

May 11, 2008
FAIR GAME

Big Rescues Can Work. Just Ask New York.

By [GRETCHEN MORGENSON](#)

AS the great American credit crash continues to reverberate, we still have nothing that resembles an intelligent and comprehensive plan for dealing with mass foreclosures and the economic consequences associated with the debacle.

Democrats in the House passed two bills on Thursday that would have the government insure up to \$300 billion in mortgages to help homeowners avoid foreclosure. It would also provide \$15 billion to states to buy and renovate foreclosed properties. Prospects for neither bill are bright; the White House has promised to veto both.

Even as the housing crisis deepens, it has become fashionable to argue that the markets should be allowed to fix the problem. Doing nothing is preferable to a Washington solution, the argument goes, because lawmakers so often compound the problems they set out to solve.

And so we drift, with the usual ideological battle lines drawn. Liberals want to help borrowers, and conservatives decry anything that smacks of a bailout. Foreclosures, meanwhile, could reach 2.5 million this year, and house prices continue to fall.

Yes, this problem is maddeningly big and complicated. But America is full of smart and caring people; surely there exists a handful of wise men and women who can stow their axes and their differences to right the ship.

To that end, I spoke with [Felix G. Rohatyn](#), the financier and former ambassador to France who is vice chairman of [Lehman Brothers](#). A central player in the 1975 plan that saved New York City from bankruptcy, he seemed a good person to consult on how to approach the foreclosure mess.

The solution back then was to create an entity called the Municipal Assistance Corporation that raised money selling bonds backed by sales tax receipts and stock transfer taxes. The goal was to revive the city's economy while balancing its budget. It worked. A few years later, the budget was balanced and New York was back on its feet.

Every crisis is different, of course. And the one that pushed New York City to the brink was considerably smaller than today's. The city had \$12 billion in debt outstanding, and the upheaval was regional, not global.

Still, interesting parallels exist. Then, as now, banks had been too easy with their lending, and borrowers — city officials — thought the party would never end. The dollar was in a tailspin as it is now, and a broad-based denial of the problem's depth held sway.

Echoing those who maintain that "greedy borrowers" should get no help today, many in Washington in 1975 argued against a rescue of New York. Mr. Rohatyn recalled the spokesman for President [Gerald R. Ford](#) comparing New York City to a wayward daughter hooked on heroin. "You don't give her \$100 a day to support her habit," the official said.

IN May 1975, with the city three weeks away from bankruptcy, Mr. Rohatyn was enlisted to help it raise \$900 million. After that, the city needed \$1 billion a month for each of the next three months. Once that hurdle was overcome, it would need an additional \$4 billion in 1976.

"We did not have time for theoretical analysis," Mr. Rohatyn recalled. "What we needed was for people who had never really worked together before — and some who had antagonistic relationships — to cooperate quickly and on hugely difficult political and economic matters."

Shared sacrifice was the first order of the day. "We knew the only sources we could look to were the people who had created the problem in the first place," Mr. Rohatyn said. That meant the unions with their rich contracts, he said, and the banks, which had lent too much to the city.

After considerable wrangling and brinkmanship, city unions agreed to job cuts and a wage freeze while investing some of their pension money in M.A.C. bonds. The banks, for their part, agreed to exchange billions of dollars in short-term debt for long-term bonds.

Keeping the public apprised on the efforts to save New York was an important lesson, Mr. Rohatyn said. "I could try to lie to the newspapers about the condition of the city, but I thought it was better to tell them the truth," he said. Not easy, but certainly the right thing to do.

One of the beauties of M.A.C., Mr. Rohatyn explained, was that it was completely bipartisan. "We had Democrats working with Republicans, business working with labor; we had a virtuous circle," Mr. Rohatyn said. "It wasn't without emotion or heat, but ultimately we were all going in the same direction."

Other partnerships emerged. [Lewis Rudin](#), then head of one of the city's real estate dynasties, persuaded his industry colleagues to prepay a year's worth of their real estate taxes.

But all this collaboration met a brick wall when [Hugh L. Carey](#), the governor of New York at the time, and Mr. Rohatyn went to Washington for financial help. William E. Simon, the Treasury secretary, was against providing any aid and urged Mr. Carey to raise taxes instead.

In late October, Mr. Ford gave his infamous speech at the National Press Club, vowing to veto any bill that would provide federal money to New York. The famous Daily News headline — "Ford to City: Drop Dead" — ran the next day.

By November, however, school districts in other states were having problems selling bonds, and banks were increasingly worried about their exposure to a New York default. The turning point, Mr. Rohatyn said, came at an economic summit outside Paris sponsored by President [Valéry Giscard d'Estaing](#) of France and Chancellor Helmut Schmidt of West Germany. Mr. Ford was there with other world leaders.

"When they were told the city was about to go bankrupt, they said to Ford, 'You're going to have a global dollar crisis,'" Mr. Rohatyn recalled. Mr. Ford changed his mind.

The federal government gave the city \$2.3 billion of seasonal financing and three years to balance the budget. By 1981, the city could again sell bonds to the public.

MR. ROHATYN plays down his role in the success of M.A.C., identifying Mr. Carey as the hero of the moment: "We would have gone bankrupt under any other governor; he took the heat and the responsibility." Mr. Rohatyn said his association with M.A.C. was the most rewarding experience in his professional life.

M.A.C. saved New York City with a sound financial structure, shared sacrifice and a remarkable collaboration among adversaries. Its operations were open, not secretive. Discipline was combined with federal aid.

There was a will to do what was necessary in 1975 that is missing today.

Maybe the current problems will indeed work themselves out as many seem to expect. But to miss such an opportunity for leadership does seem a shame.

For all of us.