completely run out of options in attempting to close its projected gap, a finding of imminence might appear precipitous.

IV. Conclusion

In summary, it appears that while a determination under the substantial likelihood and imminence standard pursuant to section 2(12) of the Act does requires a certain level of speculation, the adherence to the guidelines and parameters followed by the courts in application of such criterion will significantly reduce any attendant element of arbitrariness. While the scenarios presented above do not purport to reflect every possible configuration of events, they clearly show that the Board's discretion in deciding to reimpose a control period under this standard is diminished based upon the magnitude of the problem facing the City, the remedial measures available to the City and the proximity of such determination to the close of the City's fiscal year. Applying this analysis, the following becomes evident:

In April, a Board determination employing the substantial likelihood and imminence criterion will, almost under any conceivable set of facts, tend to indicate that reimposition is not warranted (Scenarios 1 and 2).

In July, reimposition of a control period will be warranted only where it appears that a deficit in excess of \$100 million has been incurred in the immediately preceding fiscal year (Scenario 3). Projected current year imbalance would not at this point in time be sufficiently imminent to warrant reimposition. Such imbalance, however, when coupled with a prior year deficit, irrespective of size, would necessitate close scrutiny and stern direction to the City to take remedial action or face renewed control (Scenario 4).

In October, the availability of preliminary results of operations for the preceding fiscal year will guide any decision to reimpose. As to the current fiscal year, reimposition would be warranted only where sustained, irreversible fiscal instability appears certain (Scenarios 5 and 6).

BEL:slt

NEW YORK STATE FINANCIAL CONTROL BOARD

The Financial Control Board (FCB), created by the New York State Financial Emergency Act for the City of New York, reviews and monitors the management of New York City's financial affairs. The Control Board is scheduled to go out of existence on July 1, 2008, but can be terminated earlier if all bonds issued pursuant to its act have been retired.

Due to significant improvements in its finances and operations, the City has been able to meet the conditions necessary for ending the statutorily defined control period and certain Financial Control Board approval powers have therefore been reduced. Nevertheless, the Financial Emergency Act still requires FCB to review annually the City's four-year financial plans and all City contracts, and

to notify the City of any violation of the act's provisions. Similarly, FCB determines each year if a control period should be reimposed because the City has incurred a deficit greater than \$100 million, has failed to pay debt service or has fallen short on other specified grounds.

To avoid unnecessary duplication of effort and expense in financially monitoring the City, FCB and the Municipal Assistance Corporation (MAC) have agreed to share data, studies, analyses and reports. As in the past, FCB's expenses are repayable from funds provided by MAC.

The Special Revenue Fund appropriation of \$1,988,800 recommended for 1989-90 maintains the Board's operations at current levels.

**STATE OPERATIONS
ALL FUNDS FINANCIAL REQUIREMENTS BY FUND TYPE
APPROPRIATIONS**

Fund Type	Available 1988-89	Recommended 1989-90	Change
Special Revenue Funds — Other	\$2,015,900	\$1,988,800	-\$27,100
Total	\$2,015,900	\$1,988,800	-\$27,100
Adjustments:			
Transfer(s) From:			
Collective Bargaining Agreements			
Special Revenue Funds — Other		-39,400	
Appropriated 1988-89	\$1,976,500		

COMMISSION ON GOVERNMENT INTEGRITY

**STATE OPERATIONS
ALL FUNDS FINANCIAL REQUIREMENTS BY FUND TYPE
APPROPRIATIONS**

Fund Type	Available 1988-89	Recommended 1989-90	Change
General Fund	\$5,495,400	\$2,400,000	-\$3,095,400
Total	\$5,495,400	\$2,400,000	-\$3,095,400
Adjustments:			
Transfer(s) From:			
All State Departments and Agencies			
General Fund		-495,400	
Appropriated 1988-89	\$5,000,000		

September 1986

THE FINANCIAL CONTROL BOARD DURING SUNSET

(1) Sunset: What It Means

(A) On June 30, 1986, three statutory conditions were satisfied, ending the Control Period and initiating sunset:

- (a) Federally guaranteed debt paid off,
- (b) three successive budgets balanced according to GAAP, and
- (c) full access to credit markets certified.

As a result, the Financial Emergency Act suspends the FCB's powers to approve City financial plans, borrowings, and contracts.

(B) During sunset, the FCB is required to "review" financial plans, borrowings, and contracts; to re-examine financial plans at least quarterly; and to notify the City if a financial plan or modification to the plan does not conform to the standards set forth in the Act and to take "such other action as it deems appropriate".

In addition, during sunset, one new power is added: each year the FCB must determine whether a new control period, under which the suspended powers are reimposed, should be declared; this responsibility must be carried out in public. ✓

(2) The FCB During Sunset: Mission, Goals, Strategies

(A) Mission: to help preserve the City's fiscal independence by avoiding imposition of a new control period.

(B) Goals

- (1) Ensure adherence to the City's multi-year financial planning process as defined in the Financial Emergency Act (development of financial plans, reserve funds, GAAP balanced budgets for covered organizations, etc.) in order to achieve recurring budget balance.

- (2) Undertake analyses of important economic, fiscal, social, and physical developments that have major implications for the City's financial planning process and financial condition.
- (3) Fully inform the Governor of current and anticipated fiscal and economic developments affecting the financial condition of the City; and advise him on their implications for the State and for the City's efforts to maintain recurring budget balance.

(C) Strategies to Achieve Goals

- (1) Maintaining adherence to the financial planning process, by
 - reviewing City financial plans, borrowings, and contracts, including at least quarterly reviews of revenues and expenditures,
 - monitoring the levels of federal and state aid and federal and state legislation having fiscal impacts on the City,
 - consulting with City officials to ensure that City financial plans meet the standards set forth in the Financial Emergency Act (reasonable estimates, reserves, etc.) and that borrowings and contracts are consistent with current financial plans,
 - providing information to the public on the City's financial plans, including, where appropriate, the views and recommendations of the FCB, and
 - making public annually the FCB's determination with respect to imposition of a new control period.
- (2) Undertaking analyses of major developments and trends which may have important long-term fiscal implications for the City's financial planning process and financial condition, such as
 - development of fiscal indicators to provide early warning of major impacts on the City's budget resulting from economic, financial, social, and physical conditions and trends,
 - analysis (and periodic evaluation) of recent federal tax reform legislation to determine its

impact on City revenues and borrowing costs and on various key economic sectors of the City,

- analysis of City expenditure trends in light of anticipated continuing reduced federal aid and growth of uncontrollable (fixed) expenses,
- analysis of major spending demands on the City's budget, including a comparison of spending demands on the City with those on other large city and county governments, and
- short-term analyses, such as how budget gaps are eliminated (over, for example, a 2-3 year period), for the City as a whole and for selected agencies and covered organizations.

(3) General FCB Calendar of Activities

(A) July - August - September

- initiate major studies and analyses (short -and long-term)
- review Office of Special Deputy Comptroller (OSDC) annual report on City contracts and make recommendations, if any, to the FCB
- review Municipal Assistance Corporation (MAC) annual report and make recommendations, if any, to the FCB
- review Mayor's annual management report and make recommendations, if any, to the FCB

(B) October - November - December

- review revenue and spending activities during first quarter of fiscal year under the financial plan; consider modifications, if any, to the plan; and publish report on first quarter results
- review City auditor's report on the City's financial statements and make the annual determination with respect to the amount of deficit, if any, during the preceding fiscal year; and publish that determination
- review OSDC quarterly report on contract volume

(C) January - February - March

- review revenue and spending activities during second quarter of fiscal year under the financial

plan, preliminary budget estimates, and modifications to the financial plan; and publish mid-year report

- review Mayor's mid-year management report and make recommendations, if any, to the FCB
- review OSDC quarterly report on contract volume
- issue FCB annual review of City productivity improvement efforts

(D) April - May - June

- review OSDC quarterly report on contract volume
- review executive budget submitted to City Council, new financial plan, and modifications to the budget and plan resulting from Board of Estimate and City Council action; and publish report on the financial plan
- FCB requests joint certification from State and City Comptrollers concerning market access of City
- FCB issues report on its determination as to whether the City (1) has failed to pay principal or interest on notes or bonds when due; (2) has issued notes in violation of the Act; (3) has violated any provision of the Act which substantially impairs its ability to pay principal or interest on obligations or to adhere to a balanced budget; (4) has access to credit markets, as certified by Comptrollers; and (5) has not incurred a deficit in excess of \$100 million in the current fiscal year

Throughout the year, the FCB staff will continue to carry out a variety of monitoring functions: the revenue unit will monitor changes in economic forecasts and actual revenue results, relate them to the City's revenue projections, and periodically provide new projections, as appropriate; the expenditures unit will monitor actual City spending results and other developments relating to expenditures, relate them to the City's spending projections, and provide new projections, as appropriate; the finance unit will monitor the progress of the City's capital program, relate it to the City's long-term borrowing plans, and provide analyses of debt service costs and the level of outstanding debt; and the legal affairs unit will coordinate FCB review of City contracts and borrowings, provide legal advice on matters arising under the Act, and assure FCB compliance with relevant state laws and regulations.

(4) FCB Meetings

The Control Board is required to hold one public meeting each year: the meeting at which it makes its determination with respect to the conditions that would trigger the end of sunset. This meeting, which would be attended by principals, would be scheduled for late June of each year.

From time to time, other meetings of the Control Board may be required. For example, in June it is not possible to say with certainty that operations for the then-current fiscal year have not resulted in a deficit of greater than \$100 million. That question can be definitively answered only upon release of the report of the City's auditors, which occurs in late October.

Consequently, it will be necessary to hold a meeting thereafter (in November) to reaffirm that this condition did not occur. Other occasions to meet may arise, for example, to revise the FCB's contract review regulations. It is unlikely that these meetings will require the attendance of FCB principals, but rather could be handled by representatives of the public members of the Board.

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