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Remarks of Harrison J. Goldin
The Civic Federation and Federal Reserve Bank of Chicago
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Although my firm, Goldin Associates, and I have been deeply involved as a consultant to diverse constituencies in the financial distress and bankruptcies of such high profile municipal securities issuers as Harrisburg, Pennsylvania, Jefferson County Alabama, Detroit and now Puerto Rico, it is New York City with whose financial collapse I was most closely associated and with whose recovery and aftermath I am most intimately familiar. So while New York is in many ways unique, both the causes of its near collapse and the wide-ranging remedies that led it to new found viability are a template for comparably situated cities, school districts and, to a degree, even states around the country. Hence, in speaking to my assigned topic, what impact emergence from deep financial distress has on the quality of life in a community and the government's ability to deliver services, I am going to speak primarily about the New York City experience.

One cannot explain clearly what happened to New York after its fiscal crisis without referring, even summarily, to what got it into trouble in the first place. There is, of course, the well-understood overarching theme of New York playing the role of social service provider of last resort, with its historic free, high-quality City University, heavily subsidized 24-hour mass transit system, extensive network of municipal hospitals and generous welfare system. But what is arguably no less important is that while, the City was focused on dispensing and constantly enriching these services, its knowledge of their cost and impact was virtually nonexistent. The City was like a generous uncle who inherited a fortune and dispensed his largess with abandon, without ever giving thought to the potential limits of his fortune.

Let me explain the point by illustration. When I ran to be elected the City's Chief Financial Officer, I promised that I would for the first time in New York's history commission an independent audit of its finances. I didn't think anything was necessarily wrong, but it seemed like prudent management to obtain such an audit and for me as a fiduciary to get what lawyers call a "receipt and release," a base line accounting of what I inherited as the new Comptroller. When I sought audit bids shortly after taking office, it emerged that the engagement was so large and challenging that no one accounting firm was willing to take it on alone, so we split it among three different firms. After a few weeks, the managing partner of one firm asked to meet with me. "Mr. Goldin," he said, "have you noticed that on the 6th floor of the Municipal Building, when you get off the elevators, the corridors are lined with pasteboard boxes?" "Oh yes," I answered, "they're unsightly; I'll have them moved right away." "No, no, no," he said, "that's not the point. Do you know what's in those boxes? City checks, blank City checks, in a public hallway, where anyone can grab a handful. And they're not numbered," he said, "moreover, when you enter the large room off the corridor where 30 or 40 clerks sit filling out the checks to pay City bills – going out into the corridor to get a new supply when they run out – there are signature stamps strewn all about, with your name on them. So you've got an unguarded supply of unnumbered blank checks and freely available signature stamps. And finally, when the cancelled checks and bank statements are received at the end of the month, they are neither examined nor reconciled to the City's books." That was the first indication I got that all was not right with the City's management of its financial affairs.

But it got worse. A few days later, the engagement manager of another accounting firm asked to meet with me. "Mr. Goldin," he said, there is a closet up on the 7th floor in a room open to the public, which is also filled with dozens of clerks. One clerk sits outside the closet, haphazardly guarding it, when he's not running an errand or at lunch. Inside that closet are shoe boxes filled with several billion dollars face value of bearer bonds, City securities which are the equivalent of cash that contractors deposit at the start of a construction job to guarantee proper completion of their work. When a contractor started work on a job, he would bring the required amount of bearer bonds, which the clerk would record in a notebook. On the completion of the job, when the contractor returned to retrieve his deposit, the clerk would search the stash of bearer bonds and hand over whatever instruments seemed equivalent in dollars to the original deposit."

Now that report caused me to go into a near panic. Two floors above my office, I had just found out, were several billion dollars of virtual cash, seemingly freely accessible to anyone who passed by and decided to shove a supply of bonds in his pocket. I immediately called the Police Commissioner, who dispatched a cop to guard the cache. I spent a nervous weekend, arranging to transport the bonds to a bank. It wasn't a simple thing. The hoard was of such a size that no armored car company would take all the bonds in a single shipment because of the insurance coverage required. All weekend, while I made arrangements to move the bonds, I was in a sweat: for God knows how long, the memory of man runneth not to the contrary, the bonds had sat virtually unattended; and on my watch there would be a world-class heist. A few days later, the police closed off the street between my office and the nearest bank vault, with officers, holding guns drawn, deployed at intervals, while armored trucks holding $75 - $100 million of bonds at a time spent the afternoon going back and forth to the bank, transporting the bonds to a safe place.

That gives you a taste of how chaotic it turned out the City's financial management was. As it developed, New York was operating on an accounting system that was accrual on the revenue side and cash on the expense side, the least conservative of all possible accounting systems. The City knew it had hundreds of thousands of employees, but in fact had no exact count. I asked the head of the school system to bring me the print out of all of his employees and to be prepared to sit with me and explain what each person on the list actually did. He got through the first half dozen names when it became clear that he and his senior staff had no handle on the specific duties of their tens of thousands of employees.

So, at the heart of New York City's post-crisis recovery was a total, comprehensive revision of its accounting system (now on a modified cash basis), the creation of an integrated financial management system (whereby all accounts are automated, with no possibility of a cash expenditure unless it is supported by available cash) and the installation of a centralized, automated management information system. The City is required to construct annual budgets that satisfy the requirements of Generally Accepted Municipal Accounting Principles and to prepare rolling four-year financial plans. Annual audits generate certified statements. The upshot is that in the aftermath of its near bankruptcy, New York City's finances are transparent, professionally managed and disciplined. As a result, expenditures cannot exceed revenues and the City is impelled to live within its means, precluded from financing deficits, capitalizing recurring expenses and borrowing against fictitious receivables. This financial construct has significant social and service consequences. In New York City's case, it had to impose tuition at its formerly free university, raise the subway and bus fare, close hospitals, revise the pension structure for new employees, re-rationalize the number of firefighters who man apparatus and the number of firehouses. In a word, services had to be reduced substantially and re-thought from top to bottom. The upside is that a stable municipal financial environment has created a universe conducive to outside investment and business expansion. New York City's economy has burgeoned, with its position as a financial capital strengthened, its appeal as a creative center materially enhanced and its tax base growing steadily.

While the jury is still out on Detroit, Jefferson County, Alabama's post-bankruptcy experience is similarly encouraging, with matrixes of financial viability improving steadily. Chicago, the Chicago school system and the State of Illinois are clearly still on the wrong side of the mountain. But some recent signs are encouraging, especially the City's resurgence as a corporate capital. Still unclear is whether the political will is sufficient and the necessary coalition of public officials, unions and civic lenders can be mobilized, as a prelude to the delineation of the requisite steps for financial recovery. That involves, first, documenting definitively the magnitude of the problem; second, developing a credible multi-year remediation plan; third, formulating credible independent mechanisms for monitoring compliance; and finally, establishing service priorities around which consensus can coalesce. A tall order, to be sure; but it's all going to happen, one way or another. The question is whether it happens without the compulsion of a Bankruptcy Court or can be achieved by a herculean and heroic effort led by elected officials and public-spirited leaders and citizens of the great City of Chicago.