RELEASE OF FINANCIAL INFORMATION BY LARGE CITIES

by

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ABSTRACT

Cities and other municipalities have not been subject to the requirements of disclosure to securities investors that companies are under federal securities law. Recent events have resulted in proposed legislation to require cities to inform bond buyers about their finances and factors affecting them. This thesis discusses what kinds of information are involved, how it will be used, and what the policy implications for cities are. It presents original survey research that sheds light on these questions.

Name and Title of Thesis Supervisor: Dr. Kent Colton, Assistant Professor

TABLE OF CONTENTS

CHARTS

FIGURES

TABLES

APPENDIX I

APPENDIX II

APPENDIX III

APPENDIX IV

BIBLIOGRAPHY

I. Introduction

The U.S. Congress, underwriting banks, bond dealers, and bond buyers have discussed increased regulation of municipal securities at various times, but no legislation has been passed as of this date. Different arguments apply to a debate about regulation of municipal securites than to any type of nongovernmental securities and the consequences of regulation might be different. The practices of the municipal securities market affect most citizens. Investors may or may not care about the purposes of local government. If they were to review the functioning of a muncipal government, their judgments might be different than those of local elected and appointed officials. The financial interests of bond owners, bond dealers, and underwriters might conflict with thepersonal and financial interests of local citizens and taxpayers. It may be that municipalities should somehow continue to be protected from the disclosure, liability, and other burdens of regulation placed upon private corporations that issue securities.

Until recently, many bond owners have known almost nothing about the financial conditions of their debtors. Very few people who have ever lent municipalities money bybuying their interest-bearing bonds or their short-term interest-bearing notes have not been repaid with interest at the time expected. A relatively few people have lost money recently in municipal bonds, but these are almost the first problems since the Great Depression of the 1930's.

Municipal bonds are regulated much less than corporate securities. There are many ways they could be regulated. The one that received the most attention in the industry and Congress in 1975 and 1976 is mandatory "disclosure". As the term is used in these discussions, the word "disclosure", also used in many other reform campaigns, means that the particular entity informs interested parties or the general public, about itself and what it does. In this discussion, "municipal disclosure" means that the municipality's administrators inform the general municipal securities market or its particular underwriters, dealers, owners, and potential purchasers of its securities about its finances and other relevant information.

In the past, most municipalities did not have a disclosure policy. In the last several years, however, some degree of municipal disclosure has become common because of pressures following financial crises in a few municipalities. However, varying types and amounts of information have been released causing uncertainties for people trying to use it. There is continued pressure for a federally mandated disclosure policy and the probability that there will be such a policy is much higher, now, than ever before. The increased demand for municipal disclosure and for some sort of federal regulation of municipal securities may cause a change in the relationships of municipalities and their creditors.

Some of the important questions on regulation of municipal disclosure that are being or might be considered by Congress are:

(1) How might municipal disclosure policies affect the interest rates on municipal securities?

(2) Is it best for Congress or a federal agency to define the information that must be disclosed? If so, what information should they require?

(3) Is federal regulation of municipal disclosure polices politically acceptable?

(4) Is it necessary for local governments to conform to one standard of accounting practices in order that municipal disclosure be effective, and, if so, how could this be implemented?

(5) Who will be responsible if the disclosed material is inaccurate or incomplete?

(6) How much might disclosure policies cost local governments?

(7) Will policies of disclosure sufficiently satisfy investors so that they will continue to buy municipal bonds even if some local governments have more financial problems?

(8) What indirect effects might municipal disclosure have on local governments?

Some of the questions that decision-makers for a particular municipality might evaluate in developing a municipal disclosure policy are:

(1) If allowable, will there be advantages in limiting or expanding the scope of information that is reported compared to what has been suggested?

(2) How should information be distributed?

(3) What will the disclosure program cost the municipality?

(4) Will the policy cause political conflict?

(5) How will the information be used?

(6) Will the municipality have an advantage in the bond market if it changes its accounting practices or has more extensive or more frequent audits or employs a prestigious firm of CPA's?

These sets of questions are further developed in this thesis. The history and purpose of municipal disclosure and the potential usefulness and costs of particular information are considered. However, the narrow range of information concerning the legality and payment provisions of municipal securities contracts, the special domain of the bond counsel, are not discussed. The range of possible information that might be used to describe municipal issuers is very large because municipal bonds are issued by state governments, county governments, city governments, small town governments, school districts, utility districts, airports, port authorities, highway authorities, etc. The sources of revenues and factors affecting the security of revenue bonds and of general obligation bonds are diverse. For simplicity, therefore, most of this discussion is confined to disclosure policies of large cities to potential purchasers and current holders of long-term general obligation bonds.

The second chapter of this thesis discusses the history of the municipal disclosure controversy. The most important sources cited in this thesis are briefly described and their use further explained. The third, fourth, fifth, and sixth chapters consider information describing revenues, debt, expenditures, and nonfinancial factors, respectively. A short introduction to each of these chapters is followed by charts showing the relevant data and various reporting recommendations. The concluding chapter discusses the general policy implications of the factors considered in the body of this thesis.

A number of commissions composed of experts and influential people have suggested information to be disclosed. However, little data has been published providing insights into the perceived desire for and possible uses of such information by the municipal securities market, in general. Information selected for disclosure may be packaged in prospectus statements and annual reports. Other information is available through personal experience, by word-of-mouth, and through the general news media. As part of the reseach for this thesis, this author developed and administered three surveys: (1) a survey of "Investor Needs for Information in a Municipal Propsectus Statement", (2) a survey of "Investor Perceptions of Boston", and (3) a "Survey of Financial Officers". The results from these questionaires supplement published recommendations and their implicit theories of the purposes of municipal disclosure. Some of the recommendations of the commissions are supported while others are contradicted. New theories on using information describing cities are suggested by the survey results and developed in this thesis.

For ease of expression, two surveys when discussed in this thesis are referred to by shorter titles than those used in labelling the forms when they were distributed. The survey of "Investor Needs for Information in a Municipal Prospectus Statement" is referred to as the Indicator Survey. The survey of "Investor Perceptions of Boston" is referred to as the Perceptions Survey.

How the survey data generally supplements various disclosure guidelines and other advice given at various times and their format and distributions are explained in the last section of Chapter II. The survey data is used to critique various suggestions for disclosure of information on revenues, debt, expenditures, and nonfinancial information in the other chapters. The survey results are cited as sources throughout the thesis. All of the results are not discussed together in any one section of the thesis. However, the cover letters, survey forms, and tabulated results of the Indicator Survey, the Perceptions Survey, and the Survey of Financial Officers are included in Appendix I, Appendix II, and Appendix III, respectively. Appendix IV includes the major disclosure recommendations cited.

II. History of marketing and regulation of municipal securities and of recommended changes in disclosure and analysis practices

Why have investors bought and traded municipal securities while knowing very little about their issuers? Why is this currently a subject of concern? Of the reasons that municipal securities were marketed without full disclosure, which still apply and what are new factors? What recommendations have been given and how have they been received? What questions remain unresolved and what contributions does this thesis make towards their resolution?

This chapter is concerned with these questions and discusses them in an historical context. In historical order, proposed legislation to regulate municipal securities information release and analysis and studies making disclosure recommendations used in Chapters III, IV, V, and VI are described. The most recent evidence used in this thesis -- the results of three surveys by the author -- is explained. This chapter has nine sections: (A) The early history of municipal bonds and the development of federal securities regulation, (B) Established market procedures, analysis standards, and rating of municipal bonds, (C) Disclosure advice prior to 1975, (D) SEC involvement prior to 1975, (E) Two municipal financial crises that spurred interest in regulation, (F) Responses to the UDC and the NYC financial crises, (G) SEC involvement after 1975, (H) Technical questions in municipal disclosure policy development that are related to accounting, auditing, and liability assignment, and (I) Description of the survey research.

A. <u>The early history of municipal bonds and the development of federal securities regulation</u>.

Municipal bonds are promissory notes that enjoy exemption from federal income taxes and most local taxes. They were developed as a vehicle to distribute the cost of needed public facilities over the time of their use and among transient populations. Their tax-exempt status serves to lower the interest costs municipalities must pay.

Throughout the history of the United States, banks and other capital investment organizations have financed the development and expansion of towns and cities. Banks made large loans to finance the development of ports, railroads, mines, and other private enterprises. To help those investments succeed, the banks made loans to enable city and town governments to build roads, schools, and other public facilities needed by people and industry.

If a bank made commercial and municipal loans in only a dozen towns, the loan officers could become familiar with the characteristics of the populance, economy, government, and the political and business leaders. However, as the capital markets increased in sophistication, there were advantages for the financial institutions in making loans to a greater diveristy of municipalities and private firms. Because it facilitated management, bankers traded loan contracts among themselves. This trading increased the need for formality and made it more difficult for the banks to keep track of their clients.

Investor services assigned ratings to municipal and private bonds, which served to facilitate marketing. According to one rating critic:

> "Moody's began rating bonds in 1919, Standard & Poor's not until 1950. Until the Great Depression, Moody's rated most issues Aaa or Aa... (In the) pre-Depression days when the rule of thumb was the number of railroads passing through a town. One railroad called for a single A, two for Aa, and so forth."/ 48, p. 85 /

The "railroad rule of thumb" did not show which municipalities' securities were the most risky to buy. In the 1930's, 78% of municipal bonds that defaulted were rated "triple A" or "double A" at the time. / 49, p. 135 /

The boom of the 1920's and the Depression of the 1930's showed the need for order in the investment markets. Fortunes were lost in fraudulent schemes and it was impossible to estimate the risk of many investment possibilities. The powerful provisions of The Securities Act of 1933 and The Securities Exchange Act of 1934 are the bases of federal regulation of most securities investments.

Before corporate securities are distributed to the public, The Securities Act of 1933 generally requires complete and accurate disclosure of: the identity of, and renumeration to, the directors, principal officers, and underwriters of the issuer; the identity and holdings of major stockholders; the most recent financial statements and material contracts of the issuer; the proposed use of the funds to be acquired through the issue, underwriting agreements, and other information relating to the issuer. This disclosure is to be made in a registration statement that must be filed with the Securities and Exchange Commission (SEC) and in a prospectus that must be furnished to securities purchasers. Other provisions of the 1933 and 1934 Acts provide penalties for fraudulent and deceptive practices, set other business standards, and require SEC registration of brokers. / 37, p. 569 /

Municipal securities, banks, and broker/dealers effecting transactions only in municipal securities were exempt until 1975 from all substantive provisions of the 1933 Act and subsequent securities regulation and legislation except for very general "antifraud" provisions. All the SEC rules involving fraud included municipal securities transactions. However, only dealers who also dealt in corporate securities were forced to register with the SEC and keep records following SEC standards. If the SEC discovered that registered dealers were behaving fraudulently, it could easily stop the offending actions. The Commission has authority to investigate violations of The Securities Acts by registered dealers, and through administrative proceedings, to discipline them by suspension or revocation of their registration, which could force the firm into bankruptcy. [44, pp. 2043-2044] Although the SEC staff could try to prove that the firm had acted fraudulently, it did not need to do so to discipline a registered dealer. Effective discipline could be applied if the SEC could prove that the firm had violated SEC administrative rules.

If an unregistered dealer or municipal securities issuer were behaving fraudulently, possibilities for legal recourse were much different. Unregistered dealers in municipal securities who behaved fraudulently had a smaller risk of being caught and punished. They were not forced to file or keep records that could be used as evidence. The SEC could not review their cases in administrative hearings, nor punish them by suspending their licenses, as no license was required. If dealers' fraudulent actions were discovered, the SEC could prosecute them in civil court for violations of statutory laws or private citizens could sue them for damages on various grounds. When unregistered dealers were discovered behaving illegally, the SEC could charge them with violating the "antifraud" provisions of The Securities Acts of 1933 and 1934. As discussed later, in 1975 much controversy developed in the legal system about whether some evidence of deliberate fraud is necessary for the "antifraud" provisions of The Securities Acts to apply or whether negligence and reckless actions are sufficient grounds. Until 1976, the SEC never brought suit against a municipality (which are never required to register with the SEC) under those provisions of The Securities Acts.

The administrative differences in regulation of municipal securities and other securities were not part of a carefully analyzed policy. In fact, as The Securities Act of 1933 was originally drafted, municipal securities were not exempt from any of its provisions. /_44, p. 2044_/ In the Hearings for the Bill, the President of the New York Society of Certified Accountants testified in favor of the original version and argued strongly that municipal securities investors needed more information than was usually available. This was successfully countered by extensive testimony that full application of the Act to municipal securities markets would unduly burden the securities industry and impair the fund raising abilities of municipal issuers. /_37, p. 570_/ At the last minute, the Bill was redrafted so that municipal securities "were made exempt for obvious political purposes". /_44, p. 2044_/

If some aspects of the credit extended to municipalities had been brought under regulation in the time of securities reform following the stock market crash and the Great Depression, later events might have been different. A resolution of conflicts between the interests of investors and municipalities was not even begun. One lawyer who had counselled a bankrupt municipality wrote in 1935:

> "If individual bond holders are permitted to bring individual mandamus proceedings, the going value of the municipality will be seriously reduced and there will be no hope for a settlement short of a time when the municipality, by resort to devices like the appointment of assessors on a platform of resignation or residence in jail for contempt or like the legislative abolition of the municipality and the substitution of another, or like the separation of the tax roll into two, one for current expenses and the other for debt service, beats the creditors to their knees so that all are willing to get together on a reasonable settlement." /_13, p. 44_/

Because the question of regulation of municipal securities was dismissed without resolution in the 1930's, great uncertainty persists as to the rights of the city, its citizens, and its creditors -- not only when it is bankrupt but also when it is financially sound.

In the years following The Securities Acts of 1933 and 1934, there was a great deal of abuse of the municipal securities market by individual dealers. As personal incomes increased, the tax-exempt feature of municipal bonds attracted more non-institutional investors. Some municipal securities dealers were able to take advantage of some investors' lack of sophistication by using methods the SEC prohibited private securities dealers from using. Unqualified commission salespeople used high pressure to sell revenue bonds issued by small, unknown, and mismanaged municipal corporations and other low-quality, high-risk bonds. Sometimes they said that a quick purchase was best because the bonds were in short supply or that the sellers had to take a loss in the sale because they had immediate personal needs for cash. Sometimes they misrepresented the sources of funds for repayment of bonds. Some firms inflated the prices or substituted for the bonds actually ordered by their customers. [37, p. 571] As discussed earlier, when fraudulent behavior by municipal securities dealers was discovered, some private citizens sued for damages, and the SEC prosecuted others in court. However, it was obvious that many people had been cheated by firms that were never prosecuted.

B. Established market procedures, analysis standards, and ratings of municipal bonds.

Although they have recently changed somewhat, the following procedures have been used to market municipal bonds since the Great Depression. When a municipality had special cash needs, its financial officers first consulted with a bond attorney and sometimes with other financial experts. They helped the municipality's financial officers to check the procedures for authorization of the bonds. These usually involved voter approval of tax-supported general obligation bonds, or a pledging of cash streams from a particular project, such as a toll bridge, for revenue bonds. The bond attorney and financial consultants helped to decide exactly how much money was needed, whether the bonds should be repaid serially or all at one time, and whether the bonds should pledge the "full-faith-and-credit" of the municipality and its taxing powers.

Banks usually bid competitively on the bonds, and the municipalities sold the bonds to the bank charging the lowest interest. When the bonds were sold in large volumes they were usually bought by bank syndicates (groups of banks bidding together). If not enough banks bid competitively, a negotiated sale was arranged. That is, municipal officials arranged bond terms with a bank that had a special interest or knowledge of the municipality. In either case, independent dealers or dealers affiliated with banks sold the bonds to individuals and organizations. Underwriting banks and dealers both took a commission.

Before the sale, the municipalities notified Moody's and/or Standard & Poor's, the most prominent rating agencies, of their intentions. Initially, municipalities were not charged for having a rating assigned to their securities. To increase profits, the rating agencies began to charge the municipalities in the 1960's. Even though ratings are a service to the investors, they had become so necessary for successful sales that practically all municipalities subscribed. The agencies gave the municipalities a list of information to provide for their first ratings which municipalities were required to update. The rating agencies usually reviewed each issuer once every three years, although they could change a rating whenever they wished. The rating applied to all outstanding securities of that issuer. A bond might receive a different rating from Moody's and from Standard & Poor's and each agency used a slightly different format.

Use of the rating services was convenient for most municipalities even though those receiving low ratings were hurt. Financial officers merely had to gather stacks of information and mail them to the rating agencies. They did not have to summarize or specially prepare the material. The rating agencies did not require an independent audit. They did not always verify the accuracy of the material they received. [37, p. 586] Because the rating agencies usually assigned only one analyst to all the issuers from a state, there was little time for extensive follow-up meetings with the municipal financial officers.

Before the sale municipal issuers distributed offering circulars with very little detail, unlike those of private issuers. The notice of sale and prospectus statement which accompanied municipal bonds and notes were generally one to four pages long. Most of the statement was devoted to a description of the bond itself and was prepared by the bond attorney. There was almost no information about the finances, government, population or local economy of the issuer. The rating and reputation of the bond attorney in national investment circles were very important in determining the interest rate.

The costs of the bond rating, bond notice, and the prospectus were a very small part of the expenses of marketing general obligation bonds. A survey by the Municipal Finances Officers Association (MFOA) of 481 local governments found that the average expense of marketing municipal bonds was composed of the following costs:

	Marketing costs per $1,000 in bonds ($)	Cost distribution (%)
Special Election Costs	1.25	12.7
Legal and Financial Fees	2.02	62.7
Fiscal Advisor	-	(31.5)
Bond Notice	.06	2.5
Prospectus	.10	3.3
Printing of Bonds	.20	8.5
Bond Rating	.09	2.7
Other Costs	.08	2.7
	3.80	

/¯54, pp. 135-136_/*

The total of these costs for marketing when the bonds were issued was less than the interest costs that municipalities usually pay for each year they are outstanding. The differences in interest rates was caused by many factors including: capital market interest rates, size of the bond issue, volume of the bonds issued by other municipalities at the same time, special securities attached to the bonds, reputation of the issuer, and the rating assigned by the agencies. If the municipality could influence these factors so that it could borrow at lower interest, it could achieve considerable savings. Although not a standard procedure, some municipalities would make presentations to the rating agencies to convince them to upgrade their securities, often resulting in the underwriters' increased willingness to bid at lower interest rates. Some municipalities hired financial consultants who could maintain trained staff to advise them on these factors. One financial consultant said that he could sometimes influence the rating agencies in their evaluations. /¯23_/

If a municipality were downgraded, the voters might blame its administrator. However, other political costs to the administration were minimal

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* as reported by Steiss. This information is useful in comparing marketing costs to evaluate market strategies. However, the data reported is flawed because the year in which the survey was taken was not reported and because the distribution (%) figures do not reflect the "cost per $1,000" figures.

under the standard process in which bonds were marketed with minimal disclosure and ratings assigned by the private investor services. Information given to the rating agencies is supposed to be confidential. Standard & Poor's Corporation released a statement that:

> "...information received as part of the bond rating process which has not been publicly disseminated is to be strictly limited to the parties involved in the bond rating process, and under no circumstances will it be available to any person outside of the department." [60, p. 32]

If the information given to the rating agencies were publicized, it might be used as evidence for criticism of the municipality's administration.

The ratings are, and were, convenient tools for the marketing of municipal bonds. Unlike underwriters of corporate securities, who carefully analyze all of their purchases, underwriters of municipal securities win an average of only 24% of their bids, [59, p. 126] so a thorough analysis of all their potential purchases would be very time consuming. If purchasers were going to buy only a few bonds, they could examine a selection in a certain range of interest with acceptable ratings for their purposes and decide on the basis of the convenience of maturity dates. A bond dealer could bring to a potential purchaser a dozen of the short notices of sale and discuss them in one appointment. Although the investors could have considered expensive limited circulation reports compiled by the rating agencies, few did. [23]

Use of the rating services of municipal bonds was further strengthened by bank regulations and common law. Federally insured banks are not allowed to buy municipal bonds unless they are rated at least Baa (or BAA). Bank officers and others administering the investment of funds in trust are held to have a "fiduciciary responsibility". Their investment purchases must be of a certain quality to legally satisfy their obligation. The ratings of Moody's and Standard & Poor's can be used as evidence of the quality of municipal bond purchases. Even if the bonds were to default, the trust managers who bought highly rated bonds would not be held personally, legally responsible. /‾40_7 Use of the letter ratings made it generally easier to establish standards for bond purchases. They could be used to describe a portfolio of bonds. For instance, pension managers could assure employees that they were taking good care of their money because they bought AAA and AA rated bonds.

The dependence of the municipal securities market on the two profitable, privately owned rating agencies for bond evaluation became institutionalized for many reasons, including convenience for busy municipal administrators, underwriters, bond dealers, and final purchasers and use of the ratings to describe portfolios and allowed investment decisions by trust managers.

The rating agencies have never reviewed the standards that they use to determine what rating a bond should receive. However, in 1941 a panel of fifty experts in municipal finance was asked to rate a list of criteria as to effect on the soundness or unsoundness of the finances of any municipality. Those criteria were then applied to twenty-five randomly selected cities and their results correlated highly to Moody's ratings. /‾48, p. 85_7 These results support the theory that, if analysts have access to the necessary information, they can assess the "quality" of a bond as well as Moody's and the other rating agencies.

The purpose of municipal credit analysis has been obscure. A bank vice-president wrote to the Treasurer of Boston that, "The purpose of municipal credit analysis is not to be able to predict default. The objective is to be able to rank bonds according to a limited set of criteria...Quality is a relative thing measured across a spectrum." [18] A statement by a small service for investors defined the "aim of credit analysis" differently as being "(A) Evaluate the ability of the issuer to pay its debts, (B) Evaluate the willingness to pay debts, (C) Determine whether there are significant features of weakness which may lead to trouble in the future, and (D) Assist in comparisons of one issuer with another -- to place the credit in a category as to quality." [60, p. 36]

If investors buy a municipal bond to hold it until maturity, their only risk is of default. Many institutional investors, however, have found that they can maximi e profits by trading bonds on the secondary market where prices are affected by many factors including general capital market movements and changes in ratings. They assume a risk of market loss.

Some investors speculate, trying to outguess when the rating agencies will change a rating. If bonds are bought on the secondary market before the rating is upgraded, the bonds can often be resold for a higher price. Analysis of bonds' potentials for price movement in the trading market is different than analysis of the risks of default.

In 1968, Rabinowitz described his experiences with quality analysis of municipal bonds:

> "This writer has been privileged to work for a number of years as an independent consultant to major investors in municipal bonds who have been willing to take the trouble to set up their own systems of identifying those bonds of high intrinsic quality that have equally high possibility of being either upgraded or downgraded. It is a terrible chore to handle the incredible mass of statistics concerning the 'objective' facts concerning municipal finance and urban development; the statistics themselves are often obsolete, aggregated in difficult ways, and incomplete, reflecting the diversity of our federal system and the neglect of urban research in our past, but the <u>dollar rewards</u> of an improved intution concerning how the rating services may rate or reclassify certain types of communities, given certain changes in underlying characteristics of the local economy and its populace, can be substantial." [48, p. 80]

Most purchase decisions are, and where, made without the benefit of detailed analysis such as that described by Rabinowitz. It is not known to what extent investors and other participants in municipal securities wanted to do detailed analysis. It is clear that, although many banks had special divisions to handle the purchasing and dealing of municipal bonds, few insitutionalized a municipal credit analysis function. In fact, survey results submitted to the Senate in 1976 show that 53 out of 87 investment banking firms, commercial banks, and property and casualty insurance companies with municipal portfolios had no full-time municipal credit analysts. /_63, p. 271_/ Furthermore, although the libraries of several prestigious business schools carried extensive works on analysis of private securities, they carried no works on analysis of municipal securities.

Independent municipal credit analysis has been hampered by these problems:

(1) The necessity to dig for information. Most municipalities do not distribute it and the rating agencies do not avail it to others;

(2) Difficulties in comparing financial information. The data vary because of accounting practices, government structures, and services offered;

(3) Difficulties in comparing non-financial information. Much of the data was collected by local agencies in irregular years using incompatible definitions, area boundaries, and statistical and sampling techniques;

(4) The lack of a consensus on the purpose of such analysis and on how it should be done; and

(5) The lack of a policy by institutional purchasers to retain municipal credit analysts and to take their advice.

C. Disclosure advice given prior to 1975

In practically all capital markets, except that of municipal securities, many people are employed and great attention is paid to evaluating the "intrinsic value" of securities and their potential for increasing or decreasing in trading price relative to similar securities. The idea that very little analysis is done of municipal securities is troubling, despite the convenience of the ratings. Several prestigious study groups have advised municipalities to give investors certain types of information that would facilitate analysis. In Chapters III, IV, V, and VI, their recommendations are compared and evaluated.

In 1951 Dr. Frederick L. Bird, research director of the municipal department of Dun & Bradstreet and a member of the Mayor's Committee on Management Survey of New York, pointed out the potential public realtions advantages of disclosure for the City of New York:

> "It is necessary to understand, and have consideration for, the investor's point of view; to determine what he wants to know, and properly should know, about the city financial affairs; to provide such data in readily understandable form... Each sale should be preceded by publicity designed to give potential bidders and investors adequate notice and also pertinent, up-to-date financial information well presented as to attract special attention. Thus, the prospectus should go to a comprehensive audience well in advance of the date set for receiving bids, and in a few pages should present as clearly, simply, and effectively as possible not only basic financial statistics, but data on the various important security factors that govern the issuance and administration of the city's debt. The opportunities for strengthening the city's financial standing that stem from such a statement, if skillfully prepared, are great."
> [1, p. 36]

Dr. Bird's comments were contained in a report (hereafter referred to as the "1951 New York City Report") which also gives a description of the minimum information to be reported on the community, financial trends, tax detail, fund assets, bond principal maturities, finances of overlapping units, etc. [1, p. 37] (See Appendix IV, Table A-IV 2)

In 1946, 1955, 1958, and 1963, the Investment Bankers Association published guidelines for bond prospectus statements (hereafter referred to as the "1963 IBA Format". [1, p. 38] It suggested a standard format for general obligation bonds with information on property valuations, bonded debt, overlapping debt, unfunded debt, sinking funds, debt service requirements for the next five years, comparisons of operating revenues and expenditures, property tax collections, and general tax information. [1, pp. 64-66] The format suggested for issuers of general obligation bonds is only three pages long but much more detailed than most offering circulars which have been distributed. (See Appendix IV, Table A-IV-2)

In 1964 The Advisory Commission on Intergovernmental Relations, a prestigious standing committee with members including mayors, state and federal congressmen, a governor, and the Secretaries of HEW and the Treasury, did a thorough study of various problems in municipal finance. The Commission published a report in 1965 called State Technical Assistance to Local Debt Management (hereafter referred to as the "1965 State Technical Assistance Report"). In this report the Commission recommended that states design programs that would develop and maintain state files on local debt and related data, disseminate data on local government finances, and prescribe minimum standards for official statements on local debt offerings. The Commission recommended information to be included in a notice of sale and information to be included in an official statement for appraising bond offerings (i.e. prospectus statement). [1, pp. 37-43] (See Appendix IV, Table A-IV-3)

Administration of Local Government Debt, a textbook by the Director of Finance of the City of Philadelphia, Lennox Moak, which was published in 1970, elaborated on standards for reporting on debt which had been given by the National Committee on Governmental Accounting, Auditing, and Financial Reporting (NCGA). The investor, he suggested, is interested in "(A) the ability of the government to meet the payments of principal and interest upon its debt, (B) the willingness of officials to use their powers to service the debt, and (C) the record of the community in debt and other financial management."

Moak's text suggests that fund and combined statements be given for the balance sheet, revenues, cash receipts and disbursements, delinquent taxes receivable, and a schedule of investments. It also suggests reporting the schedule of bonds payable, by type of security pledged, and the balances of sinking funds, debt service funds, and other reserve funds. The NCGA has recommended statistical trend data for ten years for the following: expenditures by function, revenues by source, tax levies and collections, assessed and estimated actual value of taxable property, property tax rates and tax levies for all overlapping governments, special assessment collections, ratio of annual debt service expenditures for general bonded debt to total general expenditures, and the schedule of revenue bond coverage. The NCGA also recommended reporting figures for debt service requirements until maturity, the value of outstanding direct and overlapping debt, and the legal debt margin. The NCGA has also recommended a list of miscellaneous data items of which Moak suggests that the most important information is the following: a description of the general government organization, its physical improvements and numbers of employees, and a distribution of the property tax roll by type of property with names and assessments of the largest taxpayers. Furthermore, the NCGA and Moak suggest that population trends, the bases of the economy, and per capita and personal income of the residents are important to the investor.

The information listed by the NCGA and by Moak is much more extensive than that suggested by the 1951 New York City Report, the 1963 IBA Format, and the 1965 State Technical Assistance Report. Those recommendations were designed for information to be distributed to bond purchasers in an official prospectus. Moak's recommendations did not assume prospectus reporting. He suggested disclosure by releasing that information to the rating agencies, financial journals, the U.S. Census Bureau, banking commissions and state insurance departments, principal banks in the region and in the nation's financial centers, investment banking firms that have bid on the issuer's securities, associations of investors, the IBA, the MFOA (Municipal Finance Officers' Association), the bond counsel, taxpayer associations, and various state and local government agencies. /_27, pp. 444-446_7

Most municipalities ignored the advice of the 1951 New York City Report, the 1963 IBA Format, the 1965 State Technical Assistance Report, and that of Moak. In general, they continued to release the short notice-of-sale bulletins when selling bonds. They prepared annual reports but did not design them for use by the bond investor.

D. SEC involvement until 1975

Over the years, various federal legislation has been passed that helped to clarify and espand The Securities Acts of 1933 and 1934 as they applied to regulation of corporate securities. However, municipal securities retained their exemption from all of the securities regulations except the "anti-fraud" provisions. The SEC's main administrative powers in municipal securities regulation were over municipal bond dealers who also dealt in corporate securities. The SEC made very clear the hard-line approach it would take towards municipal securities if it had more authority. Its position was stated in a 1967 SEC administrative prosecution of a dealer in both municipal and private securities:

Walston & Co., Inc., and Harrington CCH Fed. Sec. ., Rep. 77, p. 474 (SEC 1967)

> "It is incumbent on firms participating in an offering and on dealers recommending municipal bonds to their customers as 'good municipal bonds' to make diligent inquiry, investigation, and disclosure as to material facts relating to the issuer of the securities and bearing upon the ability of the issuer to service such bonds. It is, moreover, essential that dealers offering such bonds to the public make certain that the offering circulars and other selling literature are based on adequate investigation so that they accurately reflect all material facts which a prudent investor should know in order to evaluate the offering before reaching an investment decision. The offering circular used by the registrant in this situation fell far short of this standard of disclosure."/_44, p. 2046_/

In 1972, the Securities Industry Association (SIA) recommended limited federal administrative regulation of the municipal securities industry. /_44, p. 2048_/ The SIA proposal was debated in Congress and in Congressional Hearings from 1972 to 1975, when The Securities Acts Amendments of 1975 were passed. The SIA had specifically suggested in 1972 that an entirely new, self-regulatory body for the municipal securities industry be created with a limited oversight power vested in the SEC. The extensive discussion of the proposed legislation presented an opportunity to suggest mandatory municipal disclosure, but it was not taken because of bureaucratic conflict.

The SEC had responded to the SIA proposal with a recommendation that all brokers and dealers as well as banks be included under the regulatory provisions of The Securities Acts of 1933 and 1934. The Dealer Bank Association, a trade organization representing 130 commercial banks who were underwriters and traders in all forms of public securities, proposed that existing bank regulatory agencies be given expanded regulatory powers over the banks acting as dealers in municipal securities. The banks preferred to be regulated by agencies with which they had already developed a rapport than by the SEC which has had no authority over banks. The banks suggested that the same regulations be imposed by the SEC on independent dealers and by the several bank regulatory agencies on bank dealers.

Two important compromises evolved when this legislation was developed, which limited the expanded powers of the SEC. The first compromise limited the SEC's authority over municipal securities dealers. All banks and other brokers and dealers in municipal securities were required to register with the SEC. The Municipal Securities Rulemaking Board was established as part of the SEC but given a separate board of directors and a fair degree of administrative independence. The MSRB was required to adopt rules regarding professional standards, prevention of fraud, inspection of dealer records, etc. The bank regulatory agencies were given primary enforcement over dealer banks like the Dealer Bank Association had suggested. [44, p. 2048]

The second compromise, which also conflicted with the SEC's position at that time, concerned information requirements for municipal securities. Central to the thrust of regulation of securities to protect investors is examination and regulation of information given to investors about the security. This is the strongest point of The Securities Act of 1933 and of SEC regulation of private issuers. Yet a witness representing the Municipal Finance Officers Association (MFOA) at the 1974 Hearings on this legislation stated that he had learned, while working previously in cooperation with the staff of the SEC, that in the "real world" any requirement imposed upon dealers to provide a customer with information was tantamount to a requirement imposed upon the issuer. The witness supported an amendment to the Bill that would have prohibited any requirement that an issuer or a dealer supply information concerning the issuer of a municipal security to a purchaser or to a prospective purchaser. [44, p. 2051]

In response to this testimony and other pressures from the representatives of municipalities, Senator Williams and Senator Tower introduced an amendment to the bill that prohibited the Securities Rulemaking Board from imposing standards of disclosure on state and local units. /‾63, p. 215_/ Section 15 B (d) of the 1975 Amendments to The Securities Act reads:

> "The Board is not authorized under this title to require any issuer of municipal securities, directly, or indirectly through a municipal securities dealer or otherwise, to furnish to the Board or to a purchaser or prospective purchaser of such securities any application, report, document, or information with respect to such issuer: Provided, however, that the Board may require municipal securities dealers to furnish to the Board or purchasers or prospective purchasers of municipal securities, applications, reports, documents, and information with respect to the issuer which is generally available from a source other than such issuer. Nothing in this paragraph shall be construed to impair or limit the power of the Commission under any provision of this title." /‾44, p. 2053_/

Interestingly, the senators who proposed and backed this amendment were the same senators who proposed and backed a bill in 1976 mandating municipal disclosure.

At the time of the amendment, Senator Tower stated on the Senate floor that its purpose was simply to clarify "that the (Securities Acts Amendments of 1975) bill is not intended to tamper in any way with the prerogatives of state and local governments in their sale of securities". /‾44, p. 2061_/ Since that time, the validity, implications, and wisdom of the amendment have been questioned.

E. <u>Two municipal financial crises that spurred interest in regulation</u>

Two large municipal issuers, the New York Urban Development Corporation and New York City, defaulted bringing renewed consideration of municipal securities regulation, particularly of mandatory disclosure.

The Urban Development Corporation (UDC) was a special public development corporation created to build low-income housing and other public projects in the State of New York. It financed its projects with "moral obligation bonds which it issued several times a year to fund the rapid pace of construction. The bonds were actually housing revenue bonds made more attractive by attaching to them the "moral obligation of the State of New York". John Mitchell, a bond attorney who later became U.S. Attorney General under the Nixon administration, designed the enabling legislation for the bonds, providing that in event of depletion of a reserve of a year's debt service requirements, the legislature would be notified and would apportion funds. Although the legislature understood at that time that it would never be obligated to appropriate funds, some people in the bond market misinterpreted the statute. [36, pp. 3-6] The moral obligation feature of the bonds was very innovative -- because they were not general obligation bonds, they did not require voter approval; because they were not plain revenue bonds, close scrutiny was not given to the flow of funds from the projects.

The UDC was funded by bond proceeds and by the rental income from the housing projects. Of the total UDC housing units, 90.4% were dependent on non-guaranteed federal housing subsidies. This rental income was needed to repay the bonds and to maintain the facilities. The official statement accompanying the UDC's Series A 1971 and 1972 bond issues stressed the informal understanding with HUD officials about continuing subsidies.

Warning signals of the UDC's financial troubles first appeared in early 1973. The finance director had resigned, complaining that agency wide and individual cash-flow projections had not been prepared on a regular basis and that those available covered only short-term cash requirements.

Later in 1973, the UDC's auditors were unable to express an opinion as to the accuracy of the accounts with respect to fee income, project costs, and mortgage loans. /‾36, pp. 141-144_/

The usual underwriter of the UDC's bonds, First Boston, did not know what to do when it received the draft of the 1973 audit. It seemed that the UDC might have trouble repaying outstanding bonds unless the State of New York contributed funds. The bank lacked the understanding of state politics to know whether the State would honor its "moral obligation". If the bank were to refuse to underwrite the new bond issue, the UDC would have more problems meeting immediate debt service demands on outstanding debt. Because of the UDC's rapid expansion and the cutback in federal housing subsidies, it used proceeds from new issues, intended for new construction, to repay outstanding bonds, although this was unethical and risky. Without more bond proceeds, the risk of default on outstanding bonds would have been increased. If the rating agencies downgraded the UDC when they reviewed the damaging audit, the market risk would have been increased. This would have reflected badly on the bank.

The bank responded to this difficult situation by agreeing to market the bonds and by insisting on disclosing the situation so that the bank would not be held responsible. Paul Miller, the President of First Boston, has been quoted as saying:

> "I want you to go up to the UDC and I want you to pull out every piece of dirty laundry that you can possibly find. I want you to hang it all out in the official statement. We want everything made a matter of public record and then we will see what value the market place will put on the moral obligation with this kind of disclosure in it." /‾36, p. 145_/

The "dirty laundry" was in a special section called "Summary of Certain Financial Considerations and Risks" in an official UDC offering statement accompanying bonds offered in May, 1973. This was circulated by the dealers without review by any state officials with the exception of the New York State Comptroller, who ignored it (state review of offering statements was not customary). It was clear to the underwriting bank that the State Legislature was not aware of the UDC's financial condition. However, there was little communication between the financial community and state executive leaders.

There was almost no market reaction to the damaging prospectus. Investors continued to rely on the moral obligation feature and purchased bonds of the new issue at a very low interest rate. Moody's retained the UDC's "A" rating.

When the UDC financial problems became better known because it finally defaulted, many purchasers of the 1973 bond issue complained that the dealers had never shown them the prospectus statement which contained evidence of its financial problems. Although the SEC requires that dealers show the prospectus statements of private securities to the final buyers before the purchase, it does not have authority to require the same for municipal securities. Because detailed prospectus statements were so uncommon when municipal securities were issued before 1975, buyers might not have known to ask for one.

The Moreland Commission as appointed to investigate the UDC scandal. The Commission, which included industry representatives, acknowledged that although many investors and the rating agencies had understood that the federal housing subsidies might not continue and that the State of New York was not legally obligated to fund the UDC's deficits, they had not questioned the security of the bonds until it was too late. The Moreland Commission recommended increased disclosure as a way to insure sound financial practices and to restore the confidence of investors. The panel felt that if the UDC had regularly delivered detailed financial statements to bond purchasers, investor pressure would have kept the UDC from expanding its operations to such a risky point. [36, p. 30]

The UDC crisis may have contributed to the reluctance of banks in 1974 and 1975 to buy NYC bonds by raising doubt about the value of the city's bond ratings and the financial support of the State. For years the budget deficits had been a subject of NYC mayoral campaign discussions. Until the UDC situation, however, the banks had been willing to buy the City's frequent and large debt offerings. Usually, the banks located in NYC negotiated together with the City and were able to distribute part of the bonds outside the State. For the first time, the bank leaders told the City's financial officers that the market for NYC bonds was saturated.

The City had no choice but to continue to try to sell its securities. The bank officers tried to find out more about the City's finances. However, the City's administration was unable to give the bankers consistent and reliable information about its cash-flow and numbers of employees. [15]

The high interest rates that NYC was forced to pay on the securities it managed to sell during this time placed further strain upon its budget. Its cash shortage (caused by many factors) made it difficult to repay all of its bonds and notes that came due in 1975 and it suffered a series of near-defaults and declared a moratorium on repayment of an outstanding short-term issue. The uncertainty about the security of its bonded debt has been prolonged and caused a great deal of confusion. Even managers of NYC employee pension funds thought that the city's bonds were too risky, although they bought them anyway to avoid increased layoffs of public employees. The possibility of legal bankruptcy was extensively discussed and the inadequacies of municipal bankruptcy law were again realized. The City's situation was somewhat resolved without formal bankruptcy proceedings. The federal government made emergency loans to the City. [15] The City's financial administration was removed from elected officials and put under an appointed board with financial experts. This management corporation, "Big M.A.C.", substituted its bonds for those of NYC and secured them by liens on the City's tax revenues. It was hoped that investors would place more trust in the management of "Big M.A.C." then they did in the City's elected officials.

In the Senate Hearings on aid to New York City, Lennox Moak, municipal finance expert and Director of Finance of the City of Philadelphia, tried to make clear the distinction between municipal bankruptcy and default.

> "Potential bankruptcy -- When a corporation's financial affairs are in such a difficult condition that a thorough reorganization of these affairs is a prerequisite to its continuance as a viable organization and when such reorganization can be effected only under the protective wing of superior legal process that allows time and freedom from harassment, we must recognize that one is confronted with a de facto temporary bankruptcy -- the NYC situation currently.
>
> Potential default -- A default consists of an impending temporary inability to meet obligations as they fall due. This can occur to corporations which are in basically sound financial condition but which are temporarily unable to secure orderly access to capital markets for external reasons that have little relationship to basic financial strength." [62, p. 96]

If the Big M.A.C. solution and the federal loans had not been possible, a full bankruptcy of New York City would have had disastrous consequences. The City had already cut back on some "vital services" by closing some schools and fire stations and by reducing the size of its police force.

Even without bankruptcy proceedings, national and international capital markets were shaken. Part of the attention was due to the importance of New York City and the volume of its outstanding debt.

It is easy to see how a form of panic can build up in such situations because of damaging and inconsistent statements from people with conflicting personal interests. The administrators of NYC, for instance, had to claim that the City was financially sound when they knew it was not so that it could continue to borrow. They also had to claim that the City was in desperate financial trouble, to impress upon the state and federal governments the urgency of its requests for aid. Each mayor and comptroller needed to criticize the others to try to save his personal credibility as the contradictory claims became more obvious and the deficit more difficult to manage. When the City sold a RAN issue at a very high interest, the comptroller said in a press release that it was caused by "...the City's ever-increasing cash needs which have necessitated extraordinary borrowing by the City and every expectation of a continuing need for high borrowings." [15, p. 152]

F. Events following the financial crises

The UDC and New York City financial crises incited a flurry of activity and reactions from the market, the news media, the President, and Congress. Interest rates on all tax-exempt securities went up, and many cities claimed that they were unable to enter the bond market at all. In the Senate Hearings on federal loans to NYC, the President of Standard & Poor's Corporation said:

> "There has been a massive erosion in the value of municipal securities nationwide far out of proportion to the actual risk. This adverse market psychology has caused many bond issuers to pay abnormally high interest rates." [62, p. 305]

A bill similar to the 1972 proposals of the SEC was proposed by Senator Eagleton. This bill would have required municipal securities dealers to register, file regular statements with the SEC, and comply with all other provisions of The Securities Act of 1933, but it received little attention. There are more municipal issuers than there are private issuers, so the SEC would have had to expand greatly to handle the extra work.

Another bill which deals with municipal disclosure has received much more attention. The 1976 version of the Williams-Tower Bill (S. 2969 of the 94th Congress) would require the SEC to set forth the accounting methods to be followed in the preparation of financial statements, but it does not contemplate or permit direct regulation of municipal issuers through registration, waiting periods, or the filing of sale documents with the SEC. [63, p. 14] The bill (herafter referred to as the "1976 Williams-Tower Bill") would require the preparation and distribution of annual reports and a notice of sale and prescribes information to be included in each. Much of this information has seldom been published by municipal issuers. This bill was sponsored by Senator Williams and Senator Tower, who had also sponsored the 1975 amendment that prohibited the MSRB from requiring municipal issuers or bond dealers to provide unpublished information about the issuers's finances. Hearings for the bill proposed by Senator Eagleton and for the bill proposed by Senator Williams and Senator Tower were held together in 1976.*

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* Ronald W. Forbes (Associate Professor of Finance at the School of Business at University Center at Albany) submitted a statement and the tabulated results of a survey of official statements -- the "Summary of Reporting Practices" which is used throughout this thesis. This survey was apparently conducted in late 1975 when the longer statements were beginning to be more popular and shows the inconsistent and incomplete state of disclosure practices at that time. It tallied how many times 174 prospectus statements included a number of indicators including: unemployment data, personal income data, identification or accounting practices, and current property tax rate. (See Appendix IV, Table A-IV-(1))

Other actions on disclosure were taken by the Municipal Finance Officers Association. The MFOA has long been active in municipal finance by publishing textbooks, promoting uniform accounting standards, and giving certificates to municipalities that have reached their suggested reporting standards. In 1976, it published and circulated widely a list of proposed items to be included in a prospectus statement (hereafter referred to as the 1976 MFOA Disclosure Guidelines). This organization's position is that municipal disclosure should be voluntary not mandatory.

At least one financial officer used the 1976 MFOA Disclosure Guidelines. The Chairman of the Board of County Commissioners of Alleghany County, Pennsylvania, testified that the county had received only one bid on an bond issue that had been presented in a four-page prospectus. Fortunately, representatives from ten major municipal bond underwriters were willing to meet with him and his staff, and in two weeks his staff was able to develop a "full disclosure 24-page document" based on the 1976 MFOA Disclosure Guidelines, after which the offering received favorable bids. /̅ 63, p. 167 _7

The rating agencies did not support the 1976 Williams-Tower Bill. Their executives testified that "full disclosure" involved so much data that it would be impractical to generally distribute. Mr. Harries, the President of Standard & Poor's Corporation, said that the information necessary to evaluate the quality of a recent debt offering of the State of New Jersey was five inches high when stacked. /̅ 63, p. 110 _7 The director of the municipal bond research division of Moody's Investor Service, Inc. gave an interesting view of full disclosure for the purpose of analysis:

> "The definition of full disclosure remains vague, however, and ultimately must embrace everything which a qualified analyst decides is necessary to his reaching a conclusion... To have standardized information served up to him is a time-consuming part of his work. The provision of a centralized location where all information would be on file is the dream of the scholar and the hope of the bond analyst who is dependent on files of information which are costly to compile and maintain. /̅63, p. 153_7

Further legislation relating to information about municipal bond issuers was proposed in the House. Representative Murphy of New York introduced H.R. 675, a bill that would require the SEC to prescribe standards for making accurate municipal bond ratings and to assure that the procedures used in such ratings are fair to issuers of municipal bonds. /̅60, p. 3_7 The SEC opposed it, however, because the bill would "inject this agency into qualitative assessments of the merits of municipal securities", which would be against the "established principles of the federal securities laws whereby the Commission has tried to steer clear of making a determination of what is or is not a good security". /̅19, p. 1_7 Although the Murphy Bill has very little chance of passing, its assumption that rating standards can be developed is interesting. At the House Hearings on this Bill, Jackson Phillips, Executive Vice President of Moody's Investors Service, Inc. said that if it were passed, the SEC would have two alternatives:

> "On the one hand, it could look to the history and experience of state and local government in the United States, identify those factors which appear to have been causative of debt difficulties or protective against them, find in contemporary affairs the evident counterparts of past precursers which were of predictive value relative to the causative factors, and so determine the relevant information on which critical judgement is to be brought to bear. This will prescribe a standard as accurate as can be devised. If this were done with care, scholarship, and experience, the rating system which would evolve would, we believe, be substantially indistinguishable from the system used by Moody's.
>
> On the other hand, (the SEC might) try to devise a mechanical or formula approach. This could be done by specifying which factors may or may not be used in making the appraisal, or even by stating mandatory weights which must be assigned to permitted factors." /̅60, p. 48_7

In both alternatives, Phillips has divided the analysis process into two decisions: (1) Which information should be considered? and (2) How should it be evaluated? The 1951 New York City Report, the 1963 IBA Format, the 1965 State Technical Assistance Report, the 1976 MFOA Disclosure Guidelines, and the 1976 Williams-Tower Bill address the first question, only.

Because the questions of who should analyze bonds, what information they should consider, and how such information should be evaluated, were not resolved, potential bond purchasers were painfully aware that they did not know what risk they were assuming. The interest rates on the securities of some cities were very attractive, however. For example, in June 1976, Detroit sold a long-term bond issue for 9.78% annual interest; in July 1976, Philadelphia sold a short-term note issue for 8.07% annual interest; and in October 1976, Boston sold a long-term bond issue for 7.87%. (See Table IV-p. 121)

One county auditor explained how a disclosure policy became a prerequisite for market acceptance of a bond:

> "The golden rule has long prevailed in the investment market and that is, 'those who have the gold, rule.' When underwriters do not get disclosure, they just don't have to bid on the bonds and some of us found that out. The fact has been elementary in the field of investments for many, many years that an investor would investigate before he invests and if he has nothing to investigate he takes his other options and goes somewhere else." [63, p. 241]

G. SEC involvement after 1975

The disclosure advice given before 1975 in the 1976 Williams-Tower Bill and in the 1976 MFOA Disclosure Guidelines did not deal with the following question: If municipalities try to give the investment market the information it needs for independent analysis, who should be responsible and what should be done if the information is incomplete, inaccurate, or misleading? These disclosure suggestions assume that the information will be reasonably accurate and given with good intentions. If not, they rely on the traditional penalties for a governmental official who violates the legal responsibilities of his office. However, punishments and safeguards designed to discourage embezzlement and other corruption are not appropriate.

A case involving new interpretations of the antifraud provisions of The Securities Act of 1933 (discussed earlier, see pp. 13-15) came up through the federal court system at the same time in which municipal disclosure emerged as a political issue. New development of liability standards by the courts through the case has influenced the status of federal government and market demand for municipal disclosure.

The facts of the case, Ernst & Ernst v. Hochfelder (U.S. Supreme Court Reporter, Vol. 425, pp. 185-218) do not involve municipalties or municipal securities. The case concerns an investor who sued the auditor of an investment counselling firm because the audit failed to uncover a fraudulent scheme perpetrated by the president of the investment counselling firm. The fraud had not been discovered because the only pertaining evidence of irregularity was that the president would not allow anyone else to open his mail, even in his absence. He had defrauded one investor successfully for a number of years. This activity might have continued indefinitely if he had not committed suicide and confessed in a farewell note. /‾14, p. 185_/

In such situations the investor normally sues the auditor for damages on grounds of negligence. Hochfelder, however, sued the auditor, Ernst & Ernst, for violating the antifraud provisions of The Securities Act of 1933:

"It shall be unlawful for any person, directly or indirectly, by use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange

(a) to employ any device, scheme, or artifice to defraud
(b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or
(c) to engage in any act, practice, or course of business which operates as a fraud or deceit upon any person,

in connection with the purchase or sale of any security." [44, p. 2043]

Based upon these provisions, the lower courts found that the auditor had committed a fraudulent act. [14, p. 185]

The lower court rulings on the Hochfelder case expanded the type of actions that would be considered fraud under the Securities Act Rule 10-b. If the auditor's behavior in that case was fraudulent, the behavior of auditors of municipalities, bond counsels, underwriters, dealers and others involved with municipal securities who had inadvertently overlooked some factor related to the securities might also be considered fraudulent.

Another federal district case seemed to increase the investigatory burden on underwriters of municipal securities. Sanders v. John Nuveen involved commercial paper that, like municipal securities, was not covered by many provisions of federal securities law. The district court decision appeared to impose a greater duty on underwriters to ascertain the reliability of information concerning an issuer than that provided for securities subject to all the provisions of federal securities law. In this case, the underwriters were held liable for damages to investors for omission of material facts concerning the financial affairs of the issuer, notwithstanding the availability of independently audited financial statements upon which the underwriters claimed reliance. The court found that the underwriter had not been diligent in its investigatory duty. It said that the underwriter should have reviewed the accountant's workpapers, thereby exposing the accountant's compliance with the fraud. [63, p. 399]

If the Supreme Court had upheld the lower courts' holdings in Hochfelder and John Nuveen and applied the same principles to all cases involving securities that are not registered with the SEC, then underwriters of municipal securities would have the same investigatory burden as underwriters of commercial paper. If so, a scenario could conceivably develop such as the following: A city does not inform an underwriting bank buying its bonds that there are material facts missing from the prospectus statement; the bankers assume the prospectus is accurate and sufficiently complete because its finances have been audited by an independent accountant; after the underwriter has distributed the securities it somehow becomes known that material facts have been omitted from the information received by the final purchaser, and, finally, the final purchasers sue the underwriting banks for money damages.

Professionals in the securities field were understandably reluctant to take chances such as these until their potential liability became more clear. The underwriters and bond dealers were reluctant to accept responsibility for the completeness and accuracy of information given by municipal issuers. The director of Moody's Municipal Bond Division said, "Any suppression or failure to provide information in the municipal market can only lead to suspicion of the motives of the participants involved." [63, p. 115]

The underwriters were able to secure a disclosure policy from most issuers because it was clear that the banks could invest all of their capital elsewhere, but they still pressed for federal legislation that would mandate a standard of disclosure. Their pressure was related to the degree of liability that it seemed they could be assigned with the progression of Ernst & Ernst v. Hochfelder. When a year later, the liability of underwriters seemed reduced because of later court rulings on the case, one of the Secutities and Exchange Commissioners said that there were some signs at that time that some industry participants were no longer anxious to push for municipal disclosure legislation "they previously considered a desirable means to clarify the limits of their liability and to provide explicit statutory defenses against private damage suits." He warned them that they still needed disclosure legislation. /̄11, p. 1_7

Although the Supreme Court reversed the lower court's Hochfelder rulings (March 30, 1976), it did not sufficiently resolve liability principles that could apply to municipal securities issuers, dealers, and underwriters. The Court held that a private cause of action does not lie under the "antifraud" provision of The Securities Act, Rule 10-B, in the absence of "scienter", "a mental state embracing an intent to deceive, manipulate, or defraud". /̄12, p. 2_7 The holding was that mere negligence does not create a private cause of action where the investor has not relied on that person's or firm's advice in its purchase decision. However, the majority opinion did not view the reliance or non-reliance of the investor as a factor in whether the auditor was behaving in a fraudulent manner. The Supreme Court left open the questions of whether reckless behavior short of scienter would support a claim under The Securities Act /̄11, p. 1_7 and whether scienter is a necessary element in a SEC action. However, a federal district court soon ruled that it is necessary for scienter to be a factor as a necessary element for SEC actions under Rule 10-B. /̄12, p. 2_7 A Securities and Exchange Commissioner then stated that its enforcement actions "were not intended to and should not be subject to a scienter standard". [11, p. 1] He also said that "in any event...there are probably years of litigation ahead about the exact scope of the Hochfelder decision". [12, p. 2]

The SEC has been a strong advocate of a policy of mandatory municipal disclosure. In addition to strong public statements by its commissioners, the agency has taken official actions that have affected whether investors demand disclosure and that might affect whether federal legislation mandating municipal disclosure is passed. The SEC is a powerful and respected agency and is usually effective because it has a large and proficient staff which is experienced in preparing legal arguments and assembling evidence. If municipal disclosure were mandatory, capital markets and securities trading might operate more smoothly -- a goal of the SEC. If another agency were to regulate municipal disclosure, there might be conflicts between it and the SEC (as there have been conflicts between the SEC and the bank regulatory agencies). If the SEC were to regulate municipal disclosure, it might have to increase its staff and build up new expertise in municipal finance.

The SEC has announced investigations of New York City and of the City of Philadelphia. While the credibility of New York City in the securities market had already been damaged, the City of Philadelphia seemed to enjoy a better reputation. However, just to be named in a news release as the subject of SEC investigation brings suspicion on all of the outstanding securities of an issuer. Legally, the City of Philadelphia must now inform potential bond investors that its finances are under investigation. [47, p. 1]

If the City of Philadelphia and other municipal issuers had been registered with the SEC (as required by the original draft of The Securities and Exchange Acts of 1934 /̅ 44, p. 2044 /̅ and by the Eagleton Bill), then they would have had to have complied with the SEC record-keeping rules. Because municipalities do not register, the SEC must obtain from them material to review for evidence of fraudulent activity. The SEC has demanded that the financial offices of the City of Philadelphia produce for scrutiny copies of thousands of documents, minutes of meetings, tape recordings, and memos dealing with the preparation of the City's budget. Although most of this is theoretically open to public inspection, Lennox Moak*, the Director of Finance, said that it would take months to accumulate it all. He stated that he has no intention of interrupting "the important work of the City... to seek to make these records available or to attempt to explain them to representatives of the SEC." [47, p. 8] Because the authority of the SEC to investigate and to sue municipalities has not been established, both New York City and the City of Philadelphia have taken legal action against the SEC. [47, p. 8; 40, p. 5]

Another case has been cited in the legal and political maneuvering over the questions of municipal disclosure. Although this case also does not directly concern municipal securities, some of the findings may be applicable to the question of whether it is legal for the federal government to regulate municipal securities.

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*Lennox Moak is one of two members of the MFOA Debt Administration Committee appointed to the Municipal Securities Rulemaking Board. [46, p. 5] He was an expert witness in the Senate Hearings on loans to New York City but did not appear for committee discussions of the 1976 Williams-Tower Bill. His textbooks on municipal finance have been cited extensively in this thesis and stress the importance of providing accurate and extensive information to investors.

In late June of 1976 the Supreme Court ruled on National League of Cities v. Usery, a case dealing with a law extending federal wage-and-hour standards to municipalities. The court ruling on the Usery case was that Congress does not have power under the Commerce Clause to pass legislation displacing the freedom of states and cities to structure integral operations in areas of traditional governmental functions. Justice Harry Blackmun, who cast the decisive vote in that case, wrote a separate concurring opinion. He said that a balancing approach had been implied that did not outlaw federal power in areas such as environmental protection, "where federal interest is demonstrably greater". [40, p. 5]

The SEC cited Blackmun's opinion in a case it filed on July 27, 1976, against a reclamation district, a public agency of the State of California, which the SEC says fraudulently offered and sold about $2,220,000 in tax-exempt securities. This is the first time the SEC has ever actually filed a case against a municipal issuer. The SEC's points in its brief for that case which responded to the Supreme Court findings in the Usery case were as follows:

> "Simply stated, securities fraud is neither an 'attribute of state sovereignty' nor a 'function essential to separate and independent existence'
>
> "Federal proscription of securities fraud certainly will not impair the state's ability to function effectively in a Federal system.
>
> "The Federal securities laws do not supplant any state policy choices.
>
> "Application of the anti-fraud provisions will not deny to the States the right to decide whether or not to sell securities; when, where, and to whom and in what form to sell securities; what interest to pay purchasers of their debt securities; and for what purposes the proceeds of the securities issue will be applied.

"Neither, will application of the antifraud provisions of the securities laws force the States to relinquish important government services.

"Maintenance of the integrity of the municipal securities market will, if anything, preserve the ability of governmental units to finance those fundamental services 'which governments are created to provide'.

"The federal interest to protect the investing public and the municipal securities market is very great." [40, p. 5]

The opposing legal arguments were stated in a legal brief filed in a suit by New York City against the SEC on the same day that the SEC had filed the brief described above (in its case against the California district). N.Y.C. filed its suit against the SEC in response to the SEC investigation of N.Y.C., mentioned earlier. N.Y.C. is seeking a declaratory judgement that would order the SEC to stop its investigation on these legal grounds:

"Neither the Securities Act nor the Exchange Act authorizes the SEC to regulate, investigate, or take any action with respect to states or municipalities or their officials in connection with the issuance or sale of municipal securities.

"Congress expressly recognized prior to the passage of these acts that any attempt to regulate state and municipal issuers or securities would raise constitutional difficulties.

"There is no function more fundamental to a sovereign's separate and independent existance than the raising of funds by borrowing or otherwise, for all other functions are dependent on it.

"It is unconstitutional for Congress to regulate or otherwise determine the manner in which states and their political and governmental subdivisions may incur and repay their debts, for by doing so Congress would displace the freedom of states and municipalities to structure integral operations in areas of traditional governmental functions.

> "To the extent that the provisions of the federal securities laws are interpreted to authorize the SEC to regulate, investigate, or take action with respect to municipalities or their officials in connection with the issuance or sale of municipal securities, such provisions are unconstitutional." [40, p. 5]

Two constitutional issues in federal regulation of municipal securities have been cited. The one that emerges from Usery and in the suit filed by New York City against the SEC relies on the 10th Amendment to the U.S. Constitution which provides:

> "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people."

The second constitutional issue concerns the 11th Amendment which some lawyers claim protects state and local officials from SEC anti-fraud action. [40, p. 5] The 11th Amendment to the U.S. Constitution provides that:

> "The judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by citizens of another state, or by citizens of any foreign state."

H. Technical questions in municipal disclosure policy development that are related to accounting, auditing, and liability assignment

To be most useful in analysis, financial and other information must be accurate and comparable. Setting of accounting standards would help to assure the comparability of financial data. Auditing would help to assure the accuracy of financial data and may also help to uncover inefficiency, fraud, or other conditions of interest. As explained earlier, pre-assignment of liability -- or responsibility for inaccuracies and important omissions -- has been an important factor in SEC and investor pressure for disclosure by municipalities.

1. Questions related to accounting practices

In many fields, accounting practices have been standardized. Because some local accounting practices are mandated by local government charters and statutes and because the jurisdiction of the federal government in this area is unclear, attempts to standardize municipal accounting have been unsuccessful. There are a number of different local government accounting techniques that have been approved by professional accounting societies. Standard local government accounting practices vary so much that there are fifteen different ways of representing the financial condition of the municipality. /̅62, p. 93̲7 Expenditures and revenues may be recorded using cash, accrual, or partial accrual bases. Under a cash basis, the item is not shown until cash has been spent or received. Under a full accrual basis, the tiem is recorded when the liability is incurred (such as paid time due to employees for sick leave and vacation) or when the legal action has been taken to obtain a revenue (such as providing a state-reimburseable service or mailing a tax bill to property owners). Under a partial accrual basis, some revenues and expenditures are recorded when it is known how large they will be and when they fall due while others are recorded only when cash has been transferred. Some municipal corporations may assign a cash value to assets such as land and machinery and depreciate its recorded value every year, but most general governing bodies do not unless they operate special enterprises such as auditoriums or waste disposal plants. Local governments usually use fund accounting because the uses of certain funds are legally restricted. Usually, changes in the balances of all major fund groups are included in the annual financial report because a totla of the changes may be misleading. Although standard fund categories have been recommended, others are frequently used. /‾26_7 A major change in accounting practices used may be expensive and inconvenient. In fact, a 1972 study of the 1, 822 municipalities belonging to the MFOA found that only 133 had agreed to comply with the set of uniform accounting standards promulgated by that organization in 1947. /‾56, p. 87_7

It is not at all clear how much more difficult it is for analysts to compare the finances of municipalities because of variations in their accounting practices. Even if accounting techniques were standardized, the finances of similar cities still might not be comparable because they may be structurally different in other ways. For example, some municipalities may have financially independent school or utility districts. In any case, interpreting the financial statements of a given municipality is more difficult if one does not know its basis of accounting. However, only six out of 174 issuers surveyed by Forbes in 1975 bothered to identify their accounting methods in their official statements. (Summary of Reporting Practices) /‾63, p. 271_7 The Williams-Towers Bill, as drafted in 1976, would go a step further than reporting of accounting practices but not as far as standardizing them by assigning to the SEC the power to set standards for the accounting practices to be used in required propsectus statements and annual reports. /‾63, p.11_7 However, it might be very difficult to prepare financial information using a set of accounting practices that is different from those used in all records. Such a provision might result in increased standardization.

The additional problems presented in development of a municipal disclosure policy by local government accounting practices are as follows:

(1) Because accounting practices of individual governments are not adequately reported, it is more difficult to understand their financial statements; (2) Because of the diffences between government accounting and profit accounting, it is more difficult for an investor, who is not a trained accountant but who can understand a company's annual statement of earnings, to understand municipal financial statements; (3) Because of the variations in local government accounting practices, it is more difficult to compare the revenues and expenditures of municipalities that are otherwise similar; and (4) Standardization of local government accounting practices may be expensive and politically difficult and may interfere with home-rule doctrines.

2. Questions related to auditing procedures

An auditor is a specialized and specially licensed accountant who normally reviews the accounting records of an entity to see if its financial records are in order. Definitions of what an audit should cover vary considerably. One auditing firm, in a report on the advisability of municipal disclosure policies, stated that an audit should cover fund accounting, budgetary accounting, legal compliance, and the basis of accounting. An audit of fund accounting traces the balances and encumbrances of various funds. An audit of budgetary accounting compares actual revenues and expenditures with those that had been anticipated. An audit of legal compliance checks how well the unit followed its own legal restrictions and applicable rules of the federal and state governments. An audit of the basis of accounting checks whether the city was properly using one of a generally accepted set of local government accounting principles. The auditor may recommend changes in in the units financial record keeping and cash management practices to make them more efficient. [16, pp. 8-11]

An audit report is technical, detailed, and may be more than a hundred pages long. The auditor may also provide a summary opinion on particular aspects of its review or a statement that everything is in order. However, much of the information that has been recommended for municipal disclosure is not included in an auditor's report. The auditor does not usually consider revenue sources and policies or the purposes of expenditures.

Some cities have found that it is most efficient to maintain auditing departments. Because embezzlement by city officials is rare and this risk is usually covered by surety bonds, in the past it was not generally thought that there were significant dangers or conflicts of interest in relying on an audit by trained city employees. Lately, however, there is a greater tendency to use independent auditors who are disinterested parties and therefore have no reason to cover up fraud or ignore inefficiencies and irregularities. [64] In fact, independent auditors stake their professional reputations on the accuracy of their reports and may also be held legally liable for damages. A positive report from an independent auditor may do a great deal to allay investors' concern over the risk attached to securities of that city. [23]

The main reason for a city to object to an audit requirement is its expense. An audit by a prestigious firm of Certified Public Accountants commands the most respect from sophisticated investors and is generally more expensive than one by state- or city-employed auditors. A thorough audit of a large city takes at least several months and may require a year's preparation time.

Auditors have been actively involved in discussions of municipal disclosure. Certain CPA fims have been aggressive in explaining the expanded role they could take in improving municipal information releases. If more municipalities hire these firms and use them for more extensive auditing, then thier workloads and profits will be increased. However, the types of auditing these firms are advocating as appropriate in aiding investor scrutiny may not otherwise help a city in its financial management.

The 1976 version of the Williams-Tower Bill includes a provision requiring review of financial statements by an independent or certified auditor applying to fiscal years starting after December 31, 1978. The SEC would be given the power to decide which financial statements shall be audited and what procedurew will be used. /‾63, p. 7_/

3. Questions related to liability assignment

One reason suggest for legislation mandating municipal disclosure is to limit the potential liability of underwriters and bond dealers to final purchasers of securities. The Williams-Tower Bill, as written in 1976, limits the potential liability of the underwriter to the total price of the bonds. It does not limit the liability of the issuer or specifically provide that the antifraud provisions of The Securities Act of 1933 should apply. Underwriters would still, then, be liable for large sums under the general "anti-fraud" provisions. /‾63, p. 7_/ One SEC Commissioner said that the bill is inadequate in this respect and should contain:

> "remedies and conditions under which participants in muncipal securities may claim defenses against liability for the use of false or misleading information in connection with the offering or sale." /‾11, p.1_/

These concerns had been minor when municipal bonds were considered as safe as Federal Treasury Notes.

After the passage of The Securities Acts of 1933 and 1934, a complicated web of case law and administrative regulations was developed to deal with financial liability due to omissions and errors in corporate financial statements. Some private companies have found liability for claims about their finances is a great burden. In fact, SEC enforcement of their reporting requirements has been held to apply also to obscure information of interest only to certain kinds of speculators and chartists whose analysis techniques are commonly considered superstitious. [46, p. 3]

The Municipal Securities Rulemaking Board has suggested that an express cause of action for damages based on material misstatements or omissions be created by Congress. They recommend that issuers be included within the scope of liability established. Certain defenses, reflecting the ability of the various participants to ascertain the accuracy and completeness of the information in question, should, they suggest, be established for each category of participant in the municipal securities distribution process. According to this principle, the Board suggests that the municipal issuers should have an absolute liability with respect to all information set forth in an official statement except for information furnished by an official source other than the issuer. If an action is taken against them, the Board suggests that the issuer should be required to demonstrate that it had no reasonable grounds to believe and didnot believe that other official sources were materially inaccurate or misleading. [63, p. 403]

If the city management somehow errs in its financial statements or other presentations of important financial contingencies and the auditor does not discover the error in time to correct it before the underwriter, bond dealers, and final purchasers rely on it in making their investment decisions, who should be liable? Does it make a difference whether the city deliberately or carelessly misled investors or whether the discrepency was due to external factors? If the municipality does not default, how important in legal proceedings are the dollar amounts of the reporting errors or a drop in resale prices of its securities following publication of the error? In general, how should such damages be measured? Can an acknowledgment of error or other remedial actions somehow substitue for full financial acceptance of responsibility and repayment of money damages? These questions have not yet been legally resolved for municipal securities.

If the liability of the underwriter and bond dealers are limited, the whole burden might fall upon the city and its contracted auditors, bond counsels, and financial consultants. It is not at all clear whether the cities and other municipalities will be able to pay the full costs if compensation is to be made for all direct and indirect investor damages due to errors in the disclosure material. Also, a full financial burden of liability may deter broader reporting, cause over-stressing of "dirty laundry", or interfere with aggressive marketing and public relations.

One exampe of a conflict over misreporting has already arisen in a situation involving the City of Philadelphia, which, as mentioned earlier, is under SEC investigation. City administrators had placed an advertisement for its bonds in The Wall Street Journal that gave a short financial description including a projected surplus that did not actually materialize. [47, p. 1] Even though Philadelphia has not defaulted, it may be more difficult for owners of its bonds to resell them. In this example, it is not at all clear what remedy is appropriate or whether the market will accept the statement of Lennox Moak, the Director of Finance, that there had been "absolutely no wrongdoing, absolutely no effort to deceive". Even if Philadelphia is not forced to pay money damages, investors may be less willing to buy its securities following this incident. This particular situation may be resolved by a long, expensive, and politically damaging court battle.

I. Description of the survey research

As mentioned in the introduction, this author developed and administered three surveys: the Indicator Survey, the Perceptions Survey, and the Survey of Financial Officers (See Appendicies I, II, and III). The results of the Indicator Survey and the Perceptions Survey are very useful because the circumstances affecting investor demand for municipal disclosure have changed so much that it is hard to know how most market participants feel. These survey results describe the opinions a fairly representative group at a recent data. Also, almost no research at any time has been concerned with market use of information and opinion formation -- it has primarily been concerned with the assignment or effect of ratings. The results of the Survey of Financial Officers are helpful in describing the recent disclosure experiences of cities and supplement Forbes's "Summary of Reporting Practices".

The 1951 New York City Report, the 1963 IBA Format, the 1965 State Technical Assistance Report, the 1976 MFOA Disclosure Guidelines, and the 1976 Williams-Tower Bill were all written by open or closed committees of experts. Their lists of recommended information for reporting were probably compiled in customary committee style in which a few people make detailed suggestions and everyone else approves or disapproves. These sets of recommendations are not accompanied by any explanations or defenses of why they recommended or ignored particular information. The 1965 State Technical Assistance Report includes in its document copies of the 1951 New York City Report and the 1963 IBA Format. The 1976 MFOA Guidelines include a mention of the 1965 State Technical Assistance Report. Yet neither is accompanied by an explanation of why their recommendations vary from the previous ones.

Lennox Moak published suggestions for information to be reported to various groups and a discussion of "factors considered by investors and the rating agencies in determining preferences". He explains in a very convincing manner why many financial characteristics and characteristics describing the local economy and social situation are important in perceptions of bond security.

This author did a thorough search of industry and academic publications on municipal securities and finance and was unable to find any published data that would support or contradict Moak's descriptions or the recommendations of other sources. However it seems reasonable that there should be some guidelines to use in deciding whether a particular piece of information should or should not be disclosed. In fact, some of the results of the author's surveys show a gradient of information by importance and others suggest hypotheses about how such information is and can be used. The results of the three surveys are used to develop a strategy in municipal information release.

1. Survey distribution

The Indicator Survey and the Perceptions Survey were distributed by the author in cooperation with the City of Boston in May, 1976 and July, 1976. There were two mailings of each survey, the second a follow-up to those who did not answer the first. The mailing list, supplied by the city, had been compiled for use in mailing prospectus statements and other material directly related to the marketing of the city's securities. The list of 2,300 independent and bank-affiliated bond dealers was divided (every-other-one) so that half (1,150) received each survey. The mailing list was substantially the same as the standard, professionally used Directory of Municipal Bond Dealers of the United States compiled by the Bond Buyer, the leading publisher in the municipal securities market.

The second mailing increased the total response rate and legitimacy of results. The data from each mailing were similar. A few questions appeared on only the second mailing. The tabulated results in the appendix include the total number of responses to each question.

In total, there were 191 responses to the Indicator Survey including 67 bank-affiliated dealers and 124 independent dealers. There were 172 responses to the Perceptions Survey including 55 bank-affiliated dealers and 117 independent dealers. These response rates (17% and 15%) are good for surveys distributed by mass mailings. Each survey had a large response from the New York City and Boston areas but more than two-thirds were from other areas including every state. Particular responses were confidential.

The "Survey of Financial Officers" was mailed in August, 1976 and September, 1976 with a cover letter on letterhead stationary from the Department of Urban Studies of the Massachusetts Institute of Technology (MIT). It was addressed to the treasurer, comptroller, or director of finances of each of the forty largest American cities. It was returned by financial officers from thirty-one of those cities. (See Appendix III for a list of responding cities)

2. Description of the Perceptions Survey

Almost all of the questions on the Perceptions Survey concern opinions of Boston's economy, property, government, and quality-of-life, although a few questions address opinions of the City's securities. The results can be viewed not only for what they show about Boston but also as an example of investor opinion formation. The results of the Perceptions Survey are discussed only in Chapter VI (Investor Perceptions of Local Economic Factors and the Character of Local Communities -- Disclosure of Information on Economic and Social Factors) and Chapter VII (Summary and Conclusion). As mentioned earlier, the survey form and tabulated results are in Appendix II.

3. Description of the Survey of Financial Officers

The Survey of Financial Officers is much shorter than the Perceptions Survey and the Indicator Survey. Although its results are not drawn explicitly into discussion in Chapters III, IV, V, and VI, they are useful in further establishing cities' initial and recent experiences in implementing disclosure policies. As mentioned earlier, the survey form and tabulated results are in Appendix III.

All of the responding cities release some sort of annual report and a prospectus statement. The annual report may be an auditor's report and may be released some while after the fiscal year ends. It may also be a public relations document with picutres of the administration and lists of goals and accomplishemnts. The annual financial reports released by the thirty responding cities were written and released by the office of the city auditor, the city accountant, the city comptroller, the treasury, or the finance department. Sometimes the annual report and the propsectus statement are released by completely separate offices.

City auditors are infequently used for the annual report -- six cities used state auditors and thirteen used independent auditors. More cities brought in independent auditors for preparation of the prospectus statement than the annual report. City auditors were also more involved with preparation of the prospectus statement. Often audited annual reports were used as sources for the prospectus statement. Some cities had only the financial section of the prospectus statement audited and others used independent auditors for the financial sections and city auditors for the rest of it.

The lenght of the propsectus statements released by these cities varied greatly. The shortest was only four pages and the langest was 165 pages. The average length was 44 pages.

The average number of annual reports distributed by these thirty cities was 369 copies. The range of distribution was between 100 and 850 copies. They were distributed to the following:

Distribution	Count (out of 30)
To local banks	29
To nonlocal banks	22
To local bond dealers	26
To nonlocal bond dealers	25
To a few local citizens	17
To more than a few local citizens	14
To many local citiznes	7
Local journal	2
Local libraries	1
Mailing list	1
Municipal and state govenments	1

Atlanta sends a monthly report to its underwriter. Philadelphia is the only city that sends out a regular newsletter. Ten of these cities distribute more annual reports than propsectus statements, four distribute the same number, and fourteen distribute fewer. The average number of copies of the prospectus distributed is 467 with a range between 75 copies and 1800 copies not including a recent distribution by the City of Boston of 3,000 copies. All of the cities responding except Oakland and Jacksonville maintain regular mailing lists.

The only state input into prospectus preparation was a Pennsylvania guiding statute used by Pittsburgh.

Only Chicago and Detroit would admit to being unable to place a bond issue and both blamed it on the "New York Situation". Detroit did not receive an acceptable bid on housing authority bonds that it tried to sell three times between December 1974 and March 1976.

4. Description of the Indicator Survey

The questions on the Indicator Survey are of two types. Most concern particular indicators such as "total population" or "net indebtedness". The other questions concern reliance on and use of various sources of information. The results of the Indicator Survey are cited throughout this thesis as explained in this section. As mentioned earlier, the survey form and tabulated results are included in Appendix I.

On the Indicator Survey, seventy-four indicators were grouped into four sections: (1) population and other characteristics, (2) financial statistics, (3) economic statistics, and (4) property indicators. Questions concerning these indicators were asked to find out whether each piece of information should be disclosed, how much description or explanation it merits, and whether it is worthwhile for a particular city to include it in its statements if similar data for other cities is not accessible. Respondents were asked three questions about each indicator: (1) How does it rank of a scale of importance? (2) Is it one of the three most importantindicators of that section? and (3) Would it have significantly more meaning if it was compared to other cities?

The scale of importance used had a range of possible responses of "1", "2", "3", "4", "5", or "don't know". A response of "1" meant that the indicator was considered to be "very important", a response of "5" meant that the indicator was considered to be "irrelevant" and those between described a range of average importance. When all of the indicators of the various sections are ranked together by mean importance ratings, the results show a fairly even gradation of importance between "1" and "4", although none have an average below "4". Although there was also a fairly even gradation within each section, the indicators in the financial section were generally ranked higher than those in the other three sections. In Chapters III, IV, V, and VI, the perceived importance of each indicator is discussed using the rank of the mean of its importance ratings relative to the other seventy-three indicators on the survey (i.e. the relative importance ranking is 39th out of 74). The mean importance (i.e. 2.39) is reported in the appendix and in chapter summary charts but is only occassionally mentioned in discussion.

Of the seventy-four indicators, the ten most important are:

Indicator	Relative Importance Rank (out of 74)
Total debt outstanding	1
Debt per capita ratio	2
Funded debt outside of legal debt limit	3
Net indebtedness	4
Records of tax collections compared to tax accruals	5
Assessed taxable valuation of commercial property	6
Summary of revenue sources for five years	7
Assessed taxable valuation of residential property	8
Debt retirement schedule	9
Excesses in operating expenditures over originally approved budgets	10

All of these ten indicators can be said to be "very important", according to the bond dealers surveyed. On the "1" to "5" scale with "1"="very important" and "5"="irrelevant" used on the survey form, all of the ten most important indicators had an average importance rating greater than "1.5".

Although the bond dealers ranked "total debt outstanding" higher in importance than "debt per capita ratio", the actual difference in their average importance rankings is only .005.

At the end of each of the four sections of characteristics on the Indicator Survey, respondents were asked to list the three from that section that they thought were the most important. The purpose of these questions was to provide a way to check respondents' ratings of importance on the 1-5 scale. A few respondents, for instance, confused the directions and marked the most important indicators "5" instead of "1". Responses on these questions were also used to test the validity of ranking by mean importance rating. The number of times that each particular indicator was listed as one of the most important three were adjusted for a few indicators only appearing on the second mailing. The indicators in each of the four sections were then ranked by both the numbers of mentions and the mean importance ratings. (See Appendix I) These rankings differed only slightly thereby showing the basic consistency of these results.

As mentioned earlier, the survey also asked respondents to check "yes" or "no" if the information would have significantly more meaning if compared to other cities. There were twenty-five indicators for which more than half of the respondents desired comparisons. There is some overlap with the twenty-five most important indicators -- such as total debt outstanding, median household income, pension liabilities, and total population. (See Appendix I) Some other information, not considered relatively important, was also considered to be significantly more meaningful if comparisons were given -- such as energy costs, population by age group, and crime rates.

The other questions on the Indicator Survey, relating to information use, are not cited as extensively in the body of this thesis but are important to its conclusions. Their results are also tabulated in Appendix I. Responses to several questions showed the importance of prospectus reporting. When asked to rank sources of information used in evaluating the credit worthiness of a city's specific bond issues, aggregated results adjusted by mean show the following ranking:

(1) The prospectus statement of the bond issue
(2) Moody's and Standard & Poor's published bond ratings
(3) In-house research
(4) Yields of comparable issues
(5) Limited circulation reports
(6) Informal recommendations of colleagues

In response to another question, 74% said that the poor quality of information in a prospectus, independent of other inputs, has sometime detered them from purchasing a security. Also, 73% thought that the municipality with the inferior prospectus will be forced to pay somewhat or significantly higher interest rates.

Despite the asserted importance of adequate prospectus statements, 62% said that they, their staff, and/or their clients usually spend less than one hour reviewing a propsectus and only 5% spend more than several hours. Therefore, 86% said that a short document with note of a bond sale and key information would be useful if they also had access to a detailed prospectus. More than half would obtain more information if the sources of information upon which they usually rely leave them uncertain as to whether to buy a specific issue. In response to another question, 98% said they would go to the underwriter, if they would obtain more information, and 91% said they would go to the municipality that is issuing the bonds. By far the most important part of the prospectus to them is the "analysis of debt and revenue structures.

III. Disclosure of revenue information

Are some revenue sources more important to bond security than other revenue sources? How might disclosure of revenue information affect a city? What is meant by and how important is the quality of financial management of revenues? This chapter explores these questions, using some of the results of the Indicator Survey and the sources identified in Chapter II (the 1951 New Yokr City Report, the 1963 IBA Format, the 1965 State Technical Assistance Report, the 1976 MFOA Disclosure Guidelines, and the 1976 Williams-Tower Bill).

This chapter has seven sections: (A) General discussion of revenues, (B) Year-end balances, (C) Property tax rates and levise, (D) Locally generated revenues other than those from property taxes, (G) State and federal aid, and (H) Summary and conclusions. The charts preceding the first chapter show the relevant data from the Indicator Survey and from the Summary of Reporting Practices so that existing disclosure of revenue information may be compared with investor's desires. Other charts, preceding each section, compare recommendations for disclosure of the type of revenue information discussed.

Chart III-1

Frequency of Reporting Revenue Information in 1975

Section of Chapter III in which Discussed	Indicator	Reporting	Not Reporting
A	Operating Statements of Revenues and Expenditures for the most Recently Completed Year:	44	130
A	Detailed Statement or Explanation of Sources of Revenues and Expenditures:	25	149
C	Current Property Tax Rate:	109	60
D	Current Year Assessed Valuation of Taxable Property:	139	22

Source: (Excerpted from exhibit submitted by Professor Ronald Forbes, New York University) U.S. Congress, Senate. Committee on Banking, Housing, and Urban Affairs. Hearings before the Subcommittee on Securities on S. 2969 to Amend the Securities Exchange Act of 1934 to Require the Preparation of Annual Reports and Distribution Statements by Issuers of Municipal Securities, and for Other Purposes, S. 2574 to Amend The Securities Act of 1933 to Provide for Registration of Securities Issued by State and Local Governments, February 24, 25, and 26, 1976. 94th Congress, Second Session, Washington, D.C.: U.S. Government Printing Office, 1976, p. 271.

Chart III-2

Results of Questions on the Indicator Survey Concerning Revenue Information

Section of Chapter III in which Discussed	Indicator as listed on survey form	Relative Importance Ranking (out of 74)	Mean Importance Rating (on 1-5 scale)	Proportion Desiring Comparisons (%)
E	Records of tax collections compared to tax accruals:	5	1.3	58
D	Assessed taxable valuation of commercial property:	6	1.4	52
A,F,G,	Summary of revenue sources for five years:	7	1.4	48
D	Assessed taxable valuation of residential property:	8	1.4	51
A,F,G,	Growth of revenues by source over five years:	12	1.5	45
G	Total state and federal aid to city and as percentages:	13	1.6	65
D	Estimated market value of commercial property:	15	1.6	45
D	Estimated market value of residential property:	16	1.6	46
D	Assessment practice information:	18	1.7	45
-	Statement of assets and liabilities over five years:	24	1.9	36
D	Percentages of property exempt from taxation by type of property and adjusted assessment:	27	2.0	53
G	Trends in retail trade:	45	2.7	43

Chart III-3

Disclosure Recommendations Given for General Information on Revenues

	Types of Descriptive Information Recommended				
Recommending Report	Trends of Total Revenues	Sources of Total Revenues	Trends of Sources	Fund Assets	Several Years' Operating Statements
1951 New York City Report	Yes	Yes	Yes	Yes	No
1963 IBA Format	Yes	Yes	Yes	Only of sinking funds	No
1965 State Technical Assistance Report	Yes	Yes	Yes	No	No
1976 MFOA Disclosure Guidelines	No	No	No	Ambiguous	Yes
1976 Williams-Tower Bill	If required by the SEC	If required by the SEC	If required by the SEC	If required by the SEC	If required by the SEC

A. General discussion of revenues.

The three basic sources of government revenues are taxation, service charges, and grants. On the average, cities receive a large amount of revenues from federal and state grants. The remaining revenues are raised from local taxes and service charges. A composite pie chart using U.S. Census data represents the average of revenue sources for a number of local government units in 74 Standard Metropolitan Statistical Areas (SMSA's). [See Figure III-1, p. 79]

The total amounts of local government revenues and the amounts received from property taxes, non-property taxes, state and federal aid, and other property sources vary a great deal between cities. Although per capita data can be misleading, it is useful in showing the range of variation. Companion tables to Figure III-1 show the per capita revenue amounts and tax burdens of some of the 74 SMSA's whose revenue figures were averaged to give the data in Figure I. [See Table III-1 and Table III-2, pp.

Available resources to the local government unit for each fiscal year must subtract the amounts due for maturity of bonds and needed for repayment of any deficit from the previous year. This is represented by an equation in Figure III-2 [p.

The implication of revenue disclosure is that the city's financial management has developed projected streams of revenues under various contingencies. Theoretically, it has used these projections in a prudent manner when deciding to incur long-term debt. Although optimistic revenue projections are often published in local economic development plans for local citizens, they are not included in documents for use by bond buyers who are more cynical and in a position to sue should these projections be inaccurate.

Some favorable and unfavorable factors can be identified as having a bearing on future revenues. These would include such factors as agreements between the city and the state governments about state aid, annexations of suburban areas, legal limits on the tax rate, or major developments affect- the property base, such as new industrial parks or the closing of a military base. Analysts who are doing a thorough study of the city's finances might be interested in making their own projections of future city revenues under such contingencies or in judging how well the city management has dealt with similar uncertainties in the past.

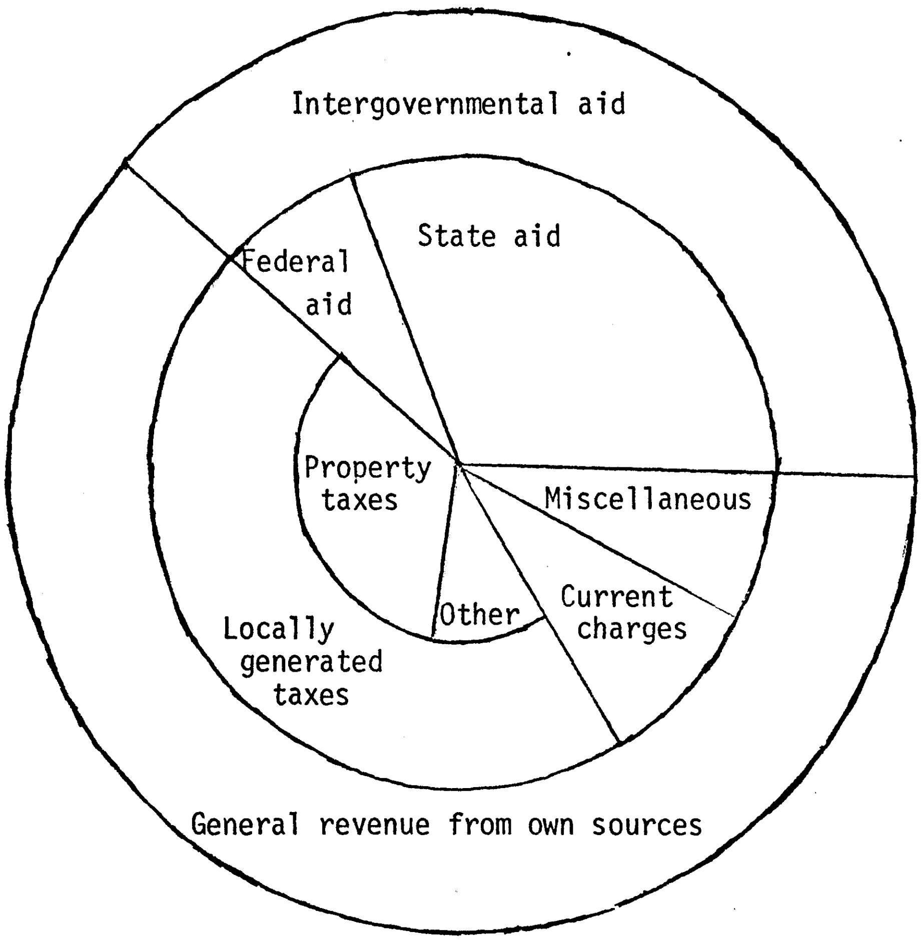
The scope of revenue contingencies may be difficult to define and their disclosure may be expensive, so revenue contingencies should not necessarily be included in the prospectus. An advisory board for municipal disclosure could help to decide what information about revenue contingencies are "material facts" what the city's liability is. If the city financial administration has a policy of being open and helpful to municipal credit analysts, the analysts could ask the city for any other information they might want and could perhaps make some useful suggestions.

Logically, to understand the revenue situation, analysts must know about sources so that they may develop hypotheses about continued levels. The earliest three sets of disclosure guidelines by expert commissions (the 1951 New York City Report, the 1963 IBA Format, and the 1965 State Technical Assistance Report) suggest that revenues be reported by source or major category. The 1976 MFOA Disclosure Guidelines does not recommend that general revenue sources be reported. Because these sets of recommendations are not accompanied by explanations, it is not clear why the MFOA committee dropped this recommendation of the earlier commission. It might have been an oversight, a deliberate omission to reduce disclosure costs and statement length, or an assumption that the information is available from other sources. The U.S. Census Bureau does publish information about the revenue sources of many large cities, but by the time it is published, it is two to three years out-of-date and is not accompanied by explanation of tax rates or grant programs. [58] Even though they should know about Census publications, the respondents to the Indicator Survey gave a relative importance ranking of 7th out of 74 to "Summary of Revenue Sources for Five Years" when asked whether it should be included in prospectus statements. The result on this question clearly contradicted the recommendations given in 1976. Further exploration might be done on how much detail on revenue investors would want directly from the cities if they had access to a more detailed or up-to-date Census publication.

Instead of requiring reporting of trends of revenues and expenditures by category, the 1976 MFOA Disclosure Guidelines suggest disclosing financial statements on operations for the last five fiscal years. [33, p. 5] Forbes's study in 1975 found that 44 out of 174 issuers included them for the last year. These issuers may have included operating statements because of confusion over what revenue information is most important. Government operating statements cannot be interpreted accurately without knowing the basis of accounting which were included in only six of the 174 statements analyzed by Forbes. [63, p. 271] While statements on operations are normally supplied to rating agencies and are useful for local citizens, such statements are generally at a level of detail completely inappropriate for mass distribution. Because they are usually given for only one or two years, trends cannot be extrapolated without access to earlier statements. The superfluous detail may obscure the most important points. However, the advantages of release of financial statements on operations are that carefully kept financial records, often audited, present no collection costs and little basis for questions of accuracy or completeness.

Figure III-1

Composite of Local Government Revenue Sources in Metropolitan Areas



Source	Proportionate Share (%)	
Intergovernmental aid (excluding interlocal)	38.9	
Aid from state government	31.3	
Aid from federal government	7.6	
General revenue from own sources	46.5	
Locally generated property taxes	37.2	
Other local taxes	9.3	
Local charges	9.5	
Miscellaneous local revenues	5.2	
General revenue	100.0	Total

Source: (Compiled from) U.S. Bureau of the Census. Local Government Finances in Selected Metropolitan Areas and Large Counties: 1973-74. (Series GF-74, No. 6) Washington D.C.: U.S. Government Printing Office, 1976, Table 1.

Table III-1

Comparison of Revenue Sources and Levels of Some Cities
(Dollars per capita) FY 1973-74

Standard Metropolitan Statistical Area (SMSA)	Total General Revenues	State Aid	Federal Aid	Total Locally Generated	Local Property Taxes	Local General Sales and Gross Receipt Taxes	Current Charges (Local)	Miscellaneous Locally Generated Revenue
Atlanta	614	129	65	419	209	28	120	36
Boston	670	120	53	495	423	-	53	16
Cincinnati	589	146	48	394	172	7	106	47
Cleveland	635	144	44	447	253	10	75	62
Dallas	503	112	40	351	215	23	65	37
Detroit	718	105	42	365	306	-	79	46
Houston	471	96	32	343	230	21	49	31
Kansas City	557	115	50	392	220	8	63	40
Milwaukee	828	339	44	418	304	-	58	52
Newark	754	198	39	518	415	-	48	20
New Orleans	487	152	56	279	84	52	67	31
New York	1303	515	60	729	359	62	120	56
Philadelphia	623	173	52	398	205	-	57	36
Pittsburgh	518	154	51	312	181	-	51	24
St. Louis	508	129	40	340	199	21	46	25
San Francisco	994	285	77	632	407	34	110	55

Source: (Compiled from) U.S. Bureau of the Census. Local Government Finances in Selected Metropolitan Areas and Large Counties: 1973-1974. (Series GF-74, No. 6), Washington, D.C.: U.S. Government Printing Office, 1976.

Table III-2

Comparisons of Tax-Burdens in Some Cities
(State and local taxes in 1972-73 in dollars for a family of four earning $10,000)

City	Total	Income	Real Estate	Sales/Other
Atlanta	644	83	294	264
Boston	1,793	287	1,341	165
Cincinnati	847	225	465	157
Cleveland	755	155	443	157
Dallas	429	-	204	225
Detroit	905	297	369	239
Houston	388	-	163	225
Kansas City	850	241	380	227
Milwaukee	1,507	392	921	194
New Orleans	678	64	324	285
New York	1,398	292	751	355
Philadelphia	1,050	561	334	155
Pittsburgh	1,088	440	493	155
St. Louis	859	241	357	261
San Francisco	1,241	64	948	229

Source: (Compiled from) Department of Finance and Revenue, Washington, D.C. Major State and Local Tax Burdens in Washington Compared with Those in the 30 Largest Cities, as quoted in Boston Redevelopment Authority. "Boston's Economic Program: Planning and Development for the 1976-1985 Decade". (Draft), January 1976, Table III-30.

Chart III-4

<u>Disclosure Recommendations Given for Information on Year-end Balances</u>

Recommending Report	Types of Descriptive Information Recommended: Fund Balances	Trends of Total Balances	Audit for Budgetary Accounting
1951 New York City Report	Yes	No	No
1963 IBA Format	No	Yes	No
1965 State Technical Assistance Report	No	Ambiguous	No
1976 MFOA Disclosure Guidelines	Ambiguous	Ambiguous	No
1976 Williams-Tower Bill	As required by the SEC	As required by the SEC	As required by the SEC

B. Year-end balances

The most basic comparison of "total available resources" for the year and total revenues is controversial. The difference (as shown in Figure III-2) reflects proceeds and redemptions of bonds and the city's cash surplus or deficit. Although Lennox Moak claimed that a deficit is not necessarily a bad thing and may be easier to manage than a surplus [28, p. 76], investors seem to feel differently. Recent public apprehension about municipal insolvency has forcused attention on any mismatches between revenues and expenditures. A comparison of the trends of the total revenues, the total budget base, and the total expenditures would indicate the existence of any problem more clearly than would the trumpeting of a single positive or negative figure at the end of the year. Yearly comparisons of the balance could show whether a deficit was accumulated by continual overspending or as a result of unanticipated fund needs or unpredicted lost revenues. The trends of total revenues, budget bases, total expenditures are important in showing whether the financial management and administration of a city can reasonably estimate expected revenues, determine a reasonable level of planned expenditures, and live within the budget. This sort of analysis is part of an audit procedure for budgetary accounting. This is an area of municipal finance in which there may be some policy trade-offs between extensive auditing and extensive reporting.

The local or national news media usually picks up a single surplus or deficit figure as an indication of the city's financial health. The mayor, comptroller, or other administrative staff have interviews or send explanations to the news media on the year-end figure. If they could refer to

Figure III-2

Equation Defining Available Resources

"A"	+	"B"	+	"C"	=	"D"
Resources at beginning of year		Revenues received in year		Proceeds of debt issued in year		Total resources available in year

− "E"	−	"F"	−	"G"	=	"H"
Payment of principal of debt		Payment of interest on debt		Payment of expenses		Resources at end of year

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Source: Moak, Lennox L. and Hillhouse, Albert M. Concepts and Practices in Local Government Finance. Chicago, Illinois: MFOA, 1975, p. 63.

an independent auditor's summary, their explanation would have more credibility. Such explanations should be included in information directed towards bond buyers as part of a marketing strategy. If statements were sent directly from the city financial offices to underwriters, more detailed and technical defenses and exhibits could be used than those presently used by elected officials and newspaper reporters.

New York City has had a law for years requiring that it finance its expenditures from current receipts. [62, p. 188] This law was obviously not enforced. If it had been enforced over the years, the deficit would have never accumulated to the unmanageable figure it did. If New York City had had regular independent audits for legal compliance, more attention might have been directed towards this illegality. If the city had had reporting requirements, the national investment community would have been aware. Bond holders could have pressured the city through letters, through their personal and political influence, and by threatening not to buy any more New York City securities. Without pressure from bond holders, this illegality was not resolved, although it might have been resolved earlier if the taxpayers of New York City or the Attorney General of New York State had sued the City in New York State court or the political situation had been different. This kind of intervention was unlikely because it would have resulted in an increased tax rate.

As discussed in the second chapter, if the current legal cases relating to the SEC's right to sue a municipality and standards of fraudulent action had been resolved years ago, the SEC might have sued New York City in federal court for not disclosing the material fact that they were violating their own budgetary laws. Even if the SEC had been unsuccessful, resulting publicity would have probably brought increased market pressure on New York City. Suggestions currently being considered but not yet adopted that might have prevented the large accumulated deficited in New York City are: a required independent auditing for legal compliance or budgetary accounting, reporting of the audit results to the SEC or bond holders, and legal standing for SEC involvement.

Chart III-5

Disclosure Recommendations Given for Information on Property Tax Rates and Levies

Types of Descriptive Information

Recommending Report	Trends of Tax Revenues by Type of Tax	Trends of Property Tax Levies	Property Tax Levies and Rates of Overlapping Units	Rates for Each Type of Tax	Property Tax Rate	Tax Authority Limit
1951 New York City Report	Yes	Yes	No	No	Yes	No
1963 IBA Format	No	Yes	Yes	No	Yes	Yes
1965 State Technical Assistance Report	Ambiguous	Yes	Yes	No	Yes	No
1976 MFOA Disclosure Guidelines	Ambiguous	Yes	No	Ambiguous	Ambiguous	Yes
1976 Williams-Tower Bill	Yes	Yes	No	Yes	Yes	Yes

C. Property tax rates and levies

Property taxes are the most important locally generated revenue source, averaging 37.2% of total revenues in 74 major metropolitan areas (see Figure III-1). [58, p. 7] However, this percentage varies a great deal mainly because of state aid policies and the use of other taxes such sales, payroll, and income for local tax revenue (see Table III-1). Property tax revenues are dependent on the value of the total property tax base, assessment practice, the tax rate, and the collection rate. Some municipalities are legally limited as to the rate of taxes that they may impose. Assessment practices and tax rates are determined through various political procedures. Whether the effective tax rate can be reasonably increased might affect bond security.

The property tax rate must be known to relate the size of the tax levy and the tax rate. Many cities are now in the position of having such high property tax rates that property owners are claiming hardship and threatening to move from the city or to abandon rental property. If analysts wish to explore the validity of those claims and form a hypothesis about whether the city can reasonably raise taxes if more revenues are needed to pay debt service, they must know the effective tax rate and compare it with that of other cities (see Table III-3). The effective tax rate is the actual rate times the assessment to sales ratio. Assessed value may range from 20% to 100% of market value and may vary within a municipality by type of neighborhood, type of property, date of last assessment, and the formula used by the assessor. The tax burden on property also includes the property tax rate imposed on the property by overlapping units and fees charged for vital services to property, such as for water and sewer connections.

In 1975, 109 out of 169 issuers included the current property tax rate in the official prospectus statement (Summary of Reporting Practices). [63, p. 271] The Williams-Tower Bill would require the disclosure of "tax rates" and of the legal limit on taxing authority. [63, p. 7] The wording on both the Summary of Reporting Practices and the Williams-Tower Bill is unclear as to whether it means the actual or the effective tax rate. The MFOA guidelines never specifically require either the actual or the effective property tax rate, although it does suggest including the legal tax limit, procedures, and the unused taxing margin in the prospectus statement. [33, p. 7]

Cities may find that it is inconvenient to have to change their financial statements when property taxes are raised. Its financial offices may need to have prospectus statements ready for the printer two months before a bond issue is sold and during that time, the tax rate and other financial policies may be changed. If statements were released that did not report the most current tax rate, the city might be said to be misrepresenting the situation by omitting a "material" fact. Some might argue that the possibility of increases should be disclosed. This could create polical difficulties if the increase is controversial.

Table III-3

Effective Property Tax Rates in 1972-1973 in Some Cities

City	Effective Rate per $1000 of Market Value ($)
Atlanta	13.93
Boston	52.20
Cincinnati	21.85
Cleveland	21.84
Dallas	10.95
Detroit	21.43
Houston	10.02
Kansas City	21.14
Milwaukee	45.37
New Orleans	10.92
New York	26.72
Philadelphia	26.09
Pittsburgh	30.84
St. Louis	19.39
San Francisco	28.39

Source: (Compiled from) Department of Finance and Revenue, Washington, D.C., Major State and Local Tax Burdens in Washington Compared with Those in the 30 Largest Cities, as quoted in Boston Redevelopment Authority. "Boston's Economic Program: Planning and Development for the 1976-85 Decade". (Draft), January 1976, Table III.

Chart III-6

Disclosure Recommendations Given for Property Base Information

Types of Descriptive Information Recommended

Recommending Report	Names and Assessed Value of Largest Taxpayers	Trends of Total Assessed Property Value	Trends of Total Market Value of Property	Ratio of Assessed-to-Market Values of Property	Trends of Property-Values by Type of Property	Value of Tax-Exempt Property	Description of Assessment Practices
1951 New York City Report	No	Yes	No	Yes	No	No	No
1963 IBA Format	No	Yes	Yes	Yes	Real estate/ Personal Property/ Public utility/ Other	No	No
1965 State Technical Assistance Report	Ambiguous	Yes	Yes	Implied	Ambiguous	No	No
1976 MFOA Disclosure Guidelines	Yes	Yes	Yes	Implied	Industrial/ Commercial/ Utility/ Other/	No	Yes
1976 Williams-Tower Bill	Yes	Yes	Yes	Implied	If required by the SEC	If required by the SEC	Yes

D. Property base

The property tax base is the total of all taxable property and excludes tax-exempt property even though it uses city services. Taxable property is described by an estimated market value and by an assessed value. There are a variety of ways to determine market and assessed value and they often yield different results. The actual market value of a particular property is dependent on the demand for that location, which may vary over time. The assessed value is determined by low- or medium-ranked civil servants or by elected officials. They may use a percentage of the last sales price of the property, a percentage of the last sales price of similar property, a multiplier of the reported income from the property, a percentage of the estimated replacement cost, or other methods. There is a large, arbitrary element in assessment and in estimating market value. Ordinarily, high property tax revenues are generated by highly capitalized industrial and commercial uses and by the more wealthy residential neighborhoods.

In 1975, 109 out of 169 issuers gave at least some indication of the property tax base in the prospectus, as shown by the Summary of Reporting Practices. [63, p. 271] All of the mentioned committees which recommended municipal disclosure included the total market and assessed values of property. The 1976 MFOA Disclosure Guidelines were the only recommendations requesting an explanation of any changes in assessment practices, and a breakdown of the taxable property base into its residential, commercial, industrial, and utility components over each of the last five years. [33, p. 8]

Like other information that may be considered for municipal disclosure, information on the property base must be examined for its relevance and cost. Some information on land use is available in cities because it is used for local planning efforts and other reports to citizens, although it is expensive to collect and keep up-to-date. In addition to providing some indication concerning the ability of the locality to bear property taxes, land-use breakdowns also provide an indication of its basic character. Some municipal bond issuers are "bedroom communities" in which most of the taxes are paid by individuals. Other municipal issuers have strong industrial components, which yield property tax revenues of sufficient size to reduce the tax burden on individuals and residential property. This understanding is important in an analysis of property tax revenues and effective rates. However, it is not at all clear that such breakdowns are needed for every year. The trends of the land use composition can be seen by comparing the tenth, fifth, last, and current years as suggested by the 1965 State Technical Assistance Report. [1, p. 40] Information on tax-exempt property is not recommended by any of the commissions. Although tax-exempt property is not significant in most municipalities, some cities have not only religious property but also tax-exempt property housing cultural, educational, and governmental institutions benefiting the entire region. For these cities (such as Boston where 56% of the total assessed valuation in 1972 was tax-exempt [38, p. 19]), the tax-exempt property represents important lost revenues, which a legal change might bring into the taxable property base.

Five out of the eighteen most highly rated indicators on the Indicator Survey were characteristics of the taxable property base. Of the seventy-four indicators on the survey form, the bond dealers rated "assessed taxable value of commercial property" as sixth, "assessed taxable value of residential property" as eighth, "estimated market value of commercial property" as fourteenth, "estimated value of residential property" as fifteenth, and "assessment practice information" as eighteenth in importance. These results show a basic agreement with the suggestions of the 1976 MFOA Disclosure Guidelines, supporting their expansion of earlier recommendations. The bond dealers surveyed also rated "percentages of property excempt from taxation by type of property and adjusted assessment" 27th out of 74 in importance representing a mean importance rating of 2.0 (on a scale of 1 to 5 in which "1" = "very important" and "5" = "irrelevant"). This result is ambiguous.

Investors must not force upon cities the expense of more frequent land inventories than needed for local planning. The U.S. Census Bureau should explore the possibilities of making its reporting more consistent with the needs of the municipal bond market as shown by the results of the Indicator Survey and further studies. If the Census does, it may reduce possible conflicts over data collection and reporting responsibilities between overlapping units of local government and data will be more standardized and comparable.

Chart III-7

Disclosure Recommendations Given for Tax Collection Rates and Procedural Information

Recommending Report	Short Description or Trends of Delinquency Rates	Detailed Description of Delinquency Rates	Audit of Adequacy of Procedures
	Types of Descriptive Information Recommended		
1951 New York City Report	Yes	No	No
1963 IBA Format	No	Yes	No
1965 State Technical Assistance Report	Yes	No	No
1976 MFOA Disclosure Guidelines	No	Yes	No
1976 Williams-Tower Bill	Yes	If required by the SEC	No

E. Tax collection rates and procedures

Property tax reveneus are dependent on the taxable property base, assessment practices, the property tax rate, and the collection rate of taxes due. Uncollected property taxes can range between a fraction of one percent and over ten percent of the total annual property tax levy. Municipalities charge interest on delinquent taxes and after a certain time have the right to forclose on the property and sell it at public auction to pay the tax bill. If property owners feel that their taxes are unfairly high, they may apply for an abatement. A low rate of property tax collections is significant because it represents lost or delayed revenues and increased administration costs. It may also represent inefficient financial management, deterioration of urban properties, and widespread personal financial setbacks.

Property tax collections were a widely publicized problem of New York City. Some landlords collected rents until the City foreclosed. The City's tax collectors billed exempt properties such as schools, embassies, and public housing projects in error and then represented them as receivable revenues. [62, pp. 155-156] A 1975 audit report noted...

> "Under a disciplined accounting system, all of the accounts receivable would be collected and converted into cash within a relatively short period of time. Borrowing needed to finance the accounts receivable. To the extent, however, that the accounts receivable are inflated, then the municipality would have a deficit which must ultimately be paid by means of appropriations." [62, p. 189]

When one New York City note holder saw the audit report showing that real estate receivables were overstated by $408 million and pledged against $380 million in tax anticipation notes, he wrote to the U.S. Senate that, "...a massive public fraud has taken place with the knowledge of elected and appointed public officials". [62, p. 148] The tax collection rate and the accounting of delinquent taxes are both important in financial management. If that investor had known how New York City accounted for delinquent taxes, he might not have bought the tax anticipation notes. If the City had been forced to tell investors how it accounted for delinquent taxes, it might have been pressured into more sound practice. This incident is an example of why voluntary disclosure guidelines are ineffective in protecting investors. In fact, one of the recommendations of the 1951 New York City Report shows an anticipation of such a situation. New York City officials ignored the recommendation that the City should include in notices of bond sales a "Three year record of property tax collections and delinquencies... (and a) description of tax collection machinery, especially regarding delinquencies (and) penalties". [1, p. 37]

The consensus of bond dealers surveyed, the rating agencies, and the writers of the 1976 Williams-Tower Bill, the 1976 MFOA Disclosure Guidelines, the 1965 State Technical Assistance Report, the 1963 IBA Format, and the 1951 New York City Report is that the administration of delinquent tax accounts and the rate of delinquency are important. About one-fifth of the volume of the three-page format suggested by the Investment Bankers Association for general obligation bonds is devoted to information on delinquent taxes. It asked for three years of: "Amount of Levy by This Issuer", "Uncollected at End of Year", "Uncollected (at) Latest Available Date", and "Delinquent Taxes from Prior Years Collected During Year". The format also asks for a great deal of other detail on property tax delinquencies including responses to these questions:

1. Taxes for fiscal year are due ______________________________;
   Became delinquent ____.

2. If payable in installments, give particulars. _______________
   ____.

3. Discounts for prepayment and when applied? __________________
   ____

4. Specific practice for delinquency? __________________________

5. Explain in detail any modifications of practice during the past two years ____.

6. How are uncollected taxes handled?

   (a) Anticipated as revenue in next year's budget? __________.
       If yes, what percentage? _________________________________.

   (b) Turned over to other governing bodies? _________________.
       If yes, when? ____.

   (c) Sale of tax certificates? ______________________________.
       If yes, when? ____.

   (d) Other methods ____.

7. Has tax sale period been extended in last two years? ________.
   If yes, explain. ____.

8. Accumulated total of uncollected taxes for fiscal years prior to those reported above? $_____________________________________.

9. Are tax title liens included in uncollected tax totals above?
   ____________________________ How much? $____________________.

10. Total tax title liens owned by municipality. (Years 19__ to 19__, inclusive) $____.

....

13. Do you levy taxes in excess of actual requirements to provide margin against delinquencies? Yes_____ No_____. If yes, what ratio?__________. Current year? _____%. Previous year? _____%. Two years ago? _____%. [1, p. 66]

The 1976 MFOA Disclosure Guidelines goes into great detail about property tax collection experiences. It suggests the following procedures:

"Include descriptions of (1) the manner in which delinquent taxes are collected; (11) the interest charged on delinquent taxes; (iii) important changes in the last five years in tax...collection practices; and (iv) the reasons for such changes. State the value of total tax liens owned by the issuer as of the end of its last five fiscal years and as of a recent date. Describe briefly the procedures followed in foreclosure, including extension of foreclosure dates. Describe the priority of tax claims of the issuer over other indebtedness of taxpayers.

State whether real estate, sales, income, or other taxes are levied in excess of actual requirements to provide a margin against delinquent taxes and, if so, give the amount of such excess taxes expressed as a percentage of total taxes levied for the issuer's last five fiscal years and as of a recent date and the tax delinquency rate for each of such fiscal years and for the current fiscal year to date. Describe any anticipation of collection of delinquent taxes in budgets for current or future years. State whether borrowing is made against delinquent taxes ,and if so, state the percentage of delinquent taxes so financed as of the end of such prior fiscal years and as of a recent date. Describe the accounting principles applied in writing-off delinquent taxes, and state the period for which delinquent taxes are reflected on the issuer's books before they are written-off." [33, pp. 8-9]

The city must be careful not to appear contradictory as it tries to make two points: (1) The city's tax claims are more important than those of other creditors. (2) The city's notes and bonds are in no way less secure because of tax delinquencies. The web of case and statutory law involved with the priority of tax claims of the issuer over other indebtedness of taxpayers is technical and dynamic and its relation to total revenues is obscure. It may be appropriate but politically controversial to report on the handling of the delinquencies of very large taxpayers, such as the bankrupt Penn Central Railroad, which owns a great deal of property in New York City, Boston, Philadelphia, and other cities. In addition to property for its own use, it owns property such as Carnegie Hall, which it rents to other users. [58, pp. 164-165] Penn Central was excused from property tax payments when it filed bankruptcy, but if it becomes financially solvent, it may possibly repay them.

The 1965 State Technical Assistance Report considers sharing of delinquent tax accounts to be an example of the quality of financial management. [1, p. 43] However, foreclosure procedures and interest charges are matters that have local political implications and may involve policy trade-offs between tax collection and strategies in deteriorating urban areas. They should be resolved by the community and its administration. Investors should not dictate such policies. Much other evidence could be provided on the quality of financial management and the adequacy of tax revenues.

Reporting of collection of delinquent taxes is another area of disclosure that would be very affected if independent audits became routine. Peat, Marwick, Mitchell, & Co., a leading accounting firm, described their modern approach to government auditing as using "system evaluation". They identified the tax assessment/billings/collection process as a key cycle. The auditor should, they say, consider the organizational objectives, identify the internal control features, and evaluate their effectiveness. [16, p. 16] The auditor may be able to give the city financial management some suggestions on how to improve efficiency. The auditor assumes some responsibility for the accuracy of the analysis.

Why is disclosure in such detail of tax collection policies recommended? If purchasers and bond dealers spend as little time reading prospectus statements as the results to one question (on the Indicator Survey) showed, could they learn more by looking at other data? Whether it is important or not, however, the market seems to want it. Respondents to the Indicator Survey gave a relative importance ranking to "Records of tax collections compared to tax accruals", placing it fifth out of 74 indicators. Cities should experiment with substituting an auditor's statement on the sufficiency of reserves for uncollected taxes and abatements and a statement on handling of funds from delinquent taxes paid and from foreclosures. If legally allowed, the city might not distribute such statements unless requested. Its prospectus and annual reports distributed to bond holders could refer to the existence of such statements but not go into great detail. The prospectus could include figures using standardized definitions of trends for abatements granted and for "Amount of Levy by This Issuer", "Uncollected at End of Year", "Uncollected (at) Latest Available Date" and "Delinquent Taxes from Prior Years Collected During Year", as the IBA suggested. [1, p. 66] If other cities conduct surveys like the Indicator Survey, they can ask whether such a policy is acceptable, but if most respondents are negative, the city should provide them with the information.

Chart III-8

Disclosure Recommendations Given for NonProperty Tax Revenues

Types of Descriptive Information Recommended

Recommending Report	Itemization of Tax Revenues by Type of Tax	Tax Rates	Description of Transaction or Wealth that is Taxed	Taxing Authority
1951 New York City Report	Yes	No	No	No
1963 IBA Format	Ambiguous	No	No	Yes
1965 State Technical Assistance Report	Yes	No	Yes	No
1976 MFOA Disclosure Guidelines	Ambiguous	No	No	Yes
1976 Williams-Tower Bill	Yes	Yes	If required by the SEC	Yes

F. Locally generated revenues other than those from property taxes

In 1973-74, nonproperty taxes, charges, and miscellaneous revenues locally raised accounted for an average of 24% of total general revenues for 74 major SMSA's. [55, p. 7] (See Figure III-1, p. 74) However, the amounts of these revenues varied a great deal between metropolitan areas. (See Table III-1, p. 75) These taxes and fees include retail sales taxes, income taxes, payroll taxes, public utility taxes, tobacco and liquor taxes, admissions and amusement taxes, motor fuel taxes, business license taxes, transport revenues, sanitation revenues and hospital revenues.

Most of the sets of disclosure recommendations include nonproperty taxes and other locally generated revenues. The 1951 New York City Report recommended reporting of trends of revenues by class and an itemization of local nonproperty tax revenue for three years. [1, p.37] The 1965 State Technical Assistance Report recommends that revenues be itemized to reveal in particular the relative size of each nonproperty tax. [1, p. 65] The 1976 MFOA Disclosure Guidelines is more vague; it recommends reporting of whether sales, income, or other taxes are levied at a higher rate to provide a margin against delinquencies and reporting of taxing authority, nonproperty tax rates, or a description of taxable transactions or wealth other than property. [33]

The emphasis by some analysts on the property base and property taxes is misguided. Property taxes were instituted when ownership of property represented wealth. However, not all apartment houses and other commercial property generate high profits, while many very profitable businesses operate out of small, rented offices. Sales and special retail taxes, income taxes, payroll taxes, and some other taxes are seen as a way to tax these businesses and commuters who use city facilities. If a city does not have the legal authority or political strength to distribute the burden of its taxes, greater pressures will be exerted on the wealth which is represented by property.

The ability to impose a nonproperty tax depends on the form of the charter of the municipality. Those with stronger home-rule provisions find it easier to choose the forms which their taxation will take. Sometimes, state legislation, a referendum, or a charter amendment is needed before a nonproperty tax can be imposed. The taxing authority of the issuer is a critical indicator of its ability to generate revenues, and so it should be summarized in the prospectus statement.

How much descriptive detail is important? Some might argue that a description of the value of what is being taxed should be given for nonproperty taxes in a similar manner to the way in which the property base is considered to be rightfully the responsibility of the city to describe to investors. If the city has a sales tax, should it give investors an estimation of retail sales? If the city has a tobacco sales tax, should it tell investors how many packages of cigarettes were sold last year? Reasonably, New Orleans, where 41% of tax revenue is from a retail sales tax, [58, p. 105] might give more information on retail sales than another city. Other revenue sources particular to given cities, such as a tax on use of an airport, might also merit further attention. In such cases, space requirements might justify correspondingly less information on its property tax base in short statements.

Nonproperty taxes are more difficult to forecast than property taxes. Their revenue levels change because of fluctuations of personal incomes, retail sales, attendance, and other sources. This makes it more difficult to plan a budget. For these reasons, and because of the shortage of quantitative information on their bases, it is more important to establish a range by examining trend data than it is for property tax revenues. This information should be easily obtainable from existing files. As suggested for property tax collection rates, an independent auditor might be able to reduce the city's vulnerability to political criticism or charges of misrepresentation if a statement were prepared for the city's use on the adequacy of its budgeting and contingency funds for nonproperty tax revenues.

As mentioned earlier, data collection is expensive. One city used data collected by a private retailer's trade magazine in its prospectus. [7, p. 18] Such information lacks the authority of Census data. Its potential usefulness to analysts has to be weighed against the possibilities that such information may be inaccurate or misleading.

It might be very expensive and politically difficult to develop detailed mandatory information requirements for various activities or wealth other than property, which might be taxed. Perhaps a review panel could make nonmandatory suggestions on the consistency of detail appropriate. Perhaps the city could develop a file of information on these subjects, including information collected by nonofficial sources and make it available to interested analysts. Perhaps cities should be allowed to release certain information with a disclaimer of responsibility.

Chart III-9

Disclosure Recommendations on State and Federal Aid Information

Recommending Report	Types of Descriptive Information Recommended			
	Trends of Total Aid	Aid by Category of Use or Program	Total Aid for Which Elgible	Statement regarding Continued Aid
1951 New York City Report	Implied	No	No	No
1963 IBA Format	Yes	No	No	No
1965 State Technical Assistance Report	Implied	Yes	No	No
1976 MFOA Disclosure Guidelines	Ambiguous	Only when extraordinary	No	Ambiguous
1976 Williams-Tower Bill	If required by the SEC	If required by the SEC	Yes	No

G. State and federal aid

Inter-governmental aid is an important revenue source for most cities. In 1973-74, aid from state governments to local governments operating in 74 major SMSA's accounted for an average of $226 per capita or 31% of general revenues. Aid from the federal government accounted for an average of $55 per capita or 8% of general revenues. [58, p. 7] (See Figure III-1) Other aid is sometimes available from county governments or surplus-producing enterprises. The amounts of aid vary greatly between cities and over time. Because of their importance to total revenues, the situation of inter-governmental received by each issuer should be disclosed to analysts. The current total aid and future levels of such aid available for general use must be considered as well as the importance of the aid to particular expenditures, such as those for debt service, school operations, and capital improvements.

The wealth of the state and the political influence of the city are important factors in the amount of aid received. The financial reputations of the state and of large cities are intertwined. This is not a new concern. Could a policy of regular reporting to bond holders have changed the following situation? In the late 1950's, the State of Michigan generously aided local governments providing 40% of all school districts general fund revenue, one-quarter of general revenue receipts of the twenty largest cities, and one-third of county revenues. The State experiences a series of financial crises resolved by imposition of a new tax, updating collections of other taxes, and a much publicized one-week delay in meeting a payroll. Neither the State nor the local units were late on payments due to bond or note holders. However, because of these events, the interest costs that Michigan municipalities were forced to pay after this were much higher -- on full-faith-and-credit bonds rated A, Aa, and Aaa, it is estimated that interest costs averaged 10-15% higher to maturity. [16, p. 429]

Just as analysts are concerned with citizens' attitudes towards paying taxes and avoiding default, they are concerned with the state government's attitude and ability to maintain needed and accustomed aid. The State of Michigan had previously cutback state aid sharply to balance state finances which might have predisposed investors to their strong reaction. Similarly, investors learned to distrust New York State through experiences with the New York Port Authority and the Urban Development Corporation. [15] For this reason, information on past actions of the state or current considerations of aid cutbacks may be relevant. However, such a requirement may infringe on the state political domain. If legally acceptable, a simple and general statement about the trends of state aid, the need for periodic legislation to continue various programs, the designated uses of program funds, and severe problems of state finances should suffice for the purposes of analysis.

This area of disclosure has clear possiblities for conflict of interest. It would be best for the city if the state government were to provide it with a statement on its policies towards aid and the sufficiency of state finances. It may not be to the political advantage of the state administration to do so, particularly if the city is large with a great deal of influence and a large budget. However, consitutional limitations on federal powers might make it difficult to require such participation from state governments.

Some cities have been including statements on the future of state aid in their prospectus statements. The City of Albany, New York, for instance, has this statement in a prospectus of about thirty pages:

> "If during the term of the bonds a significant default or other financial crisis should occur in the affairs of the State of New York or any of its agencies or political subdivisions including the City of New York, the resulting effects may substantially impair the ability of the City of Albany to sell other obligations including notes or bonds to renew or fund outstanding short-term debt. Moreover, any such default or financial crisis may substantially impair the marketability of the Bonds for resale purposes. The failure by one or more major government issuers outside New York State may also have an impact on the marketability of the Bonds or the ability of the City to sell other olbgiations." /_7, p.2_/

Is it necessary to raise the possibility of such an extreme in their official statements? Does the language suggest to bond buyers that they should not but this or other bonds of Albany? Is it the duty of a municipal issuer to try to educate a bond buyer about the secondary market in municipal securities? Cities should not be forced to dwell overly long on the negative possibilities of their associations in reputation. They should not be responsible for notifying their bond holders of financial problems of other governmental units that will not be reflected in aid cutbacks or direct costs. In this case, a cautionary statement about potential cutbacks in aid from New York State to Albany in event of more financial problems in New York City should be more than sufficient.

Issuers should be careful in projecting future levels of state and federal aid and analysts should be careful in accepting issuer's projections because they are not in local control. One recent incident involved Lennox Moak, mentioned several times as a financial expert and Director of Finance of Philadelphia. In late 1975, he placed an advertisement for the City's bonds in The Wall Street Journal that referred to a surplus in Philadelphia's budget several months earlier and proclaimed the City's financial health. This estimatation of the City's finances included $65 million in anticipated budget revenues dependent on the enactment of state and federal legislation. As many analysts and market experts predicted, this aid did not materialize. As mentioned earlier, the SEC launched an investigation of the City because of this incident. [47, p. 1]

Was it appropriate for investors to rely on projections placed in a newspaper advertisement? If Pennnsylvania had been required to give Philadelphia a statement for its prospectus about the possibilities of aid, would the City's financial officers pursued a different strategy in marketing bonds? What sort of statement could the State have given the City in such uncertain circumstances? If the State had given the City a statement and the City had used it in its advertising and somehow made an inaccurate projection, would the SEC have investigated or sued the State?

Perhaps because state and federal aid were not an important source of local government financing until the last few decades, most of the disclosure recommendations given are vague on reporting of such aid. The 1963 IBA Format asks for the trends of total state and federal aid for the last three years but goes into almost no detail, unlike its format for reporting property tax revenue. [1, p. 65] The 1951 New York City Report recommends disclosure of revenues by source but does not specifically discuss inter-governmental aid. [1, p. 37] The 1976 MFOA Disclosure Guidelines do not recommend reporting levels of inter-governmental aid although they might be apparent from the operating statements it recommends. [33] The 1976 Williams-Tower Bill would require a report fo the "nature and extent of federal or other assistance programs available to ths issuers", [63, p. 8] but this seems impractical.

The results of the Indicator Survey are somewhat helpful in this question. As mentioned before, bond dealers surveyed were very interested in the sources of revenues and their trends. They also rated "total state and federal aid and as percentages" as thirteenth in importance out of 74 indicators giving it a mean importance rating of "1.6" on a 1-5 scale. (Indicator Survey) This shows that it is necessary to report something about the levels of state and federal aid, although, as mentioned before, in 1975, only 15 out of 174 issuers included a detailed statement of sources of revenues in their offering circulars. (Summary of Reporting Practices) [63, p. 271]

The amount of detail on use of inter-governmental aid and its continued levels that should be reported is still unclear. The possible uses of state and federal aid are very important because not all aid may be used for debt service. If concern is with the risk of outstanding debt, the most useful funds are those that have no restrictions on use and those predesignated for vital or debt services. Aid predesignated for nonessential services and functions or for deferrable capital facilities is less helpful in avoiding a potential default situation. Different ways of measuring the relative aid for comparison purposes may result in varying answers. Per capita figures may not reflect aid to overlapping units or for special facilities used by the people living in a large region. An argument can also be made that state aid to low-income and elderly people should not be counted as aid to local governments.

The 1965 State Technical Assistance Report recommends that the prospectus include revenue from state and federal governments classified by use for operations, capital outlays, and debt service. [1, p. 40] This seems helpful, although it may be appropriate to further differentiate between aid used for the regular functions of that municipality, such as schools, and that for some extraordinary purpose, such as disaster relief or pollution control. It may be useful to draw on the reporting experience of the requirements attached to Federal Revenue Sharing Funds. [64] Identification of the particular aid programs that account for large amounts may be useful to analysts who have access through other sources to discussion of cutbacks and expansions of aid programs. In fact, it may be possible that bond owners could become effective advocates for those cities, because they are often wealthy individuals or institutions having influence. Cities should do further opinion surveys to determine whether they are meeting the information needs of market participants who handle their securities and if they can increase interest in aid discussions.

H. Summary and Conclusions

Revenue analysis is concerned with the sufficiency of revenues and the ability of the city to estimate them. The city must show analysts and investors the revenue aspect of its financial structure and prove that revenues will continue to be sufficient and competently managed.

Politically, the city's greaters risks are that investors might disapprove of tax rate increases, tax collection policies, and sources of tax income. Conflicts with the state government might increase because of the pressure on both to tell the investment community about future state aid.

With disclosure and independent analysis, as with analysis by the rating agencies, there is the possibility that communities with high tax rates and low levels of taxable property will be labelled "poor quality investments" and be forced to pay higher interest rates. With disclosure, however, such communities may be able to demonstrate an attitude that will reassure bond investors.

The disclosure recommendations reviewed generally do not show enough concern about revenue sources. Their attention is overly focused on property taxes, which now account for a much smaller share of local revenue sources than they did twenty years ago. It is more important for the investor to understand the circumstances affecting state and federal aid than it is to understand some of the detail on property taxes recommended. Investors must learn to understand what is involved with new tax sources such as commuter taxes. Operating statements are not very useful for analysis and are too long to conveniently distribute. The Census Bureau could be helpful by collecting standardized information on taxable assets and transactions.

Accounting techniques used in revenue management are very important -- they should probably be standardized and should be definitely reported and audited. An independent audit may help to provide credibility, while reducing the need for disclosure of details tat are politically sensitive or hard to pinpoint. An auditor's report may be helpful, in particular, to establish the adequacy of budgetary accounting, contingency funds, and tax collection procedures.

IV. Disclosure of Debt Information

The debt structure is the most important aspect of city finances in municipal credit analysis. According to one text:

> "Debt implies the use of revenues from outside the current tax structure, the annual payment of principal and interest, the encumbering of credit and anticipated revenues, and the assumption of long-term liabilities in return for long-term benefits. Analysis of debt is frequently avoided because of its complexity, its dynamic nature, and the long-term economic effects which make forecasting difficult and evaluation beyond currently available data, dangerous" [34, p. 38]

Possibilities in analysis of a particular debt structure must be understood before one can design a presentation of the facts that will facilitate analysis and perhaps even suggest conclusions. It is even more difficult (and requires greater understanding) to specify details of disclosure requirements (for the debt structure of various categories of municipal structures) in such a manner that interpretations are not unwisely pre-biased. when the specifications are used for a particular municipality.

As with all parts of a bond analysis, the city debt structure may be examined with the goal of establishing a "quality opinion" applicable to all of its outstanding debt, or it may be examined with a particular interest in a long-term or a short-term issue. An analysis of short-term debt is more directed towards immediate cash-flow than is an analysis of long-term debt. The latter is concerned with a city's ability to meet payments on bonds that may mature in as many as forty years (although most mature sooner), and it should include an examination of how the issuer's policies and reliance on short-term debt affect this. A general analysis is concerned with these subjects and with the city's patterns of borrowing as they reflect a debt management policy. Although it is unknown exactly how investors and the rating agencies analyze or should analyze bonds, it is clear that the most rigorous analysis is directed towards the debt structure. Not only does the analysis affect the interest rates, but the interest rates affect the analysis. The debt structure of various cities vary in many ways -- Table VI-1 compares short-term interest rates, long-term interest rates, and ratings of some cities. (see page 121)

The following charts present applicable data from the Indicator Survey showing how important various debt information is to bond dealers and data on existing reporting practices. Other charts, preceding chapter sections, compare the recommendations given for disclosure of debt information by the 1951 New York City Report, the 1963 IBA Format, the 1965 State Technical Assistance Report, the 1976 MFOA Disclosure Guidelines, and the 1976 Williams-Tower Bill. This chapter has eight sections: (A) Short-term debt structures, (B) Past and current levels of long-term debt, (C) Overlapping debt structures, (D) Authorized debt and the possibilities of increasing outstanding debt, (E) The uses of outstanding debt, (F) Debt retirement schedules, (G) Legal debt limits and debt-weighting ratios, and (I) Summary and conclusions.

Chart IV-1

Frequency of Reporting Debt Information in 1975

Section of Chapter IV in which Discussed	Indicator	Reporting	Not Reporting
B	Direct debt statement, 1975	165	9
B	Statement of direct debt outstanding within 120 days of sale	149	25
G	Statement of direct debt for prior five year period	7	167

Source: (Excerpted from exhibit submitted by Professor Ronald Forbes, New York University) U.S. Congress Senate. Committee on Banking, Housing, and Urban Affairs. Hearings before the Subcommittee on Securities on S. 2969 to Amend the Securites Exchange Act of 1934 to Require the Preparation of Annual Reports and Distribution Statements by Issuers of Municipal Securities, and for Other Purposes, S. 2574 to Amend The Securities Act of 1933 to Provide for Registration of Securities Issued by State and Local Governments, February 24, 25, and 26, 1976. 94th Congress, Second Session, Washington, D.C.: U.S. Government Printing Office, 1976, p. 271.

Chart IV-2

Results of Questions of the Indicator Survey Concerning Debt Information

Section of Chapter IV in which Discussed	Indicator as listed on survey form	Relative Importance Ranking (out of 74)	Mean Importance Rating (on 1-5 scale)	Proportion Desiring Comparative Data (%)
B	Total debt outstanding	1	1.2	67
H	Debt per capita ratio	2	1.2	80
H	Funded debt outside of legal debt limit	3	1.2	56
-	Net indebtedness	4	1.3	68
F	Debt retirement schedule	9	1.9	44
H	Combined debt as a percentage of market value	17	1.7	64
D	Projected capital expenditures for public facilities	20	1.7	38
C	Number of overlapping jurisdictions with debt issuing capacity	23	1.8	32
-	Statement of assets and liabilities over five years	24	1.9	36

Chart IV-3

Disclosure Recommendations on Short-term Debt Structure Information

Recommending Report	Amount of Short-term Debt	Trends, Uses, Categories, or Other detail	Amount of Short-term debt of Overlapping units
	Types of Descriptive Information		
1951 New York City Report	Ambiguous	Ambiguous	Ambiguous
1963 IBA Format	Yes	Categories of security	No
1965 State Technical Assistance Report	Ambiguous	No	Ambiguous
1976 MFOA Disclosure Guidelines	Yes	If used for Operating expenses	Yes
1976 Williams-Tower Bill	Yes	If required by the SEC	If required by the SEC

A. Short-term debt structures

There are three commonly used classifications of short-term debt contracts that are sold to underwriters and, through them, to other institutions and private citizens. These are Bond Anticipation Notes (BAN's), Tax Anticipation Notes (TAN's), and Revenue Anticipation Notes (RAN's). They are issued to cover cash needs until the particular funds pledged are received from bond sales, tax collections, or other revenues. The security of the short-term note depends on the likelihood that the particular funds against which they have been issued will appear, and on the actions planned if there should be a fund shortage. Legally, in event of default, bond holders have priority over note holders. Theoretically, this means that if an issuer does not have sufficient cash on hand to pay both bonds and notes coming due in a given month, the bond holders will be paid first and the note holders will have to wait until sufficient revenue is received. The lien situation is complicated because of other encumbrances on revenues and the general legal inexperience with municipal default.

Capital market interest rates for short-term securities are different at any given time than those for long-term securities. The typical buyer of a note has different needs and circumstances from those of the buyer of a bond.

A municipality may be able to borrow from local banks or from the state government. These loan contracts have different terms than the notes nationally marketed. The municipality may also be able to borrow interest-free from unwilling creditors by delaying payments owed.

Information on short-term debt intended for investors in long-term securities should be handled differently from that intended for investors in short-term securities. In the short-term, cash-flow is important, and the passage of a few months might significantly alter the financial picture. Moody's has recognized this and has instituted Municipal Investment Grade (MIG) Ratings for short-term securities. The rating agency monitors a city's monthly cash receipts and verifies the complete repayment of TAN's with tax receipts of that fiscal year. [23] Other short-term notes should also be paid by the source of funds predesignated for repayment at the time of issue. New debt should not be incurred to finance their redemption.

Most municipalities have not recognized that the information relevant to short-term debt is different from that which is relevant to long-term debt. The municipalities often use the same basic prospectus for note buyers and bond buyers. Most of that information shows the long-term financial picture but is too dated to be useful in evaluation the risk of notes.

Independent analysis of short-term securities, like that of long-term securities, gives investors an opportunity to make their own judgments about the risk of purchase. Mikesell and Hay suggest that for such purposes, a city should release interim statements detailing the total amount of funds available for the year, the amount of expenditures and encumbrances to date, and the balance available for the remainder of the year. [26, p. 117] More detailed short-term information is currently being released by the City of Philadelphia under a policy developed by Lennox Moak. It includes: monthly cash receipts; statements for each operating fund, each capital projects fund, and each consolidated cash account; quarterly financial statements; and reporting of significant financial developments that may influence projected fund conditions. [37]

Short-term debt policies and debt levels also affect the long-term financial management of a city. In 1973-74, short-term debt accounted for an average of 11.5% of the total debt outstanding in metropolitan areas as reported by the U.S. Census Bureau. /‾58, p. 7_/ An increase in the amount of short-term debt and regular tapping of contingency funds may indicate an increasing delay between receipt of revenues and disbursements. Such situations are difficult to detect. An increase in the amount of outstanding BAN's, however, may be a positive sign because it could be an indication of public-works activity.

Some cities do not have the legal authority to incur short-term debt. However, for those that do, short-term debt can be used to increase the flexibility of city financial management. RAN's and TAN's are used because tax collections and intragovernmental transfer payments are seldom received during the month in which they are most needed to pay bills. If the city maintained a large balance, it would not need to issue TAN's. Unless such balances are mandatory, however, political pressure to postpone tax increases lead to their depletion.

BAN's may be issued to finance the beginning of a project until necessary approvals are given or administrative delays are resolved. Notes may be issued to postpone entrance to the long-term market until the going interest rates become lower. The federal government is encouraging cities to use BAN's for preliminary construction financing of federally subsidized projects until a final cost estimate is determined. /‾23_/ Because the amount of BAN's outstanding is usually higher before a city embarks on a major construction project, trend figures of total short-term debt may be misleading.

The 1976 Williams-Tower Bill would require disclosure of the estimated amount of short-term debt outstanding. The 1976 MFOA Disclosure

Guidelines suggest that debt-service schedules should include short-term debt. [33, p. 6] The 1963 IBA Format suggests that the amounts and maturity dates of unfunded short-term debt be reported and classified as TAN's, BAN's, bank loans, warrants, judgments, unpaid bills sixty days past due, and miscellaneous items. [1, p. 63] The total is to be compared to those of a year and two years ago. This format seems reasonable, although RAN's should be another category and the trends of BAN's should be shown separately.

This thesis recommends that cities make available to note holders statements similar to those released by the City of Philadelphia or suggested by Mikesell and Hay. Such detailed statements with trend data, published annually or more often, should be sent to note holders if they request it. Because of the typical timetable within which most notes are issued, distributed, held, and redeemed, it may not be appropriate to distribute statements of short-term cash-flow information in the same manner in which detailed prospectus statements are distributed to bond buyers. Most notes mature in less than one year, and many in a few months. Most note buyers will probably be unlikely to respond with any sort of comments or questions to annual reports, long prospectus statements (such as currently distributed), or cash-flow statements.

If cash statements are circulating in the marketplace, investors may examine them before they buy the city's notes. If they are released, the existence of the statements may give the city a cooperative image, and the information included may allay some fears about the possibilities of default by certain cities that might be, according to rumor, in financial trouble. The time necessary to conduct an audit means that such figures will probably have to be released without one, although an independent auditor could moniter the city's record-keeping and reporting. While a city would probably want to attempt to disclaim liability for the accuracy of the figures, the potential harm to the city's reputation for reliability in reporting if inaccuracies are exposed would deter deliberate misrepresentation. If cities adopt policies of releasing special statements on short-term concerns, as this thesis suggests, they should avoid the administrative difficulties of assembling names and addresses of note holders and the legal responsibility for statement distribution, if possible, by supporting the assignment of this responsibility upon bond dealers.

Many or most note holders may be uninterested in actually reading cash-flow statements unless default seems imminent. Distribution of the statements to financial journals, such as The Bond Buyer and The Wall Street Journal, and to major underwriters may sufficiently bolster the city's reputation and would enable analysis by those with special interest. If municipalities distributed less information to note holders than to bond holders, however, the SEC might consider them to be withholding material information from note holders.

Table IV-1

Comparison of Long-term and Short-term Interest Rates and Moody's Ratings of Some Cities

City	Long-term Interest Rate	Date of Long-term Bond Issue	Short-term Interest Rate	Date of Short-term Note Issue	Moody's Rating - Aug. 1976
Minneapolis	4.45	4/76	--	--	Aaa
Oklahoma City	4.83	8/76	4.75	4/76	Aa
Kansas City	4.96	1/76	3.19	4/76	Aa
Dallas	5.13	5/76	--	--	Aaa
Louisville	5.17	9/73	--	--	Aa
Jacksonville	5.18	72	--	--	A-1
Milwaukee	5.19	5/76	4.32	5/76	Aaa
Portland	5.24	4/76	4.45	7/76	Aaa
San Antonio	5.34	5/76	--	--	Aa
San Francisco	5.42	9/76	--	--	Aaa
Fort Worth	5.58	2/76	--	--	Aa
Toledo	5.66	9/76	4.00	9/76	Aa
Atlanta	5.71	6/76	4.25	6/76	Aa
Phoenix	5.72	7/76	6.13	7/76	Aa
Denver	5.86	12/74	--	--	Aa

(cont.)

Table IV-1 (cont.)

City	Long-term Interest Rate	Date of Long-term Bond Issue	Short-term Interest Rate	Date of Short-term Note Issue	Moody's Rating - Aug. 1976
Memphis	5.87	--	5.48	4/74	Aa
Long Beach	5.93	8/73	3.74	--	Aa
Oakland	6.00	5/74	7.00	9/76	Aa
Chicago	6.02	7/76	3.98	1/76	Aa
Columbus	6.12	6/76	3.37	6/76	Aa
Baltimore	6.14	5/76	--	--	A-1
New Orleans	6.25	6/74	--	--	A-1
Seattle	6.30	5/76	4.75	6/76	Aa
Nashville	6.3	9/76	4.50	8/76	--
Cincinnati	6.50	4/76	3.50	4/76	Aa
St. Louis	6.52	1/76	6.52	2/76	A
Los Angeles	6.69	5/76	4.25	2/74	Aaa
Pittsburgh	6.77	9/76	4.50	7/76	A-1
Philadelphia	7.69	9/76	8.07	7/76	Baa
Boston	7.86	6/76	7.00	7/76	Baa
Detroit	9.78	6/76	7.00	7/76	Baa

(cont.)

Table IV-1 (cont.)

Source: Long-term interest rates, dates of long-term bond issues, short-term interest rates, and dates of short-term note issues are taken from results of The Survey of Financial Officers

Moody's ratings are taken from Moody's Updated Rating List.

Chart IV-4

Disclosure Recommendations for Information on Past and Current Levels of Long-Term Debt

Types of Descriptive Information Recommended

Recommending Report	Total and Net Debt	Outstanding Debt by Category	Interest Rates	Sinking Fund Balance	Trends of Debt Service Requirements
1951 New York City Report	Trends for five years	No	Aggregated in debt service schedule	Current year only	No
1963 IBA Format	one and two years ago	General obligation/ special assessment secured also by general tax/ utility and public enterprise/ special assessment only	Aggregated in debt service schedule	Current year only	No
1965 State Technical Assistance Report	ten, five, two, and one year ago	by category of liability -- ten, five, two, and one year ago	Aggregated in debt service schedule	Current year only	No
1976 Williams-Tower Bill	If required by the SEC	If required by the SEC	If required by the SEC	If required by the SEC	If required by the SEC

B. Past and current levels of long-term debt

Disclosure of outstanding long-term general obligation debt is not controversial. The level of outstanding debt is generally considered to be a "material" and relevant fact which is often disclosed and always recommended for disclosure. In 1975, 165 out of 174 issuers included a fairly recent statement of direct debt, and 149 included an update to within 120 days of the current bond offering. (Summary of Reporting Practices) /̄63, p. 271_7 The results of the Indicator Survey support a policy of disclosure of this information. The bond dealers surveyed rated "total debt outstanding" as the most important indicator of all seventy-four included on the survey form. Such information is available to city officials without research or audits.

The more complicated questions in analysis of the debt structure are the following: How should limited obligation or self-supporting debt be treated? How should the debt of other municipal corporations that have an overlapping geographical area and taxing powers be treated? How important is the possibility or probability that bonds that have been authorized will be issued in the next year? in the next two years? How important is the possibility of new bond issues shown in capital improvements plans but not yet authorized? Should the current and past use of the proceeds of outstanding long-term general obligation debt and other debt be detailed to bond holders or new bond buyers?

Long-term debt offerings can be classified into two types by security -- general obligation and limited obligation. Analysis in this thesis is primarily directed at general obligation bonds.

General obligation bonds are secured by the issuer's or by another governmental unit's giving of its full-faith-and-credit-pledge of its taxing power and other general revenue producing power. To be a general obligation bond, a security may be issued with the assumption that repayment will come from special revenues, but if there is a full-faith-and-credit pledge and the special revenues are insufficient, the general governing body will very seldom renege on its responsibility for the debt. In practice, an example was given by one midwestern city where auditors examining special assessment funds discovered that a large number of installments collected for one fund had been diverted to pay bonds issued from another fund, that had failed to make adequate collections. Although bonds of the fund from which the diversion was made were of the special assessment type, they were ultimately paid by the general funds from a tax levy on all local property. [26, p. 119]

Experience has shown that if a municipality does not support its limited obligation debt and avert default, its financial reputation and ability to market general obligation securities will be strongly damaged. If the municipality has a limited right to levy taxes, it cannot issue general obligation debt. Although many tax increases are passed by referendum, taxpayers cannot legally refuse to pay taxes necessary to redeem outstanding general obligation debt unless the municipality is in bankruptcy receivership.

Some very good but detailed approaches to disclosure of limited obligation debt have been suggested. The 1976 MFOA Disclosure Guidelines include a suggestion that:

"If any outstanding revenue, special assessment, or limited obligation bonds have not been fully supported by earnings of the relevant facilities or by other relevant receipts at any time in the last ten years, state for each year in which additional general receipts of the issuer were used or required to be used for payments on such securities, the amount due on such securities and the amount of such additional funds. Describe any contract or arrangement, such as a lease, services contract, or deficiency subsidy aggreement, requiring application of general tax or other receipts of the issuer for the benefit of other governmental entities. /̲‾33, p. 8̲/‾

The description of those contracts or arrangements, however, might be so technical that that it might have to be drafted by a bond counsel, auditor, or other expert -- further removing document preparation from the control of city officers. For many or most investors, though, such wording would be most useful if it was not in legal language.

There are many possible contingencies affecting revenue facilities. If these contingencies are determined to be "material information", then the potential liabilitiy of the city may be greatly increased and the prospectus statements have to be much longer.

The 1965 State Technical Assistance Report gave useful suggestions on presenting limited obligation debt. It recommended that separate forms be developed for these types of bonds: (1) nonproperty-tax-supported bonds (payable from gross receipts and other nonproperty taxes), (2) bonds payable from property taxes that are subject to limits, (3) special assessment bonds, (4) housing authority bonds, and (5) bonds secured by pledges of two or more revenue sources. It also recommended a "bridge" between disclosure of revenue bonds information and general obligation bond information by including:

> "(a) in the general obligation form a trend report of enterprise debt, income, expense, debt service, and surplus or deficit, and (b) in the revenue bond form a summary of general debt and related information that reflects upon the entire credit standing of the community. /1, p. 39/

This recommendation is broader than that of the MFOA which would apply only to enterprises that had a deficit or had required a subsidy. Both have similar problems in that prospectus statments designed along such lines might be very bulky, extend the conceptual boundaries of the information that must be included, and increase liability. For instance, it is possible that a city could be held responsible for misestimating the size of a deficit of a metropolitan transit system.

Ideally, arrangements should be made for exchanges of such information statements between the financial management of a city and any special enterprises under separate financial management. They could be compiled in detailed information reports available to investors on their request and released to financial journals. If this sort of distribution scheme is made possible, the generally distributed prospectus could include only the names of the enterprises and the amounts of outstanding limited obligation debt. More detail could be provided if the city had ever actually contributed from its general funds for the redemption of limited obligation debt or if it had guaranteed the debts.

For general distribution, the following excerpt from the 1963 IBA Format has the advantage of brevity:

	Amount Outstanding	Sinking Funds Balance
A. General obligations (not listed below)	$________	$________
Special assessments secured also by general tax	$________	$________
Utility and public enterprise debt secured also by general tax:		
(a) water	$________	$________
(b) sewer	$________	$________
(c) light and power	$________	$________
(d) other (specify)	$________	$________
Total general obligation bonds	$________	$________
B. Special assessments only	$________	$________
Utility and public enterprise revenue only:		
(a) water	$________	$________
(b) sewer	$________	$________
(c) light and power	$________	$________
(d) other (specify)	$________	$________
Total other than general obligation bonds:	$________	$________

[1, p. 63]

To keep the prospectus statements short and readable, as desired by respondents to the Indicator Survey, this thesis recommends the use of an expanded version of this part of their format additionally including: The amounts and trends of the payments from the general funds for redemption of special assessment bonds and repayment of utility and public enterprise debt, the dates and amounts of subsidies for debt described as "self-supporting" with an explanation of those circumstances, the amounts and names of funds with outstanding limited obligation debt, and the amounts and identification of lease contracts, service contracts, and deficiency subsidy contracts. The contract information recommended by the 1976 MFOA Disclosure Guidelines should not be included in the prospectus because it is not that important and would add unnecessary detail and bulk, but is should be available upon request for those that feel strongly enough.

The trends of long-term debt help to put the issuer's current financial condition in perspective. It is reasonable for an analyst or investor to know whether the city has borrowed heavily for years, whether capital needs have been postponed, and how the debt burden has changed relative to the total budget. Current debt-service requirements would also be more clear if they were related to their original issues. It would be interesting to analysts if a city had changed the composition of its debt structure (by type of security) and they might question its reasons (to avoid legal debt limits?) Reporting on the trends of long-term debt is not unlikely to uncover potential problems or to increase costs of data gathering and verifying. It may not be important enough, however, to be included in a short statement. The trends of interest costs are something that the city might wish to downplay.

The Summary of Reporting Practices found that only seven out of 174 issuers included a "statement of direct debt for prior five-year period" [63, p. 271] as recommended by the 1976 MFOA Disclosure Guidelines. [33, p. 7] The 1965 State Technical Assistance Report recommends a comparison of outstanding debt, characterized by type of security, for ten years ago, five years ago, and the last two years. [1, p. 40] The 1976 Williams-Tower Bill would not require disclosure of long-term debt trends, and there was no space for it on the 1963 IBA Format.

If the extra detail on trends of long-term debt is given, trends over ten years (or some of them) would be more representative than the five suggested by the MFOA because capital construction programs of cities have varied greatly (due to funding of urban renewal programs and other circumstances). Bar or line graphs, such as those used in most annual reports prepared by corporations for stockholders, would be very adequate and would not drown the analyst in detail. The trends of interest rates may be downplayed by including them in debt service trends (or highlighted if the city is now paying more favorable rates).

Annual debt service requirements over the last ten years could be effectively compared with total revenues. Because a large amount of annual debt service expenditures in previous years is from debt issued more than ten years ago, records of annual debt service show a different picture than total debt outstanding. Trend data could be accompanied by a short description of reasons for major increases or decreases of debt (such as central business district renovation or transfer of school building functions to a special district).

Chart IV-5

Disclosure Recommendations on Overlapping Debt Structure Information

Recommending Report	Types of Descritive Information Recommended: Total and Net Overlapping Debt	Itemized by Issuer	Debt Retirement Scheduel	Authorized Debt	Margin to Debt Limit	This Issuer's Share of Overlapping Debt	Explanation of Guarantees, Deficiency Agreements, or Subsidy Contracts
1951 New York City Report	Yes	Yes	Ambiguous	No	No	No	No
1963 IBA Format	Yes	Yes	No	No	Yes	Yes	No
1965 State Technical Assistance Report	Yes	Where practical	No	No	No	No	No
1976 MFOA Disclosure Guidelines	Yes	Yes	No	Yes	No	Yes	Yes
1976 Williams-Tower Bill	If required by the SEC	If required by the SEC	If required by the SEC	If required by the SEC	If required by the SEC	If required by the SEC	Guaranteed Debt

C. Overlapping debt structures

Cities have several types of long-term liabilities from overlapping jurisdictions (such as school districts, utility districts, housing authorities, transit authorities, and counties). These include jurisdictions that have a funding agreement with the city, a legal or political claim on city revenues if they should default, service city people or property, and/or tax city people or property. Where the overlapping units are separate corporate forms and the legal cooperation of the city is not needed for authorization of the issue, their debt cannot be considered to be the debt of the city government. Debt of this types is called "overlapping debt" and is either general or limited obligation debt of the overlapping entity, which may be overlying, underlying, or coterminous.

The idea that overlapping debt should be somehow reported and used in analysis is fairly well established. In 1975, 138 out of 158 prospectus statements included it. (Summary of Reporting Practices) [63, p. 271] However, the bond dealers surveyed rated it aa 23rd in importance out of 74 indicators placing it as having less importance than most indicators of internal finances. (Indicator Survey)

The 1976 MFOA Disclsoure Guidelines and the 1963 IBA Format suggest a table with the name of every overlapping entity, its amount of authorized debt as of a given date, and the percent of its outstanding debt chargeable to persons or property within the issuer's boundries. [34, p.9; 1, p. 64] The 1976 Williams-Tower Bill does not require any disclosure of overlapping debt. The 1965 State Technical Assistance Report suggests including summaries of classified revenues and expenditures of overlapping units. [1, p. 64] An exhibit developed by the Firch Investors Service mentions the "multiplicity of overlapping governmental units", but it is not explicit as how much detail of the finances of those units the agency considers. [60, p. 76]

What could be disclosed about the finances of overlapping units? Possibilities for each unit include; (1) total debt outstanding, (2) a breakdown of total debt outstanding by type of security, (3) sinking fund detail, (4) an aggregated schedule of debt service requirements, (5) detail for each outstanding issue, (6) the amounts of authorized debt, (7) legal debt limits and procedures in issuing debt, (8) a general description of the administration, finances, and characteristics of enterprises or area, (9) a summary of services provided and other expenditures, (10) a summary of revenue sources, (11) the type of taxes and the tax rate imposed upon people and property of the municipality of concern by the overlapping unit, (12) the trends of each of these, and (13) tax collection procedures.

Obviously, if a city tried to report all of this detail on each overlapping unit (there may be many), the city's statement would be unwieldly and more important information would be obscured. What is the most important information about the finances of an overlapping unit to an investor in securities of the general governing body? Logically, the most important questions about an overlapping units seem to be: (1) Is the unit in immediate financial danger? (2) If the unit defaults in what ways might the city be held responsible? (3) Are the people of the city dependent on the overlapping government for vital services? and (4) What kind of taxes (and in what amounts) are imposed by the overlapping unit on people or property within the city?

Moak suggests that comprehensive financial reports be prepared showing the aggregated effect of the finances of all municipal units in each locality. Such a policy would be a significant advance that would open new possibilities for reseach in municipal finance. He does not, however, suggest that such a policy be instituted with the purpose of informing the municipal securities market. [28, pp. 430-432]

Reporting of the finances of overlapping units might require more political cooperation than is sometimes existing. If the officers of the overlapping unit can anticipate a danger of default of that unit, their strategic maneuvering might be hampered by an obligation to frequently and officially inform other local governments. A lesser responsibility, however, may suffice and lead to greater communication than currently exists. The more detail on overlapping units required, the more opportunity will exist for policy conflicts and liability disputes between overlapping units. This thesis therefore recommends that limited and defined categories of information on overlapping units be reported in prosepctus statements and annual reports.

Chart IV-6

Disclosure Recommendations on Information on
Authorized Debt and the Possibilities of Increasing Outstanding Debt

Recommending Report	Amount of Authorized but Unissued Debt	Amounts by Category of Security	Purpose of Authorized but Unissued Debt	Assumed Interest Rates on Authorized but Unissued Debt	Description of Capital Improvements Plan
	Types of Descriptive Information Recommended				
1951 New York City Report	No	No	No	No	No
1963 IBA Format	Yes	No	Yes	No	No
1965 State Technical Assistance Report	Yes	No	No	No	For six Years
1976 MFOA Disclosure Guidelines	Yes	Yes	Yes	Include in Debt Service Schedule	No
1976 Williams-Tower Bill	Yes	If required by the SEC	If required by the SEC	If required by the SEC	If required by the SEC

D. Authorized debt and the possibilities of increasing outstanding debt

It is reasonable to consider new debt when evaluating the burden of outstanding debt. For any city, an exploration of the finances and other circumstances may lead to various perceptions of risk. Examples of such are:

(1) A city has recently completed a major capital imporvements program for which debt service requirements are high. However, because no more long-term borrowing is planned or needed for several years, outstanding bonds and new issues of TAN's and RAN's are an acceptable risk.

(2) The debt service requirements of a city are high and it is planning more capital outlays, however, the risk of its securities is an acceptable one, because its revenue base is adequate and growing.

(3) Although debt service requirements are currently reasonable, the expense of capital facilities needed and planned (to be paid by new debt issues) is so large that the security of its current long-term issues will be undermined by the extra debt service needed for as yet unissued debt before current issues mature.

It is difficult to define how much and what kind of information on the possibilities of increasing outstanding debt are needed to allow investors to form this sort of general risk perception without reducing the flexibility of the city in its future financing. How far in the future should the analyst think and what certainty is needed? The 1965 State Technical Report recommended that the prospectus "summarize all capital improvements and bond issues that are likely during the next six years". /̄1, p. 41_7 Although it is generally recommended that cities plan comprehensive capital improvement programs, there is a large element of uncertainty in these plans as financial priorities, administrations, and building costs change. Someone, such as a financial consultant, who has personal communication with investors may be able to give them the most favorable or the most probable of possible interpretations.

The 1976 MFOA Disclosure Guidelines suggest disclosure of debt including the "Amount Authorized", which it defines as follows:

> "Debt should be regarded as 'authorized' when all material legal steps have been taken by the issuer for its authorization for issuance, such as required approval of the city council or the voters. Actions tending to be of a ministerial or judicial nature, such as validation in some jurisdictions, should not be regarded as discretionary for this purpose. [33, p.7]

The 1963 IBA Format provides a half-inch blank each for the purpose and the amount of authorized debt. [1, p. 64] The rating agencies, however, claim to review much more than currently authorized debt. Standard & Poor's Corporation claims that it considers the future borrowing plans of the unit and all overlapping units and that it reviews plans for capital improvement programs for the next five years. [60, p. 37]

It is obviously reasonable to disclose authorization on the basis of which the city is really planning to issue more bonds within the year. In reality, however, things are more complicated. Some cities have very large amounts of authorized but unissued debt on their books with which they have little intention of proceeding. Others may have ongoing and immediate plans to issue debt that has not yet been authorized. Of course, what is really important in analysis is the probability of increasing outstanding debt, not the dormat authorizations of bonds so long delayed that the use for which they were intended has been forgotten.

The Indicator Survey results provide evidence that bond dealers are interested in the possibility of increasing outstanding debt. Their importance ratings showed they think that "projected capital expenditures for public facilities" is more important information than "number of assets and liabilities over five years", "number of overlapping jurisdictions with debt issuing capacity, "changes in welfare expenditures in last five years", and "employment by the city and other governmental units over the last five years".

How may the distinction between legal authorization and the likelihood of issuing be made? A city could describe part of its authorized debt as being out-of-consideration and part of its authorized debt as being really anticipated. If it does, what happens if it is politically strategic to use an old authorization? If it begins to call certain debt anticipated, will it be considered to be willfully misrepresenting the facts if it issues debt within the next six months, year, or two years, that it did not describe on the last official financial statement as anticipated? Also, is not a capital improvement program something a city develops as an internal planning mechanism -- why should it be exposed to the investment community? Could the city be held responsible for carrying out the plans announced in official statements even if the wishes of the administration and the population change?

This is an area in which there is potential for real conflict of interest between the investors who wish to be informed and the city which wants to manage itself. Extensive disclosure requirements and court findings holding the city strictly liable for the accuracy of this information could force the city to change its financial management policies. Although the Moreland Commission (convened to evaluate the financial crisis and temporary default of the New York State Urban Development Corporation) argued that disclosure will, in general, instigate investor feed-back leading to more sound management policies, that feedback could also lead to increased difficulty in city management. For this reason, this thesis recommends that investors find out about projected capital expenditures through informal channels.

Chart IV-7

Disclosure Recommendations for Information on the Uses of Outstanding Debt

Recommending Report	Explanation of Uses of Proceeds of New Issue	Categories of Uses of Outstanding Issues	Uses of Each Outstanding Issue	Past Uses of Bond Proceeds for Operating Expenses	Past Refundings and Rollovers	Detailed Description of Past Defaults
	Types of Descriptive Information					
1951 New York City Report	Yes	No	No	No	No	Only if still unpaid
1963 IBA Format	No	No	No	No	Amount, purpose, and maturities if within last two years	Explain if since 1930
1965 State Technical Assistance Report	Implied	Where practical, for latest year	Where practical, for latest year	Where practical, for latest year	No	Implied
1976 MFOA Disclosure Guidelines	Yes	No	No	Circumstances and amounts if within last ten years	Circumstances and amounts if to prevent default within last 25 years	If within last 25 years
1976 Williams-Tower Bill	Yes	If required by the SEC	If required by the SEC	If required by the SEC	If required by the SEC	If within last 20 years

E. <u>The uses of outstanding debt</u>

Long-term debt is generally used instead of cash savings to pay for capital facilities because:

(1) The use of long-term bonded debt helps to smooth fluctuations in expenditures over time so that the same tax rate can be maintained.

(2) The use of long-term debt allows current needs for capital facilities to be met in growing communities.

(3) The use of long-term debt allows capital facilities to be built much sooner after their need is perceived.

(4) The use of long-term debt allows the administration that plans the project to get fairly immediate political credit.

(5) The use of long-term debt allows more equitable payment by users of facilities serving transient communities over a period of time.

(6) The interest rates that municipalities generally pay on outstanding debt is less than the inflationary increase in construction costs so it is less expensive to borrow-build-repay than to save-repay-build.

The 1965 State Technical Assistance Report recommends that the prospectus itemizations of outstanding debt issues include their uses. It notes that the debt detail of a large metropolitan center should be reserved for the annual report. [1, p. 40] Although none of the other disclosure guidelines cited recommend reporting of the use of proceeds of all outstanding issues, several prospectus statements examined did include this information. St. Paul, Minnesota, for example, gave a list of all the project names and amounts of issues of thirty-five outstanding bond issues (such as health center, street lighting, flood control, and library improvememts). [9, p. 26] Boston, which has more outstanding debt, classified it into nine general categories of use (such as general purposes, public buildings, and public works). [8, p. 13] Depending on the judgment of the investor, a list of purposes may show that a city's management has been wise or foolish to borrow for these reasons. A list, such as either one described, takes one page or less in a prospectus statements, is easy to compile from city records, and should not increase the city's potential liability.

What is more important to the security analyst, however, is uses of bond proceeds that may indicate potential financial trouble. Because they are looking for problems, analysts are interested in any irregular uses of debt proceeds at any time in the past and currently. This section discusses irregular uses which are of interest because they may (or may not) indicate bad financial management or financial difficulties: (1) debt-financing of capital equipment, (2) debt-financing of operating expenses, (3) deficit-funding, and (4) refunding and rollovers.

(1) Debt-financing of capital equipment: Capital equipment (such as buses, fire engines, and heating systems) is often financed by long-term bond proceeds; this is often wise and can be justified because they have high initial costs, are used for a long time, and are often a part of the plans of buildings. However, large communities generally pay for capital equipment out of operating funds so that they do not need voter authorization, avoid complicating the capial programming process, and do not increase the outstanding debt counted against the legal debt limit. A policy change from excluding capital equipment to including it in uses of the proceeds of long-term bonds may indicate a shortage of current revenues. A short explanation of how this has been handled should help analysts to understand the long-term debt structure, however, the city should not commit itself to maintaining either policy because its financial flexibility would be reduced.

(2) Debt-financing of operating expenses: Use of long-term bond proceeds for operating expenses is only justifiable by a real emergency

such as a natural catastrophe. The 1976 MFOA Disclosure Guidelines specifically recommend reporting of the use of long-term bond proceeds for operating expenses [33, p. 8] An honest description of past reveneus and expenditures would show such use. A poor example was set by New York City, which included in one capital budget items such as textbooks, manpower training, and even some salaries. [15, p. 94]

(3) Deficit funding: When operating deficits have accumulated to an unmanageable level, bonds may be issued to cover them. This is called "deficit funding". It is more honest to issue bonds specifically for such purposes than to pad the size of bond issues designated for capital improvements with needs for operating funds. However, deficit funding is not generally justifiable and except in times of "deep and protracted business depression", it usually indicates financial mismanagement. [28, p. 260]

The financial policies responsible for deficits may not be in the control of the issuer. City financial statements discussing deficit funding should make this clear, and investors and bond analysts should try to understand the whole situation. Albany, for instance, was limited by New York State from increasing its maximum property tax rate. Although its long-term debt records show that for a number of years it issued very few bonds, it built up a deficit of $22 million. When the City became legally eligible for a different state classification by passing a population size criteria, it used its new enabling powers to double its tax rate and divest its school district. [7, p. 10] The financial mismanagement was in the slowness of the City and State political processes in finding a solution, not in the issuing of the deficit funding. Investors who are prejudiced against new securities of the City of Albany because the City has had a deficit and funded it with long-term securities are doing the City an injustice.

(4) Refunding and rollovers: Refunding is a procedure by which callable bonds are redeemed with with cash or with newly-issued bonds. It is legitimate and may indicate sophisticated debt management. Its normal uses are to achieve interest savings, eliminate restrictive bond covenants, and reorganize maturity patterns, or to consolidate debt. [27, p. 279] Frequently, the law prohibits the issuance of refunding bonds in greater amounts than the value of the principal of the refunded issue although maturity may be delayed. Refunding may be more of a political question than a financial one. The city must justify extension of the payment period and the new burden of fees and taxes on users and citizens for facilities built years earlier.

One kind of refunding does have cause for concern. That is a "rollover", which the 1976 MFOA Disclosure Guidelines define as:

> "refunding securities (which) have been issued by the issuer within the last 25 years for the purpose of preventing a default in principal or interest payments on securities then outstanding. [33, p. 7]

The MFOA suggests disclosure of the circumstances and amounts involved. However, it may be that a city that had refunded securities in the manner described by the MFOA may not have otherwise defaulted. It may not have had sufficient general funds or sinking funds available to redeem the bond, and refunding may have been a more convenient or politically expedient alternative than raising taxes or cutting services. Whether the city would have in fact defaulted (if it had not refunded the bonds) seems difficult to prove.

Chart IV-8

Disclosure Recommendations for Information on Debt Retirement Schedules

	Types of Descriptive Information Recommended				
Recommending Report	Total Annual Debt Service	Annual Requirements by Type of Security	Annual Requirements for Principal and Interest	Schedule Including New Issue	Schedule Including Authorized Debt
1951 New York City Report	For ten years	No	No	Yes	No
1963 IBA Format	Implied	For five years	No	Ambiguous	No
1965 State Technical Assistance Report	For ten years	No	No	Ambiguous	No
1976 MFOA Disclosure Guidelines	Until maturity	Yes	Yes	Ambiguous	Where Appropriate
1976 Williams-Tower Bill	Yes	If required by the SEC	If required by the SEC	If required by the SEC	If required by the SEC

F. Debt retirement schedules

The debt retirement schedule is a very important piece of information in security analysis. It is simply a presentation of the amount that is due every year for redemption and interest payments on outstamding serial bonds and maturing term bonds. The disclosure recommendations cited show a consensus on the importance of reporting debt retirement schedules, yet in 1975 the Summary of Reporting Practices found that only 66 out of 174 issuers surveyed included a statement of annual debt service requirements and only 36 included the interest payments. [63, p. 271] This clearly shows mow unresponsive municipal issuers have been to investor's information desires. In fact, respondents to the Indicator Survey thought that debt retirement schedules were the ninth most important indicator out of 74 indicators.

The schedule of debt retirement is necessary to make a comparison with projected revenues and other projected expenditures in a detailed analysis to see if there might be shortages of funds needed to avoid default. Most cities have so many outstanding issues and their maturities are arranged in such a way that a slightly smaller amount of existing debt should be due each succeeding year.

If there are years in which an especially large amount of debt matures, savings for that year's bond repayment should be distributed over other years. If there are years in which relatively little debt matures, those extra funds should be used to defray the debt repayment requirements of other years. Funds normally dedicated to debt service should not be used for unnecessary expenditures in the occasional year in which debt service is especially light, because that might contribute to extravagent, unplanned expenditures. If bond redemption requirements were the same every year there would be no need to save for them because annual appropriations could be marked for maturing debt.

In addition to looking for fluctuations in debt service requirements and the city's handling of them, an analyst is interested in how fast the outstanding debt will be repaid. The more quickly it is repaid the fewer encumbrances there will be on future revenues, so that more debt may be safely issued to pay for other capital needs. One way to evaluate this is to future the "average life of tax-supported debt outstanding", which may be expressed in years or as the percentage that annual retirement and/or amortization represents of the total debt outstanding (e.g. 7.14% or 14 years). Moak advised that use of this ratio increase with a safe range being 10½ to 15 years. [28, p. 376]

The rating agencies have said that they consider the shape of the debt service curve to be very important. They calculate the "debt payout ratio" by summing the scheduled bond redemptions for a certain number of years and dividing by net outstanding direct debt. The rating agencies consider a 25% redemption in five years and a 50% redemption in ten years to be a good rate. [47, p. 140]

Other analysts use another calculation to evaluate whether the burden of debt is being extended over too many years. They add five percent of all general bonded debt outstanding to current annual interest requirements. This gives the burden of annual debt service that would be due if all of the bonds were retired evenly over the next twenty years. [28, p. 375]

These several simple techniques are related to a fairly important aspect of the debt structure and could be computed by an unsophisticated investor using the debt service schedule. This is a good example of how disclosure policies might promote wider analyses by more people.

Because debt service requirements fluctuate, many cities pay into a "sinking fund" to save for bond redemption -- which is then invested in approved investments (such as U.S. government securities). Sometimes a city may, for various reasons, pay into a sinking fund all of the money needed for redemption of a particular issue years before the bonds mature. Bond owners prefer the security of having appropriations made into a sinking fund or a reserve fund somewhat ahead of the schedule at which repayment of bond principal and interest has been contracted. Bonds so secured may sell for lower interest rates than bonds of the same issuer without them, on the theory that if the issuer has a temporary cash shortage, immediate debt service requirements will still be safe. If bond owners are very concerned about the security of the bonds, they can check to see that appropriations are made to the sinking or reserve funds as scheduled. There may be prescribed legal procedures if they are not.

Should principal and interest due be lumped together when reported or shown separately? Both the 1963 IBA Format and the 1976 MFOA Disclosure Guidelines aggregate them. In fact, the MFOA suggests that assumptions about future interest costs be made so that the principal and interest costs for the new issue and for authorized but unissued debt "where appropriate" can be included with outstanding debt in the annual debt service schedules. /_33, p. 7_/ There is a danger in these assumptions because of the difficulties in estimating future interest costs and deciding when authorized debt is "appropriate". An alternative, more appropriate treatment of this subject might be to require analysis of the assumptions about the interest costs of new and future debt issues.

The 1965 State Technical Assistance Report suggested that a debt service schedules for only the next ten years would be sufficient for analysis. because after that the situation is likely to change. /‾1, p. 41_7 The 1963 IBA Format suggests reporting this for only five years, /‾1, p. 65_7 while the 1976 MFOA Disclosure Guidelines suggest until maturity. /‾33, p.7_7 This format decision is relatively unimportant. An annual showing of debt-service requirements for the next ten years followed by a lumping of debt service already contracted for years 10-15, 15-20, etc., should be sufficient and space-saving.

The 1963 IBA Format includes the yearly amounts due to sinking fund installments, but it lumps them with the requirements for principal and interest that are paid directly from general funds. /‾1, p. 65_7 Both it and the 1976 MFOA Disclosure Guidelines suggest that the current balances of sinking funds be given (also for overlapping units). If a city follows these suggestions, the unfunded amount of outstanding debt and future encumbrances on revenues would be clear, but the bond owners would still not be able to tell if proper payments were being made into trust to redeem their bonds. However, because some cities may have more than a hundred outstanding issues, reporting the status of each payment separately is impractical. Other possibilities exist to moniter payments such as appointing trust officers for each issue who could notify security owners if problems arose. The prospectus statements could then be reserved for information of more general concern.

The 1976 Williams-Tower Bill does not specify the format of the debt information it would require -- it throws out terms including the "character of amortization provisions of funded debt", "sinking fund requirements", and "debt service requirements". /‾63, p. 7_7 However, some of these format decisions in reporting debt retirement schdudules have policy implications.

Although an aggregated format would be sufficient to check the debt-payout ratio and pattern of debt service requirements, most disclosure guidelines suggest that the debt retirement schedule be disaggregated. The 1963 IBA Format suggests that it be broken down by authorized source of repayment, such as general taxation, special assessments and general taxation, utility revenues and general taxation, special assessments only, and utility revenues only. /‾1, p. 64_7 The 1976 MFOA Disclosure Guidelines suggest that it be broken down into general obligation, special assessment, utility revenue, and other indebtedness. /‾33, p. 7_7 It is unclear how much understanding may be gained by the analyst from disaggregated displays of debt service requirements. However, it will be more difficult to compare two issuers if one uses the IBA suggestions and the other the MFOA suggestions.

Chart IV-9

<u>Disclosure Recommendations for Information on Legal Debt Limits and Debt-Weighting Ratios</u>

Types of Descriptive Information Required

Recommending Report	Explanation of Legal Debt Limit	Margin to Legal Debt Limit	Overlapping Units' Margins to Legal Debt Limit	Debt per Capita	Debt to per Capita Income	Debt to Assessed Value of Property
1951 New York City Report	No	No	No	No	No	No
1963 IBA Format	No	Yes	Yes	No	No	No
1965 State Technical Assistance Report	Yes	Yes	No	No	No	No
1976 MFOA Disclosure Guidelines	Yes	Yes	No	Yes	Yes	Yes
1976 Williams-Tower Bill	Yes	Yes	If required by the SEC	If required by the SEC	If required by the SEC	If required by the SEC

G. Legal debt limits and debt-weighting ratios

What is a "safe" amount of debt for a city to have outstanding? Taxpayers have long been interested because of their concern about tax levels and the future capacity of their city to build schools, roads, and other capital facilities as they are needed. Bond owners are concerned about the ability of future revenues to repay outstanding debt. Although the level of debt that would threaten the issuer's ability to embark upon new capital projects, or to maintain a low tax level is much lower than that which would threaten its ability to repay already issued debt, both are estimated in similar manners.

Debt-weighting ratios are commonly used although they are not prescribed by formal theories of practice of municipal finance. They include: debt levels relative to property values, debt levels relative to the total budget, debt per capita, and debt per capita relative to per capita income. The rating agencies have been in a position to compile this information for many issues and use some ratios in assigning ratings. Analysts may use these formulas to compare the issuers of bonds they are considering buying and save enough time by doing so to examine a few issuers in more detail. If enough buying decisions are made on the basis of debt ratios, the interest rates the issuer is forced to pay will be affected. Thus a city that has a financial structure different from the norm may seem more or less attractive to investors because of the use of very simple formulas for evaluating the debt burden.

The traditional legalistic approach to debt limitation is characterized by two common constitutional and statutory restrictions: (a) a limit on indebtedness expressed as a percentage of the local governmental tax base and (b) a requirement of a local referendum to authorize the issuance of bonds often calling for some sort of special voter majority. The debt to property ratio in debt limiting legislation was originally developed as a way to allow more flexibility than a flat ceiling. This approach has been criticized by the Federal Advisory Commission on Intergovernmental Relations as follows:

> "(1) It pertains to present or past conditions, rather than those of the future when long-term debt will be subject to servicing, and thus takes no account of divergent trends for various governments and communities.
>
> (2) It deals with separate layers of local governments rather than the aggregate of local government for a particular area.
>
> (3) It purports to measure economic capacity by reference to only one revenue source, the property tax, which provides less than half the revenue of most local governments in most states.
>
> (4) This type of limit is, in most states, imprecise and potentially discriminatory because of the nature of the property tax base to which it refers. The real level of limitation is determined by local assessment practices rather than being closely governed by the legal provisions.
>
> (5) Being commonly applicable only to full-faith-and-credit debt, this type of limitation offers not assurance that aggregated local debt will be kept within prudent bounds.
>
> (6) Debt restrictions have probably restrained the total volume of local government borrowing to some extent, but the extent to which this is true cannot be definitely measured.
>
> (7) The restrictions have probably restrained the total volume of local government borrowing to some extent, but the extent to which this is true cannot be definitely measured.
>
> (8) Debt restrictions have tended to impair the public accountability and responsiveness of local governments in various ways, including the promotion of special districts and various kinds of financing authorities, and the complication and obfuscation of financial arrangements.
>
> (9) The restrictions have affected governmental relations in various ways. They may artificially increase the needs and demand for federal and state grants to local governments. In some states, they have contributed to urban-rural and local-state frictions." [1, p. 20]

Most limitations of tax-supported direct debt are still expressed in terms of a debt-to-property value ratio. The property value used may be the assessed value of taxable local property, the market value, or the state equalized valuation. There is no uniformity of the allowed percentile of debt-to-assessed-property values used -- Washington uses a 1.5% basis and Virginia uses an 18% basis, but 5% is the most common. /39, p. 727/

Some attempts have been made to legally limit outstanding debt while responding to the criticism of debt to property ratios as a basis for a limit. The Pennsylvania 1972 Local Government Unit Debt Act, for instance, uses as a basis the arithmetic average of the last three years' total revenues adjusted to exclude certain precommitted revenues. That legislation allows most governmental units, including all cities except Philadelphia, a maximum of 250% of the average adjusted total revenue as outstanding unfunded debt without electoral approval. Limitations on legal taxation rates and assignment of specific tax revenues to debt service can also operate as a legal debt limit. /45/

The outcome of the controversy on disclosure has the potential to affect the use of legal debt limits and of informal debt-weighting ratios. Although the authors of the 1965 State Technical Assistance Report gave nine strong arguments against the use of legal debt limits, they still recommend including in a prospectus statement "for general obligations, a summary of debt incurring power (which) could be confined to a comparison of the amount permissible under the debt limit with the gross debt, allowable deductions, and net limited debt." /1, p. 40/ It is a state and local decision if formal debt limits should be used. If a prospectus format is federally mandated or standardized through customary use, it may be more difficult for a municipality to abolish or change its legal debt limit. If debt-weighting ratios are displayed in financial information, their use may also be institutionalized.

It can be difficult to interpret information about the legal debt limits. Some financial statements present "debt within the legal debt limit" and "debt outside of the legal debt limit" without further explanation of the source of the limit or which debt applys. These assume that the reader is knowledgeable in municipal finance even though disclosure is supposedly needed for the unsophisticated investor. For them, legal debt limits should be explained without using difficult legal terminology.

The 1976 Williams-Tower Bill is vague in defining what sort of information it would require as an explanation of the "legal limitations on indebtedness". [63, p. 6] The 1976 MFOA Disclosure Guidelines are more complete and suggest reporting the legal debt limit of the issuer, the debt chargeable to that limit, the unused margin, and the legal requirements in debt issuance. [33, p. 7] The municipality runs a risk that investors will question its motives and say that they should have been previously warned if it changes the formula or level of its legal debt limit. It is necessary to resolve these questions because such information is important to investors. Respondents to the Indicator Survey rated "funded debt outside of legal debt limit" as the third most important indicator out of the 74 indicators included on the survey form, and 56% felt that it would have "significantly more meaning if compared to other cities".

This thesis recommends that the scope of audits be expanded to include an evaluation of the legal debt margin. The auditor and bond counsel could provide the city with a statement for the prospectus concerning how bonds issued within the next few years might be affected by the legal debt margin.

There are significant interpretational questions about debt-weighting ratios that municipal financial experience has not yet been able to resolve. Reliance on only the ratios seems overly limited, but they may be a very good point to begin to understand a city's debt structure. Standardized definitions of ratios would make comparisons easier. It should be clear whether short-term debt, funded debt, and overlapping debt are included and to what date. Their use may encourage limited analysis by some investors who might otherwise rely on the ratings. Reporting of debt-weighting ratios implies assumptions about those towards whom the report is directed. The collections and display costs are minimal but they may make the city look worse financially.

Debt per capita is a very popular debt ratio. U.S. Census data on total debt and various revenues and expenditures are published in per capita figures, making comparisons easy. Most prospectus reports include figures on direct debt outstanding and on population and some also calculate and display the ratio in a statistical section. Of the total respondents to the Indicator Survey, 80% wanted comparisons of debt per capita with other cities, and it was ranked second only to "total debt outstanding" in importance. However, the 1976 MFOA Disclosure Guidelines were the only one of the disclosure recommendations cited to specifically recommend reporting debt per capita. [33, p. 9]

Gross comparisons of debt per capita can be illustrative. For instance, in fiscal year 1974 the average full-faith-and-credit debt was $351 per capita in fourteen large cities that have been losing population, $221 per capita in thirteen large cities that have been gaining population, and $1,031 in New York City. [32, p. 61] Yet in more specific comparisons, debt per capita figures may be very distortive because they may not reflect the total debt burden or the real ability-to-pay of citizens or of the issuer.

In New York City, the figure used for "per capita" would not include the many commuters who contribute to city revenues through income tax, sales tax, and other fees, yet the debt figure would include debt undertaken for transportation facilities and other facilities in the central business district undertaken to serve and attract commuters. If the tax base also supports debt of overlapping units, that debt should be included in calculations of debt per capita.

Somewhat more sophisticated than debt per capita is a ratio computed by dividing debt per capita by income per capita. Standard & Poor's Corporation has assembled an unpublished index of this ratio for its private use. /̅49, p. 140_7 The 1976 MFOA Disclosure Guidelines suggest reporting "debt per capita as a percentage of estimated per capita income of individual resident taxpayers". /̅3 , p. 9_7 The use of this ratio as an indicator of ability-to-pay can be further improved by incorporating data on the cost of living. Even so, it is misleading if revenue sources other than taxes paid by residents are not considered.

Debt to property ratios are the most commonly used weighting methods, because they are the basis for most legal limitations on debt and reflect the historical importance of property tax revenues. The rating agencies consider a ratio of 10% to be high and one of 3-5% to be low. /̅47, p. 139_7 Most legal debt limits, as mentioned before, are based on a ratio of allowed debt of 5% of total assessed property values. /̅39, p. 727_7 (Other debt is issued outside of the legal debt limit.)

Evaluation of the debt burden by using debt to property ratios has some of the same problems of interpretation other debt-weighting ratios have. It may not reflect either the tax burden of debt service required for overlapping debt or the value of nonproperty tax revenues. And, as mentioned in discussions of the property tax, determination of property values involves many judgments.

The 1976 Williams-Tower Bill would not require computation and display of debt to property ratios, although it does, of course, require debt levels and property values. The 1976 MFOA Disclosure Guidelines recommend computation and display of debt to assessed value and of debt to estimated true value of property. [33, p. 9] The respondents to the Indicator Survey were asked to rate "combined debt as a percentage of market value" and found it to be fairly important or 17th out of the 74 indicators. Because it is not an expensive piece of information, this thesis recommends that it be included in propsectus reporting.

Another ratio sometimes used (although not required or recommended by and of the disclosure guidelines cited) is debt service to total revenues or debt service to total budget. This has the potential to be misleading because a rich community may need few municipal services and have a small government budget. In an interview with Fortune Magazine, the rating agencies siad that they use this ratio, considering 10% to be a comfortable level and the high teens to be a dangerous level. [49, p. 139] Lennox Moak, suggested using this same ratio, but he claims that the standard is 25%. He advises that debt service to toal revenues is a more useful ratio than debt service to total budget because the budget is inflated by bond proceeds. [28, p. 375]

The 1965 State Technical Assistance Report and other sources cautioned against over-reliance on any one weighting ratio. It suggested that an analyst use a variety of debt ratios and consider some other factors. The ratios it suggested were: "debt service as a percentage of revenue", "net general obligation debt as a percentage of total and overlapping tax levies", and "general debt service as a percentage of total and overlapping tax levies". [1, p. 49]

The results of the Indicator Survey show that investors are interested in both debt per capita ratios and debt to property value ratios. Further research will probably show that they are also interested in other debt-weighting ratios or would be if they became familiar with their use. This thesis recommends that debt ratios be displayed in a grid format with direct debt, overlapping debt, and debt-service indicators across one dimension and total revenues, total tax levies, total property values, total population, and population adjusted for income across the other dimension. This format would be inexpensive, consise, and facilitate independent analysis.

The debt of some cities has been compared in Table IV-2 (see page 161) using two different debt per capita ratios and one debt to total revenues ratio. This table illustrates some of the advantages in using a number of debt ratios to compare cities or other similar municipal governments. The first column is a ratio of long-term general debt of the city government to the general revenues of the city government. A comparison of these percentages shows that certain cities seem to have relatively more debt although they may have great potential for increasing their revenues. The second column is a ratio of the long-term general debt of the city to its population. Part of the variations in these figures arises because some cities have much more utility debt and some have separate school districts. If the school district is operated by the city government, its debt is included in the figures; if it is operated separately, its debt is not included. Utility revenues and independent school district revenues were not included in the ratios in the first column.

The third set of ratios included in Table IV-2 is the ratios of total long-term debt (general and utility) for the entire metropolitan area (SMSA) divided by the population of the entire metropolitan area. When these figures are compared, the relative debt burden of the cities look much different than it does using the other ratios. However, an individual government within the metropolitan area may have much larger and more stable revenue to support its direct outstanding debt than other local governments do and its securities may therefore be considered to be of higher quality. This type of insights would not be possible without comparison of similar municipalities using a number of different indicators and debt-weighting ratios.

Table IV-2

Comparisons Using Debt-Weighting Ratios

of the Debt Burdens of Some Cities

City/SMSA	Ratio of Long-term City Debt to General Revenues (%)	Long-term City Debt Per Capita ($)	Total Long-term Metropolitan Debt Per Capita ($)
New York City	67	919	1281
Chicago	94	296	574
Los Angeles	71	218	627
Philadelphia	119	542	775
Detroit	74	348	779
Houston	193	358	659
Baltimore	50	413	543
Dallas	232	597	1157
Cleveland	71	259	476
Indianapolis	123	385	471
Milwaukee	79	256	493
San Francisco	18	158	779
San Diego	82	171	475
San Antonio	91	126	577
Boston	64	566	567
Memphis	153	505	830
St. Louis	60	252	775
New Orleans	132	442	709
Phoenix	.7	18	941

Sources: Long-term city debt figures, city general revenue figures, and total long-term metropolitan debt figures were compiled from U.S. Bureau of the Census. Local Government Finances in Selected Metropolitan Areas and Large Counties: 1973-74. (Series GF-74, No. 6), Washington, D.C.: U.S. Government Printing Office, 1976, Tables 2 and 3.
Population figures used in computing debt per capita are U.S. Census data as quoted in City of Boston, Massachusetts. "Preliminary Official Statement Dated September 17, 1976", p.32.

H. Summary and Conclusions

Information describing the debt structure is more important to municipal securities investors than other financial information and nonfinancial information. Note holders are most concerned about cash flow. Bond holders are most concerned about the schedule of bond repayment, possible increases in outstanding debt levels, and the burden of debt service including that of overlapping debt. To understand the current financial picture, an analyst should have trend data on the levels of outstanding debt, the levels of debt service, and reliance on short-term and limited obligation debt. Certain uses of bond proceeds that may indicate financial problems are also of interest. Debt-weighting ratios can facilitate analysis particularly if several types of ratios are used. The legal debt limit can be confusing to unsophisticated investors.

Cities should be very cooperative in releasing debt information, although too much detail may hinder analysis. Certain debt-reporting policies may influence investor judgment. Investors may disapprove of certain uses of debt proceeds. Overlapping jurisdictions and revenue facilities with debt issuing capacity should cooperate by exchanging statements for reporting use. Cities should try to maintain internal control of legal debt limits and bond authorization procedures.

V. Disclosure of Expenditure Information

The primary purpose of local government entities is to provide services to people and property in the area. Most of the attention directed at local government by citizens concerns local taxes and service delivery, while that of the municipal securities market concerns bonded indebtedness and the sufficiency of total revenues. Debt service is only a small part of total expenditures and long-term debt is only used for capital improvements which according to Census data account for an average of only 15% of direct general expenditures. [58, p. 7] Of the remaining 85% used for operating expenses, about 70% is used for wages, salaries, and benefits of the staff needed to provide local services. [32, p. 53] Operating expenses also include school supplies, food, and other supplies needed for service delivery, maintenance of public facilities, and general costs of administration.

This chapter concerns disclosure of operating expenses. It is divided into four sections: (A) Disclosure of service expenditures with welfare as an example, (B) Disclosure of municipal employment information, (C) Disclosure of employee pension cost information, and (D) Summary and recommendations. This chapter is organized in a similar manner to Chapters III and IV. The charts immediately following present information on reporting practices in 1975 and relevant data from the Indicator Survey. Charts coordinated with the sections compare recommendations given by the 1951 New York City Report, the 1963 IBA Format, the 1965 State Technical Assistance Report, the MFOA Disclosure Guidelines, and the 1976 Williams-Tower Bill.

Chart V-1

Frequency of Reporting Expenditure Information in 1975

Section of Chapter V in which discussed	Indicator	Reporting	Not Reporting
A	Operating Statements of Revenues and Expenditures for the most Recently Completed Year:	44	130
-	Detailed Statement or Explanation of Sources of Revenues and Expenditures:	25	149

Source: (Excerpted from exhibit submitted by Professor Ronald Forbes, New York University) U.S. Congress, Senate. Committee on Banking, Housing, and Urban Affairs. Hearings before the Subcommittee on Securities on S. 2969 to Amend the Securities Exchange Act of 1934 to Require the Preparation of Annual Reports and Distribution Statements by Issuers of Municipal Securities, and for Other Purposes, S. 2574 to Amend The Securities Act of 1933 to Provide for Registration of Securities Issued by State and Local Governments, February 24, 25, and 26, 1976. 94th Congress, Second Session, Washington, D.C.: U.S. Government Printing Office, 1976, p. 271.

Chart V-2

Results of Questions on the Indicator Survey Concerning Expenditure Information

Section of Chapter V in which Discussed	Indicator as listed on survey form	Relative Importance Ranking (out of 74)	Mean Importance Rating (on 1-5 scale)	Proportion Desiring Comparisons (%)
A	Total welfare	25	2.0	42
A	Changes in welfare expenditures in the last five years	26	2.0	55
B	Employment by the city and other governmental units over the last five years	30	2.1	58
C	Pension liabilities and funding provisions	21	1.7	62
D	Excesses in operating expenditures over originally approved budgets	10	1.4	39
-	Statement of assets and liabilities over five years	24	1.9	36

Chart V-3

Disclosure Recommendations For Information on Services

Recommended Report	Amounts of Expenditures by Class, Category, of Fund	Trends or Comparison with Previous Responsibility	Description of Principal Services Provided	Physical Volume of Services	Services Provided by Overlapping Governments
	Types of Descriptive Information Recommended				
1951 New York City Report	Yes	No	No	No	No
1963 IBA Format	Yes	Yes	No	No	No
1965 State Technical Assistance Report	Yes	Yes	Implied	Yes	No
1976 MFOA Disclosure Guidelines	Ambiguous	Yes	Yes	School Enrollment	Yes
1976 Williams-Tower Bill	If Required by the SEC	Yes	Yes	No	Yes

(A) Disclosure of service expenditures with welfare as an example

U.S. Census data show that in 1973-74 total expenditures by local governments for personal services in the average SMSA accounted for about 55% of direct general expenditures. From 1971-72, it increased by 23.4%; and, between 1969 and 1972, it increased by 59%. /‾32, p. 81_7 In 1973-1974, public welfare accounted for 9.6% of direct general expenditures, health and hospitals accounted for 7.0%, police protection accounted for 2.7%, and sanitation other than sewerage for 1.7%. /‾58, p. 7_7

The range of services offered by local governments has been expanded in the last century. Previously, essential services were considered to be those of sanitation, public primary and secondary school education, and police and fire protection. Since then, the concept of "nonessential services" has evolved and the goals of some cities have become very ambitious. The War on Poverty and other federal programs created expectations that forced cities to create self-help programs. For instance, Mayor Wagner of New York City explained a tax-increase in 1965 by saying:

> "I intend that we shall press ahead with the war on crime, the war on narcotics addiction, the war on slums, the war on disease, and the war on civic ugliness." /‾15, p. 33_7

Even when there seemed to be more of a concensus about the definition of vital services, the proper interest of investors and creditors in the level and expense of municipal services was unclear. Dimock, for instance, wrote in 1935 that:

> "The simple fact is that we are unwilling in this country to permit the creditors to determine what shall be spent for those municipal services and what shall be applied upon their debt." /‾13, p. 51_7

In recent years it has become much more difficult to estimate what municipal services will cost. The need for and use of services may fluctuate. Wage and benefit settlements are difficult to predict and may be retroactive.

For a typical city, revenue from its own sources is sufficient to pay for all local services other than education, hospitals, housing, and welfare. /_32, p. 26_/ As may be seen in Table V-1 (see page 169), local expenditures on services vary considerable because of the level of services offered, local need or use for those services, local government efficiency in service provision, and the proportion of costs paid by the state government. The fragmentation of local government has created separate municipal entities to provide a variety of services in the same locality. As discussed in Chapter IV (Disclosure of Debt Information), more than one municipal corporation may have debt-issuing authority and levy taxes on the same people and property. This has increased the difficulty of estimating the burden of service costs to taxpayers and of comparing the provision, utilization, and costs of service with those of other cities.

To understand the debt structure, it is essential to know what services the issuer provides. Beyond identification, the appropriate level of detail on services that should be disclosed and considered by the securities analysts is controversial. An "Overview of Factors Considered in Municipal Credit Analysis" submitted to the Senate Hearings on the 1976 Williams-Tower Bill noted:

> "The level of services provided by a municipality, and the extent to which they are utilized, is a critical input to financial stability. It is unusual to see services withdrawn; consequently, during economic downturns, the municipality may face unusual difficulties in meeting operating budgets. Increasing demand for services, as indicated by trends, must be considered with a perspective on corresponding changes in revenue generating capacity." /_63, p. 285_/

Table XIV-1

Comparison of Expenditure Purposes and Levels of Some Cities
(Dollars per capita) FY 1973-74

Standard Metropolitan Statistical Area (SMSA)	Education	Public Welfare	Health and Hospitals	Police and Fire	Interest on General Debt	Capital Outlays	Total Direct General Expenditures
Atlanta	241	8	80	40	26	111	562
Boston	274	7	79	85	26	70	595
Cincinnati	289	20	51	45	24	91	588
Cleveland	263	31	48	62	22	87	605
Dallas	229	1	53	48	50	147	563
Detroit	296	19	51	67	37	94	688
Houston	224	2	41	40	26	94	466
Kansas City	251	1	24	51	34	83	524
Milwaukee	300	101	45	58	24	96	751
Newark	324	86	27	74	27	52	734
New Orleans	174	4	28	48	29	71	451
New York City	344	286	150	90	67	194	1307
Philadelphia	273	28	27	53	36	83	607
Pittsburgh	266	10	19	31	30	87	510
St. Louis	254	5	30	45	17	58	485
San Francisco	337	113	85	72	19	92	879

Source: (Compiled from) U.S. Bureau of the Census. Local Government Finances in Selected Metropolitan Areas and Large Counties: 1973-1974. (Series GF-74, No. 6), Washington, D.C.: U.S. Government Printing Office, 1976, Table 3.

In harmony with this advice, the 1976 Williams-Tower Bill suggests required disclosure of:

> "A description of the principal governmental and other services provided or performed by the issuer, the extent to which similar or differing services are performed by other governmental entities which serve the same geographical area and any major changes in such services in the last ten years. /̅63, p. 7_7

The 1976 MFOA Disclosure Guidelines recommend the same description of services except they recommend description of changes in the last five years only. /̅33, p. 11_7 Neither explicitly recommends disclosure of the total costs, cost per participant or service unit, and costs and participants or service units provided by overlapping local government entities or private philanthropic organizations. The 1965 State Technical Assistance Report, however, suggests that all expenditures be shown by category such as operations, capital outlays, and debt service. It suggests that an evaluation of an issuer should include an examination of the "percentage distribution of expenditure, by fund, to show relative functional claims on revenue and bond proceeds. /̅1, pp. 40-42_7 Such information has not been generally available to credit analysts as shown by the Summary of Reporting Practices finding that in 1975 only 44 out of 174 issuers included operating statements of revenues and expenditures for the most recently completed year. /̅63, p. 271_7

A comparison of fund expenditures could show, for instance, how expenditures on police protection compare with those for education. The history of their relative functional claims could be seen from a trend comparison of those fund expenditures -- if an analyst had access to operating statements for a number of years. It might be difficult to tell, however, how much of the change in expenditures for each program was due to change in the level of services offered, changes in utilization of services or program enrollment, increased wages and benefits for program employees, funding of accrued pension liabilities, and/or general inflation of costs or changes in efficiency. Another reporting recommendation sometimes considered for locally distributed annual report involves relating the costs of services to some measure of efficiency by comparing, for example, the response time of firetrucks with department budgets.

The 1965 State Technical Assistance Report also recommends disclosure of the physical volume of services to prospective bond buyers. It suggests that standard forms be developed to fit types of governments, liability, and selected functions. It suggests as an example that school districts should report the numbers of existing school houses, existing unsatisfactory school houses, school houses under construction, and detail such as the number of buildings, number of classrooms, capacity of buildings, and estimated costs of projects for which financing is being sought. /_1, pp. 41-42_7 This and other examples given, such as reporting of street mileage by type of construction, show a greater interest in the possibility of further capital outlays than in the current costs and levels of services.

Service disclosure standards and policies, then, necessitate assumptions about how municipal credit analysis should be done, whether such disclosure well cause investor pressure to reduce or otherwise change the services offered, and if investor influence is desirable or undesirable. Welfare will be considered as an example.

One difference between the private and public sectors is that municipal expenditures do not usually generate revenues and people do not pay taxes in proportion to services received. Welfare recipients do not usually pay much in local taxes or have much political power because they are poor and a numerical minority. Unlike police, fire, sewerage, and education, public welfare programs provide little that is of identifiable value to the persons and property whose taxes yield most of the locally generated revenues. Non-welfare-recipients may feel that welfare should therefore have lower priority.

As may be seen in Table V-1, local government welfare expenditures vary greatly. As mentioned before, local governments in the average metropolitan area spend 9.6% of their total direct general expenditures on welfare. /̲58, p. 7̲/ Per capita expenditures for welfare may vary by as much as one-fifth of total per capita expenditures.

Welfare costs fall under the "uncontrollable" category because federal law requires that the state determine elgibility requirements and benefit levels. The federal government pays between 50-80% of the federal welfare program costs depending on state need formulas. The state legislature has some control over local welfare expenditures insofar as that body determines the degree of local participation. Localities in New York State must pay 25% of total welfare costs, while those in California pay 16% and other localities pay very little. Only eleven states require local participation in Aid to Dependent Children. /̲35, p. 5̲/

As mentioned earlier, the 1976 Williams-Tower Bill and the 1976 MFOA Disclosure Guidelines suggest disclosure of "a description" of the services provided or performed by the issuer. What will this description consist of? One description of welfare services could detail exactly what benefits are offered, who is elgible, how many people receive welfare or send their children to day-care centers funded by the city, and the costs per participant for each welfare program. Another description could only describe facilities used by the programs and speculate on whether the city will issue more debt to expand those facilities. A different type of description could provide information on welfare financing -- how funds are budgeted and administered.

The results of the Indicator Survey showed that bond dealers were fairly interested in welfare expenditures. They rated "total welfare" 25th and "changes in welfare expenditures in last five years" 26th in importance relative to the other seventy-two indicators. The welfare indicators were rated as the least important of the eighteen financial indicators but were rated as more important than employment by the city and many other economic, property, and social indicators.

It is obviously reasonable to disclose local responsibility for welfare funding. However, if that is all that is disclosed, an analyst would not be able to make assumptions about how much utilization and total program costs will increase if there is a downturn in the local economy. If a city reports to the investment community how many families are on welfare, what the level of benefits is, and about supplementary programs, the investors may disapprove enough not to buy the city's bonds even though the investors may not have cared enough about welfare costs to investigate them independently.

A letter to the U.S. Senate claimed that day-care programs in New York City were costing $6,000 per child enrolled. If the City had reported to investors total costs of the day-care program and number of participants, the underwriters might have raised this and similar questions about efficiency when the City tried to negotiate a bond sale. If it had reported the same information to a "watch-dog" committee of taxpayers, they might have raised the same questions. The investors, however, might have interpreted this information as an example of inept management and based their purchase decision on that as opposed to their concern over actual costs. In fact, city officials probably were not aware of the per participant cost. This shows a need for a better review of management and internal accounting, but those results should probably be kept private.

Chart V-4

Disclosure Recommendations on Employment Information

Recommending Report	Types of Descriptive Information Recommended			
	Total Number of Employees and Payroll	Employees by Class, Program, or Fund	Trends of Employment and Cutbacks	Unionization and Contract Information
1951 New York City Report	No	No	No	No
1963 IBA Format	No	No	No	No
1965 State Technical Assistance Report	No	No	No	No
1976 MFOA Disclosure Guidelines	No	No	No	No
1976 Williams-Tower Bill	No	No	No	No

(B) Disclosure of municipal employment information

Disclosure of the level of municipal employment was not suggested by the 1951 New York City Report, the 1963 IBA Format, the 1965 State Technical Assistance Report, the 1976 MFOA Disclosure Guidelines, or the 1976 Williams-Tower Bill. The National Committee on Governmental Accounting and Lennox Moak did, however, recommend that the number and distribution of employees be included in the comprehensive financial report. [28, p. 445] As part of the Indicator Survey, "Employment by the city and other financial units over the last five years" received an importance ranking by bond dealers that placed it only 30th out of 74 indicators.

How important is the wage and salary component of city expenditures? While wages are a large proportion of total operating expenses, should it matter to investors whether the money goes for police officers or police cars, for heating or teachers? Would review of city employment by securities investors and credit analysts help improve efficiency or undermine citizen influence? Is city employment really a factor that might affect bond security?

In a composite employment picture, 1.6% of the total population of American cities are employed by the city or other municipal entities. Of them, 19% are employed in public education, 16% in police protection, and 9% in fire protection. [20, p.111] Muller found a large difference in municipal employment in large cities with increasing populations and large cities with decreasing population. In fiscal year 1973, the thirteen cities that had over 500,000 population and an increase since 1960 employed 13.1 people per 1,000 residents for municipal service delivery other than education. The fourteen cities that had over 500,000 people but a decrease since 1960 employed 18.7 people per 1,000 residents. New York City employed 31.7 people per 1,000 residents for municipal service delivery other than education. The difference in employment levels for these cities closely paralleled the difference in their per capita operating outlays. /̅32, pp. 50-51_7

Besides the difference in level of employment, there are differences in average wages, benefits, and duty hours, all of which affect total expenditures. Gross wages for municipal employees cost $141 per capita in the thirteen cities that increased in population, $240 per capita in the fourteen cities that decreased in population, and $637 per capita in New York City. Whether because of starting salaries, seniority, or overtime, in 1974, New Orleans paid its sanitation workers an average of $4,170, while New York City paid its $15,924; Baltimore paid its police and fire officers $10,098 and $10,980, respectively, while Los Angeles paid its $15,833 and $21,280; Denver paid school teachers $13,505, while Detroit paid $22,603. /̅6, Table II-15_7 In the thirteen cities with increasing population, fire department members were on duty an average of 54.9 hours per week; in the fourteen cities with decreasing population size, they were on duty 49.9 hours per week, and, in New York City, only 40 hours per week. /̅32, p.41_7

Low-income families and high-density areas need more labor-intensive services than suburban areas. Municipal employee associations in cities with increasing populations appear more able to press for favorable contract terms involving wages, hours, and fringe benefits than those in growing cities. /̅32, p. 44̲7 High-density areas are more vulnerable to strikes by public employees. The growth of collective bargaining helps to account for expansion in short-term floating debt to finance current operations -- especially when the final contracts are not set prior to the establishment of the tax levy for the next year. /̅27, p. 376̲7 As explained in the next section of this chapter, collective bargaining has probably led to increased pension liabilities, which are not always sufficiently funded and present a real threat to bond security.

Many cities have reduced the level of services offered, capital improvement programs, and administrative and service staffs as part of economy moves. A trend comparison of fund accounts might show that education had been cut back proportionately more or less than police protection. Unless considerable detail about particular expenses were shown, however, it would be impossible to tell whether educational program cutbacks involved closing the schools after hours, increasing the teacher-pupil ratio, declaring a moratorium on new construction of school facilities, or whether the cutbacks were a simple response to a decline in school enrollment. Detail on employment trends by department may be more illustrative. New York City had large numbers of positions that were approved in the budget but not actually filled and positions that had been described to investors and creditors as eliminated but that were actually filled. An independent auditor might be able to help with these problems of employment reporting accuracy and be able to provide the city with a succinct statement for prospectus reporting.

Reporting by the city staff or auditor on program employment and payroll trends would not solve the problems of comparability of municipal employment data. Figures (such as those given earlier for number of employees per 1,000 residents, municipal employee wages per capita, and average salaries) are regularly gathered and published by the U.S. Department of Labor and the Bureau of the Census. Comparisons for the purpose of bond analysis are difficult, because the data are usually aggregated for all local governments. Employment figures may also be misleading because of the common practice of contracting with private employers for the provision of certain services, such as garbage collection or special education.

Unionization of municipal employees may lead to higher wages and benefits, shorter hours, and fewer layoffs. Strikes may be very disruptive. For these reasons, analysts may want to consider how many city employees are union affiliated, how active those unions have been and whether they have ever called a general strike, whether the city has a binding arbitration agreement, and how large contract settlements have been. Some cities have discussed employee unions in their prospectus statements. Boston, for example, gives the dates at which various contracts will expire and need to be renegotiated. [8, p. 10] Unionization of municipal employees is a controversial subject. Disclosure policies might interfere with off-the-record resolutions and other management strategies. The experience of private companies that file with the SEC and must disclose labor disputes to stockholders and other creditors may be helpful.

Chart V-5

Disclosure Recommendations on Pension Funding Information

Types of Descriptive Information Recommended

Recommending Report	Unfunded Accrued Pension Liabilities	Description of other Material Liabilities	Actuarial Basis of Pension Funding	Trends of Issuer's Fund Contributions	Trends of Annual Benefit Payments	Litigation of a Potentially Substantial Nature
1951 New York City Report	No	No	No	No	No	No
1963 IBA Format	No	No	No	No	No	No
1965 State Technical Assistance Report	No	No	No	No	No	No
1976 MFOA Disclosure Guidelines	Yes	No	Yes	Yes	Yes	Yes
1976 Williams-Tower Bill	No	Yes	No	No	No	No

C. Disclosure of employee pension funding information

> "In many of our governmental units, there are today significant hidden future costs that have not yet been identified either to investors or taxpayers. One of the most significant of these is unrecognized pension costs but they must also include other amounts for services rendered that have not been recognized and recorded." /̲ 63, p. 43 7̲

Although recently the adequacy of pension funding has become of great concern to taxpayers and to the municipal securities market, formerly it was almost ignored. A 1972 list of "information required for a rating" published by Standard & Poor's (one of the two most influential rating agencies), does not mention pension funding. Until recently, the recommendations given for municipal disclosure -- the 1951 New York City Report, the 1973 IBA Format, and the 1965 State Technical Assistance Report -- do not discuss pension funding either.

The size of municipal expenditures on employee pensions is determined by:

(1) Numbers of municipal employees

(2) Contract specifications for pension formulas

(3) How the actual rate is determined -- one base year or an average of base years, counting of overtime pay

(4) Cost of living clauses

(5) Benefits extended to spouse and children

(6) How long employees live

(7) Contributions from the state, social security, and employees into the fund

The adequacy of funds to pay for municipal employee pension benefits is determined by:

(1) Sufficiency of general municipal revenues

(2) Whether the municipality has previously established a retirement trust fund

(3) Actuarial assumptions used in computing fund requirements

(4) Provisions if the municipality cannot meet its pension obligations

If there were no inflation and cost-of-living pension increases, if the numbers of municipal employees were constant, and if they all retired at the same age and lived to the same age and were paid the same wage-and-benefit packages, then the annual cost of pension benefits to the municipality would be constant. There would be no point to having a pension fund. However, none of these conditions hold. Employment by municipalities increased considerably in the last forty years -- particularly in the sixties. Unions of municipal employees have become strong. When a union strikes, or threatens to strike, it is easier for the administration to agree to increase basic pension benefits, extend benefits to those who retire early and their families, agree to cost-of-living indicators, or agree to allow base pay scales to be computed from the last year or two before retirement than to pay cash for increased wages. Employee benefits average about 35% of base wages. Between 1967 and 1972, membership in municipal retirement systems increased by 28% and local government contributions to those funds increased more rapidly than wages. So an action that was "easier" in the short run created problems in the long run.

Many cities have had no savings plan to pay for their accumulated pension obligations. In many of the older cities, the average age of municipal employees is higher so that the number retiring will continue to increase. [32, pp. 46-47] In June 1976, the City of Oakland discovered that its unfunded pension liabilities were more than five times its annual budget. Oakland, San Francisco, and other cities are now saving for previously unfunded pension liabilities not yet due in addition to paying the pensions of those already retired. For every dollar it pays in salaries, San Francisco pays seventy-four cents into its police retirement fund. /¯52_/ Various estimates have been given for unfunded pension liabilitiies -- in Los Angeles, $1 billion; in New York City $3-6 billion; in Massachusetts, $7-8 billion. /¯52 and 47, p. 33_/

Bond dealers surveyed rated "pension liabilities and funding provisions" as having a mean importance rating of 1.7 on a 1 to 5 scale or 21st out of 74 indicators (Indicator Survey). Although that is still in the range of "very important", it is surprising that the bond dealers did not rate pension funding information as being more important because some cities have much greater unfunded pension liabilities than they have bonded debt outstanding -- presenting a real threat to bond security.

The 1976 MFOA Disclosure Guidelines give a good description of how pension liabilities should be described to bond investors:

> "Describe briefly the issuer's or the enterprise's pension and other employee retirement plans and the methods by and basis (e.g. actuarial or "pay-as-you-go") on which the plans are funded. State the issuer's or the enterprise's contributions to the plans for, and the unfunded accrued liabilities as of the end of, each of the last five years. State the annual benefit payments, net of employee contributions and interest earnings of the plans, for each of the last five fiscal years, unless the plans are fully funded. State the date of the most recent actuarial study, if any, and describe briefly the assumptions upon which the study was based. If contributions are made on an actuarial basis, state the year in which such basis was first used to determine contributions and the extent to which any deficiencies in contributions prior to such time have been eliminated." /¯33, p. 8_/

Describing current pension liabilities to the bond market may become even more complicated than a statement of funding provisions and actuarial bases would be. In 1976, the City of Englewood, Colorado sued the State of Colorado in an effort to invalidate sections of the State pension law that municipal officials believed could bankrupt the City's pension plan fund. Under the Colorado Police Pension Statute of 1935, the State sets up the level of benefits and the levels of contributions from the State, the City, and the officers' pay. When the suit was filed, the contributions from these sources were inadequate to pay for accrued benefits. The City attorney charged that the police and fire pension funds had been creating a condition of debt which will have to be paid by City tax revenue and that this had been unconsitutional. [3, p. 5]

This is not the first time cities have become involved with suits that could significantly alter their financial condition. Traditionally, the bond counsel explained to the purchasers of their securities the financial potential of such cases. An increase in the number of cases makes it more difficult for securities dealers and investors to keep up-to-date. Because the outcome of some cases might affect other cities that are not parties to them, the goals of disclosing all "material" facts and of considering everything relevant in a thorough analysis become even more difficult to reach.

Cash and security holdings of all state and local retirement systems increased by 40% in three years --from $62 billion in 1970-71 to $87 billion in 1973-74. [32, p. 46] The trustees responsible for investment decisions will probably have increasing economic and policial power. The employee pension funds were very important in New York City's cash shortage -- first, pension managers said that the City's bonds were too risky for them to buy; but under threat of increased layoffs of union employees, the pension funds finally bought large amounts of notes and bonds that the City had been unable to sell elsewhere and agreed to defer repayment on some securities. [15] Because of such situations, the management and investment policies of municipal pension funds may become a factor to be scrutinized by analysts and by the rating agencies.

These examples show that disclosure of pension funding may be technically difficult. In order to comply with the 1976 MFOA Disclosure Guidelines, many municipalities may need to commission special studies they might have otherwise forgone. The detail and legal language necessary to describe pension funding may be of little interest to the unsophisticated investor. The range of contingencies that might be considered relevant is large. It may be difficult to keep disclosure statements up-to date on the progress of litigation aggecting pension liabilities.

Disclosure of pension funding also raises broader questions. Many cities would be in a better financial position now if the extent of their increasing pension liabilities had been realized earlier. If these cities had been well managed, the sums would have been discovered and steps taken to set up a viable funding plan. Ten years ago, the rating agencies could have threatened to downgrade cities without reasonable pension funding plans and the securities market press could have drawn attention to this need. The chances of pension-funding problems being discovered would have been greater if there had been more independent analysis. However, if disclosure guidelines had been mandated ten years ago following the suggestions given by the various committees of experts, disclosure of pension funding provisions would not have been required. Disregarding reporting costs, disclosure for the purpose of providing more opportunity for an analytic check cannot reach its full potential of usefulness unless some analysts have access to a very wide range of information. This range may be much wider than the average bond dealer or bond investor is interested in. This suggests a dual structure of information release.

The size of unfunded pension laibilities is in some ways surprising because pension benefits are a liability that the cities have directly contracted and that some people have a direct interest in. Hidden future costs have been historically more associated with contingent liabilities. In the 1930's, for instance, many municipalities found that canals and other water transport facilities that had been profitable were no longer in demand. If the municipality had partially funded their construction through bonded debt, it was forced to either subsidize the canal out of general funds or default. [27, p. 167] What might other future hidden costs for municipalities be? If, for instance, large metropolitan airports become less in demand because there is more traffic to small airports scattered about the region, then cities may be called upon to subsidize them. Does this very questionable possibility mean that cities should try to disclose airport use and finances now so that the market can react by estimating the risk? Disclosure of all contingent liabilities is a difficult proposition.

D. Summary and Conclusions

Operating expenses account for 85% of average total expenditures and are difficult to reduce. Their size and the importance of municipal services to the functioning of the locality make operating expenses a threat to bond security. Operating cost overruns are as important as under-estimation of expected revenues in causing year-end deficits. The bond dealers surveyed by the author ranked "Excesses in operating expenditures over originally approved budgets" as tenth in importance out of 74 indicators -- higher than other important indicators. (Indicator Survey)

City services affect citizens more than they do investors. Taxpayer pressure is a strong force to limit expenditures. Checks on the legality of expenditures are routine.

Direct general expenditures vary a great deal. Reasons include the level of services offered and utilized, the number of city employees, how much they are paid, what benefits and pensions they received and how those are funded, and how payment for certain services are share with the state. Services and service program payrolls account for the largest share of expenditures. Unfunded pension liabilities are often larger than total outstanding bonded debt.

The local political forces affecting service levels make service disclosure controversial. An article on municipal credit analysis explained that the provision and demand of services is a "critical input to financial stability". /̄63, p. 285_7 The 1976 MFOA Disclosure Guidelines and the 1976 Williams-Tower Bill recommend disclosure of a "description" of service provided. That could consist of a simple definition of government purpose, detail on service finances, or discussion of particular service programs -- their finances, facilities, and use. Welfare is an example of how disclosure may facilitate investor involvement, which may lessen the influence of local groups. This shows that service disclosure necessitates policy decisions.

City employment is an important and varying factor in total expenditures and in cost reduction strategies. Bond dealers surveyed were not as interested in city employment information as they were in many other factors. The National Committee on Governmental Accounting is the only source of those mentioned in this paper that suggested reporting of city employment information. A breakdown of employment for each service, administration, and other programs could help illustrate priorities and strategies in economy moves and make it easier to understand pension liabilities. An independent auditor may be needed to ascertain accuracy of employment information. The status of unionization of city employees may be very important to its finances but a reporting policy may be politically difficult.

The recent exposure of the size of unfunded pension liabilities in many cities is a strong argument for mandatory disclosure as another check on local government finances. However, even sophisticated analysts did not anticipate its emergence as a factor. While the technicalities of pension disclosure will probably be adequately resolved, the broader question is whether the range of information relevant to local finances can be limited so that it may be effectively disclosed.

VI. Investor Perceptions of Local Economic Factors and the Character of Local Communities -- Disclosure of Information on Economic and Social Factors

It is people and their property who need services, and people and businesses who pay taxes. Bonded debt is assumed to pay for facilities used directly by people and for improvements to the physical assets of the area. Decisions on operating expenditures, capital improvements, tax rates, bond issues, and default are made by the management of the local government with input from citizens, business leaders, and the state government. Therefore, the economy of the issuer, the economy of the region, social factors of the community, and the management of the local and state government are among the factors affecting bond security. They are less immediately causal, however, than financial factors.

Investor opinions of the City of Boston, apparent from the results of the Perceptions Survey, are an example of how people operating in the municipal securities market may perceive the local economy and character of a well-known city. (See Appendix II for the survey format used and information about its distribution.) These results are compared with information that is theoretically important and with categories of such information whose importance has been rated by respondents to the Indicator Survey. This chapter has five sections: (A) The theoretical importance of nonfinancial factors, (B) Investor opinions of the City of Boston -- results of the Perceptions Survey, (C) How investors might have formed their impressions of Boston, (D) Disclosure of nonfinancial information, (E) Summary and conclusions. The following charts display relevant data from the Indicator Survey and the Summary of Financial Officers; a chart preceding Section D compares the disclosure recommendations cited.

Chart VI-1

Frequency of Reporting Nonfinancial Information in 1975

	Indicator	Reporting	Not Reporting
Description of the population	1975 population	110	64
	1970 population	114	60
Indicators of wealth and income	Median family income -- own unit	20	154
	Median family income -- SMSA	3	168
	Total personal income of residents	14	160
Information describing the local economy and employment	List of major industrial firms located in area (with employment figures)	50	119
	Data on number of employed persons in major employment categories	10	164
	Data on level or rate of unemployment	4	170

Source: (Excerpted from exhibit submitted by Professor Ronald Forbes, New York University) U.S. Congress, Senate. Committee on Banking, Housing, and Urban Affairs. Hearings before the Subcommittee on Securities on S. 2969 to Amend the Securities Exchange Act of 1934 to Require the Preparation of Annual Reports and Distribution Statements by Issuers of Municipal Securities, and for other Purposes, S. 2574 to Amend The Securities Act of 1933 to Provide for Registration of Securities Issued by State and Local Governments, February 24, 25, and 26, 1976. 94th Congress, Second Session, Washington, D.C.: U.S. Government Printing Office, 1976, p. 271.

Chart VI-2

Results of Questions on the Indicator Survey

Concerning Nonfinancial Information

	Indicator	Relative Importance Ranking (out of 74)	Mean Importance Rating (on 1-5 scale)	Proportion Desiring Comparisons (%)
Population Characteristics	Total population	22	1.7	54
	Racial distributions	35	2.4	48
	Educational level and skill-training of workforce	39	2.6	51
	Migratory trends by economic class	41	2.6	46
	Educational level of population	43	2.7	54
	Percentage of city workforce living inside the city limits	49	2.8	25
	Population density	52	2.8	48
	Crime rates	55	2.9	56
	Population by age group	60	3.1	51
	Percentage of census tracts with median incomes above city median	61	3.1	15
Information on Local Incomes	Median household income	14	1.6	80
	Percentage change in median household income in last five years	29	2.1	37
Information on the Local Economy and Employment	Ten largest industries in the city	11	1.5	34
	Unemployment rate	19	1.7	70
	Number of industries by type and dollar value that opened or entered in last five years	28	2.1	45
	Number of industries by type and dollar value that left or closed in last five years	31	2.1	44
	Financial insitutions with home offices in the city, by rank, type, size	38	2.5	27
	Energy costs	41	2.6	54
	Number of strikes in city in last five years affecting major institutions	46	2.7	41

(cont.)

Chart VI-2 (cont.)

	Indicator	Relative Importance Ranking (out of 74)	Mean Importance Rating (on 1-5 scale)	Proportion Desiring Comparisons (%)
Information on the Local Economy and Employment	Labor participation rate	48	2.8	44
	Percentage of workforce that is union affiliated	53	2.8	42
	Number of Furtune 500 firms with repesentative offices in the city	57	3.0	28
	Sector analysis of production	62	3.3	29
	Commuting trends	63	3.3	22
Measures of Economic Activity and Indirect Evidence of Wealth	Trends in vacancy rates for commercial property	32	2.2	54
	Average value of building permits by type and volume in last five years	33	2.2	49
	Trends in vacancy rates for residential property	34	2.3	50
	Cost of living indicators	36	2.5	65
	Value of commercial bank deposits	37	2.5	43
	Trends in retail trade	45	2.7	43
	Average annual absorption rate of commercial office space	50	2.8	33
	Trends in wholesale trade	45	2.7	43
	Volume of luxury and prestige housing	56	3.0	27
	Average investment in recently rehabilitated office space	64	3.4	29
	Shipping tonnage and traffic	65	3.4	30
	Average investment in recently rehabilitated dwelling units	66	3.4	29
	Rail tonnage and traffic	67	3.4	30
	Truck tonnage and traffic	67	3.4	28
	Airflight tonnage and traffic	70	3.4	31

A. The theoretical importance of nonfinancial factors

Lennox Moak* describes many financial and nonfinancial factors theoretically affecting these decisions:

"(1) The decision of the rating agencies concerning the quality of the credit of the issuer.

(2) The decision of the investment banker to purchase or not to purchase the credit instruments -- and the rates of interest to be charged.

(3) The decision of the investor to purchase the credit instrument at the yields offered, or to put his money in some alternative investment." [27, pp. 169-170]

He asserts that using a measure of local fiscal capacity requires consideration of the economic framework of the community as well as the narrow definition of the tax and revenue bases. He suggests that these economic criteria are used by investors and rating agencies:

(1) Geographical area of the municipality
(2) Trend in numbers of residents
(3) Location of area
(4) Sources of economic activity
(5) Volumes of economic activity
(6) Maintenance of the economic plant
(7) The identity of the primary employers and their position in the regional and national community
(8) The kinds of manufacturing, wholesale trade, and retail trade conducted in the area and their relation to the national community
(9) Diversification of employment
(10) How far the residents have to commute to work
(11) Dependence on regional agricultural output. [27, pp. 160-161]

Moak claims that investors are concerned with the distribution of income among population segments, as well as with the primary measures of the current economy which are primarily the per capita income and the income of local businesses. [25, p. 160] He claims that the best index of the economic base is "total tangible property values per capita" whether the

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* Moak is cited quite often in this chapter so that his assertions can be compared with the survey data.

property is real or personal, taxable or nontaxable. In addition to taxable property values, he suggests that investors should consider the value of tax-exempt property and estimate the value of residents' personal property.

Investors may evaluate the general and fiscal management of local governments when buying local government securities as they evaluate corporate management in other investment decisions. Moak advised:

> "A well-administered government which keeps people informed of this fact, especially those persons who help to form opinion in circles which help to influence investors, will ordinarily reap dividends of substantial dimension." [27, p. 165]

Forbes also emphasized the willingness of the local government to attempt to influence and control external factors. [63, pp. 285-286]

Moak lists "educational opportunities, cultural opportunities, recreational facilities, the community record of handling problems of social unrest, the housing stock, and characteristics of the population" as being the most important social factors. He discusses how institutions of higher education, cultural opportunities, and recreational facilities can enrich a community and attract industries. Furthermore, "Investors have begun to show a marked reluctance to extend credit on equal terms to cities with great unresolved social problems as contrasted with areas not so confronted". [27, pp. 163-164]

Moak suggests that the following statistical measures of economic activity are sometimes useful as indirect measures of wealth and income:

Water-borne cargo tonnage	Military expenditures
Freight carloadings	Value of construction
Trucking tonnage	Building permits
Motor vehicle registrations	Retail sales
Gasoline consumption	Department store sales
Number of tourists	Postal receipts
Kilowatt hours produced	Bank deposits
Average daily water consumption	Newspaper circulation
Value added by manufacturing	Enrollment in local universities [28, p. 394]
Industrial payrolls	

In fact, one author of prospectus statements, said that some investors ask for such information. /‾21_/

Moak claims that analysts learn through experience to scan such information and make quick decisions although they must "caution themselves to avoid emotional reactions to current personalities or to events of transitory or superficial importance." In summary, he writes:

> "The factors discussed in the preceding pages help to determine the degree of risk that is likely to be involved in a given bond issue with a given pladeged security. In a number of respects, the discussion is admittedly theoretical, but, if it is good theory, it is likely to be good practice as well. This is not to suggest that a poor rating in a number of these factors will make the debt unmarketable. It is to say, and to say emphatically, that they influence the price at which the debt may be sold in any given general municipal bond market." /‾27, p. 170_/

The rating agencies consider at least some nonfinancial information when they assign credit ratings to municipal issuers. Figure VI-1 shows information considered by Standard & Poor's Corporation and by the Fitch Investors Service. (see page 194)

Very little research has been conducted on how such factors actually affect the quality of local government finances. It is not clear that investors actually consider all of the information that Moak says they do or that the rating agencies claim they do. One statistical study that has been completed shows significant financial differences between cities that have increasing population levels and those that have decreasing population levels. /‾32_/ Another statistical study has contradictory findings:

> "Population has minimal effects when other variables are included in the analysis. The percentage of Irish residents is distinctly associated with higher spending...Cities tend to suffer greater fiscal strain if they have powerful mayors, weak businessmen, union contracts for municipal employees, "overstaffing of municipal employees, and low rates of tax collection. These five leadership characteristics tend to go together, be associated with numerous Irish residents, and in turn to increase capital outlays." /‾10, p. iii_/

Figure VI-1

Nonfinancial Criteria Used by the Rating Agencies

by Standard & Poor's Corporation:

(1) Recent population estimate.
(2) List of the ten leading taxpayers with their assessed valuations, including the number of employees for large taxpayers.
(3) Brief description of the economy of the area, including the character of development, the level of housing activity, and the value of homes (for residential areas).
(4) School enrollment for the past ten years (where applicable).

by Fitch Investors Service:

(1) Ability to pay:
    (a) Location and transportation trends.
    (b) Population trends -- quanitative.
    (c) Population characteristics -- qualitative Wealth as measured by home ownership, per capita assessed valuation, family income, education.
    (d) Character of the local economy -- industrial, residential, trading and commerce, agricultural, mining, suburban, resort, and diversification of sources of employment.
    (e) Presence of stabilizing institutions -- colleges, government establishments.
    (f) General economic indicators -- employment, building permits, bank deposits, etc.
(2) The type of government and political situation may be a factor in willingness to pay.
(3) Economic factors which may indicate potential trouble:
    (a) Declining population.
    (b) Extraordinary rapid population growth.
    (c) Shift of racial or economic character of population.
    (d) Declining general economy -- loss of industrial plants, change of fashions, change in modes of transportation, obsolescence or depletion in major industry.

Source: Excerpted from statements submitted to Congress by the rating agencies and printed in: U.S. Congress, House. Hearings before the Subcommittee on Consumer Protection and Finance of the Committee on Interstate and Foreign Commerce, House of Representatives on H.R. 675, A Bill to Amend the Investment Advisors Act of 1970 to Provide for Regulation of Persons Rating Municipal Bonds. 94th Congress, Second Session, Washington, D.C.: U.S. Government Printing Office, 1976, pp. 37, 76, and 77.

B. Investor opinions of the City of Boston -- Results of the Perceptions Survey

A survey asking opinion questions about Boston was mailed to a group of bond buyers which was almost identical to those receiving the Indicator Survey. In total, 172 responses were received in June and July of 1976 to the Perceptions Survey. Both surveys, as mentioned earlier, were mailed in cooperation with the City of Boston, using the city's letterhead and mailing list and signed by the Treasurer of the City of Boston. The purpose of the Perceptions Survey was diagnostic. Copies of the survey forms, tabulated reaults, and a more detailed description of its distribution are included in Appendix II. In the following discussion, results to the questions are grouped by subject area instead of by question format or order in which they appeared on the survey form.

1. Perceptions of the local economy

The survey included a number of questions on major and minor aspects of the city's economy. When respondents were asked to rate the current situation of "business activities" in the City of Boston on a 1-5 scale (with "1"="very good", "2"="good", "3"="average", "4"="poor", and "5"="very poor"); the average was 2.70 (falling between "good" and "average"). They were asked whether they "perceive" "decline in manufacturing" as among "significant problems which the City of Boston must resolve to maintain economic prosperity"; and 50% of respondents did consider it to be a problem, 12.5% did not, and 37.5% did not know. In another question, respondents were asked to make projections for the City of Boston in the next five years of certain factors by checking possible responses. Their answers were evaluated by assigning numerical values ("4"="much greater", "3"="greater", "2"=

"current", and "1"="less than") and computing the mean. The future of "economic well-being of manufacturing industries" was rated to be 1.62 (between "current" and "less than" -- a fairly negative response). The future of "economic well-being of major retail business" was rated to be 1.87 (between "current" and "less than", also). The future of "economic well-being of financial institutions" was rated to be 2.23 (between "current" and "greater").

Other survey questions dealt with more minor aspects of Boston's economy. When asked to make projections (over the next five years), the bond dealers rated the future of economic well-being of high technology, R & D industries, and specialized consulting firms" at 2.34 (between "current" and "greater"). They rated the future of Boston's "popularity as a convention center" at 1.84 (between "current" and "less than") and the future of its "popularity as a home office" at 1.60 (between "current" and "less than" -- the poorest projection of this set of questions). A few other questions using different formats also asked respondents to rate minor aspects of the city's economy: "Cutbacks in military facilities" was considered to be among "significant problems that Boston must resolve in order to maintain economic propsperity" by 31%, however, 21% did not consider it to be a problem and 48% did not know; the current situation of "transportation and road systems" was rated at 2.63 (between "good" and "average"); and the current situation of "medical care facilities" was rated at 1.83 (between "good" and "very good").

These results include evaluations of many aspects of the economy that Moak considers to be factors important to investors and rating agencies in determining preference. Manufacturing industries, important both as employers and as taxpayers, were seen to have current and worsening problems. The opinion of the dealers that the transportation and road systems were above average suggests that shipping problems are not a reason for the decline of manufacturing. Retail business (a source of state sales tax, a potential tax source for the City of Boston, and an indicator of the "spending money" of the population) was also seen as declining. The city's general attractiveness to business people as a home office and convention center was seen as falling. However, high technology and medicine in the area seem to have better reputations -- although their potential as a source of tax revenue, primary employment, or attraction to other business is unclear. In general, then, investors' opinions of Boston's economy are somewhat negative with some areas of hope.

Forbes had emphasized the "controllability" of economic factors and the willingness of local government to do so. It is, however, unclear how much industry can be attracted and nourished by favorable local tax structures or aid in site location and preparation when these costs are a small part of total costs to business (compared with other factors, such as labor and energy, most of which local government cannor influence), when relocation is inhibited by moving costs, and when other local governments are competing to attract industries.

2. <u>Perceptions of the quality of city government</u>

Ten questions were asked relating to the reputation of the quality of the city's government, which Moak, Forbes, and Fitch Investors Service had emphasized. A very general question asked respondents to rate the current situation of "effectiveness of city government" on a scale from 1-5 ("1"= "very godd", "2"="good", "3"="average", "4"="poor", and "5"="very poor"). The mean of the responses to this question is 3.35 (falling between "average" and "poor"). Respondents were also asked to "rate the City of Boston's policy making and administration" in the following areas with possible responses of "good", "adequate", "poor", and "don't know". The mean ratings were computed (using "3"="good", "2"="adequate", and "1"="poor"); only one mean rating fell in the range of "adequate".

	Criteria	Adjusted Mean Rating	
(1)	Optimization of economic impacts of health care industry:	2.08	"adequate"
(2)	Provision of police and fire protection services:	1.97	"poor"
(3)	Input into decisons of the Massachusetts Port Authority regarding its financing and operating of facilities such as Logan and the Harbor:	1.85	
(4)	Input into decisons of the Metropolitan Boston Transit Authority regarding its financing, service levels, and capital improvements:	1.82	
(5)	Maintenance and imporvement of roads, sewers, and parks:	1.72	
(6)	Negotiating in securing federal funds:	1.66	
(7)	Negotiating tax abatements at reasonable levels for city interests:	1.60	
(8)	Planning for educational programs and facilities and implementation of the desegregation order:	1.53	
(9)	Negotiating arrangments with municipal unions and public employees:	1.35	

These results imply an overall lack of faith in the managerial ability of Boston's city government. The low ratings on the questions concerning its influence with the Massachusetts Port Authority, the Metropolitan Boston Transit Authority, and the federal government (criteria numbers 4,5, and 6) show an uncertainty regarding its ability to deal with intergovernmental politics. The results concerning its policy making and administration in negotiating tax abatements and in public education (criteria numbers 7 and 8) cast doubt on the City's ability to deal with local taxpayers and citizens, although the administration is rated more highly on its ability to deal with hospitals (criteria number 1). The evaluations of "provision of police and fire protection services" and "maintenance and improvement of roads, sewers, and parks" (criteria numbers 2 and 5) could imply criticism of the adequacy of its expenditures and of its internal administration; the latter hypothesis is also supported by the lowest mean rating in the section -- "negotiating arrangements with municipal unions and public employees" (criteria number 9).

This discussion is not meant to imply that the government of the City of Boston is actually inadequate or mismanaged or that the general securities market holds this opinion. However, as Mr. Moak warns: "Although reputations, both good and poor, are sometimes not warranted, the reality is that much opinion formation rests on the views of others". [27, p. 165] Many people have not formed an opinion -- good or bad -- on the quality of Boston's government -- the "don't know" response on the questions rating the city's administration was an average of 61% -- much higher than that on any other question.

3. Perceptions of Social Factors

Social factors may benefit or hurt a community by attracting population and business, enriching life or by increasing the need for certain service expenditures and undermining the commitment of citizens to the city. One purpose of the Perceptions Survey was to determine whether investors view certain intangible and certain natural assets as being present in Boston.

Respondents were asked to rate the current situation of "recreation, cultural facilities, and art" in the City on a 1-5 scale ("1"="very good", "2"="good", "3"="average", "4"="poor", "5"="very poor"). They rated the situation as being between "very good" and "good" (1.81), placing it higher than any other indicator on that question. When asked if its cultural facilities are an economic asset, 69% said "yes", 12% said "no", and 19% said "don't know". Of the total responses to that question, 38% cited examples, frequently mentioning the Boston Pops and prestigious universities in the area. When asked if its environmental qualities are an economic asset, only 29% said "yes" (26% said "no" and 45% said "don't know"). Of the total responses to that question, 17% gave examples frequently citing the Commons and Public Gardens, the architecture, and the proximity to the ocean. None of the responses to either of these questions gave examples of improvements that were new in the last twenty years.

Another question asked respondents to rate the current situation of "quality of life/environment" on a 1-5 scale ("1"="very good, "2"="good", "3"="average", "4"="poor", and "5"="very poor"). Boston received a mean rating of 3.32 or slightly below average. That may have something to do with the rating of "maintenance and improvement of roads, sewers, and parks" as below adequate (as mentioned earlier).

Population trends can be considered to be both an economic factor and a social factor. People may come to or leave an area for economic and for social reasons; once there they affect the economy, the social fabric of the community, and the finances of local government; their leaving in large numbers also affects the community. Certain population trends were mentioned in the exhibit prepared by Fitch Investors Service as "factors which may indicate potential trouble". (See page 194) In answer to a question on the Perceptions Survey of "How do you perceive population trends in Boston", 5% checked "significant out-migration to suburbs of Boston" and 25% checked "significant out-migration to other areas than Boston area". Only 1% of respondents thought that there has been "significant in-migration", while 18% thought there are "stable population levels, but significantly changing population composition". Another question asked respondents to project "overall population levels" in the City of Boston in the next five years. Of the total responses to that question, only 10% checked "greater" or "much greater", 35% checked "current", 45% checked "less than", and 10% checked "don't know".

4. Perceptions of school desegregation problems

Like many other American cities, Boston has been under federal court order to desegregate its public schools in a manner that involved reassigning many students and busing them away from their immediate neighborhoods. As has been highly publicized, Boston has had difficulty in implementing this requirement. There has been some violence in the schools and neighborhoods regarding the desegregation order, and eventually certain schools were put under federal court receivership. In response to one survey question, 97% thought that "school administration and desegregation" are among "significant problems that the city must resolve to maintain economic prosperity".

The problems in Boston related to implementation of the desegregation order can be reviewed for direct costs of administration and indirect costs of education quality. The problems can also be considered as to what they show about the quality of community and government leadership and other social factors. Some think that forced busing is causal of "white flight" and other economic changes. In an effort to see if the busing problems have affected financing costs and investment decisions, the Perceptions Survey included the following question:

How do you think that news coverage of the City of Boston's school desegregation order and related events have affected the City's financial reputation with potential investors?

Possible responses	Frequency of response (%)
The financial reputation that Boston has with potential investors has been improved:	1
The financial reputation that Boston has with potential investors has not been significantly affected:	4
The financial reputation that Boston has with potential investors has been somewhat damaged:	48
The financial reputation that Boston has with potential investors has been greatly damaged:	46
Don't know:	1

As mentioned earlier, "financial reputation" is said to be very important to the securities market. How much importance the market actually attaches to school desegregation problems is still unclear, however, as is how indicative of broad community problems they are. It is notable that on the last two questions discussed, both of which related to school desegregation, the "don't know" responses were only "3%" and "1%" respectively.

Three other survey questions are somewhat related to school desegregation. On a 1-5 scale, respondents rated the current situation of "educational levels" between "good" and "average" with a rating of 2.86 (with "1"="very good", "2"="good", "3"="average", "4"="poor", and "5"="very poor"). On the same scale, the current situation of "public safety" was rated at 3.32 (between "average" and "poor"). These questions had "don't know" responses accounting for 16% and 20% of the total. However, on another question that asked respondents to rate the City of Boston's policy making and administration on "planning for educational programs and facilities and implementation of the desegregation order"; 7% checked "good", 10% checked "adequate", 27% checked "poor", and a full 57% checked "don't know". These results suggest that the impact of the school desegregation situation is still fluid. It is possible that investors may still be reassured about the various aspects of the problem -- public violence, undermining of the teaching of basic skills, and the propriety of the city government's handling of the problem. Much depends on the future.

5. <u>Perceptions of Boston when compared to other cities</u>

Four questions asked respondents to compare the City of Boston to other cities. When asked to compare residential property values in Boston to those in other cities, 9% thought they were rising faster than those in other cities, 42% thought they were changing evenly with other cities, and 49% thought they are lagging behind other cities. This may show that investors think the property tax base is expanding or that the standard of living is lower.

"Investments in real property" include those in business and land and are important in maintaining and expanding the economic base. Only 3% thought investments in real property in the City of Boston are more attractive than other cities, 31% thought such investments are on par with those in other cities, and 66% thought that such investments are less secure. If the bond dealers who answered this question -- because of their contact with investment bankers, financial institutions, and wealthy individuals -- are either influential or representative, then Boston's economic base may have future problems (even if there is insufficient evidence to prove that other investments are better than those in Boston).

Because the rating agencies and purchasers evaluate municipalities on a comparative basis, the survey included two questions explicitly comparing Boston with fourteen other cities. Respondents were asked to compare Boston with each of the other cities in terms of "general economic chactereristics" and "general quality of life" by checking columns labelled Boston is "better", "worse", or "similar" than the other city, or that the respondent does not feel qualified to give an opinion. The results were ranked by computing a mean using a value of "1" if Boston was considered "better", a value of "0" if the two cities were considered "similar", and a value of "-1" if Boston was considered worse. The adjusted means were then inverted so that the city with the highest rating heads the list.

General Economic Comparison		General Quality-of-life Comparison	
tied for (1) and (2)	Dallas	(1)	Atlanta
	Houston	(2)	San Francisco
(3)	Atlanta	(3)	Dallas
(4)	San Francisco	(4)	Houston
(5)	Kansas City	(5)	New Orleans
(6)	Milwaukee	(6)	Cincinnati
(7)	New Orleans	(7)	Kansas City
(8)	Cincinnati	(8)	Milwaukee
(9)	Pittsburgh	(9)	Boston
(10)	St. Louis	(10)	St. Louis
(11)	Boston	(11)	Pittsburgh
(12)	Cleveland	(12)	Philadelphia
(13)	Philadelphia	(13)	Cleveland
(14)	Detroit	(14)	Detroit
(15)	Newark	(15)	Newark

Analysis of the survey results is somewhat limited because there does not exist similar data on investor opinions of other cities. The preceding questions help somehow to show that investors' overall negative opinions of Boston do not extend to all cities. However, more research is needed on comparing perceptions. For instance, if the above cities mailed questionaires to bond dealers receiving their prospectus statements with a similar question to that preceding, would the same ranking appear in their results?

6. Perceptions of Boston's securities

Most of the questions on the Perceptions Survey addressed opinions on the economy, the government, and social factors. The minds of respondents might have been preoccupied with the subjects stressed in the survey form (instead of with fiscal cash-flows and debt schedules). A few questions specifically concerned securities of the City of Boston; their answers could reflect various experiences.

A somewhat ambiguous question asked "How would you rate the security of Boston's bonds compared to...?" The following chart shows frequency of response and an adjusted mean rating (computed by assigning values of "1"= "more secure", "2"="as secure" and "3"="less secure" and omitting "don't know" responses):

	Frequency of Response (%)				
Comparison	More Secure	As Secure	Less Secure	Don't Know	Mean Rating
Compared to state and suburban issues not in Massachusetts:	2	11	73	14	2.83
Compared to other cities:	1	22	68	8	2.73
Compared to other Massacusetts municipalities:	1	30	53	15	2.62

Although the range of results in the preceding question is not very wide, they give some support to a hypothesis that, in addition to the quality of a particular municipality, there are other perceived risks associated with cities, with suburbs, and with state location. Of course, interest rates are also determined by external market factors.

As mentioned earlier, the Perceptions Survey was sent to a mailing list of bond dealers provided and used by the Treasurer-Collector's Office of the City of Boston, with a cover letter signed by the Treasurer. Those who responded to the survey (about 13%) may have had some special interest in Boston. It is impossible, however, to be certain what biases were introduced because of the low response rate. The most important question on the survey asked: "Would you consider buying a new issue of Boston's bonds if you were in the market for municipal bonds"? In response, only 18% said they would consider the bonds, while 22% were uncertain, and 60% said they would not even consider bonds of Boston. These results have implications for Boston's marketing strategy.

C. <u>How investors might have formed their impressions of Boston</u>

This section discusses the information that investors might have used in forming their impressions of Boston. It does not concern the state of Boston's economy and quality-of-life or the actual risk of its securities.

Five pages in one of Boston's recent prospectus statements are devoted to explaining the community. This explanation does not include all of the subjects mentioned in questions in the Perceptions Survey. The city's financial offices have on file all of the audit statements, prospectus statements, and other information on city finances which it has released over the years. Other sources, however, publish and release information about the city's economy and social factors. These sources include the U.S. Census Bureau, the U.S. Department of Justice, the U.S. Department of Labor, various agencies of the State of Massachusetts, the Boston Redevelopment Authority, the Mayor and his office, the School Board and Department of Education, various local and national news media, and many of the private industries, commercial establishments, financial institutions, and nonprofit organizations located in the city. There is no way to keep track of everything published. Part of this information is analyzed for various purposes by trade organizations, planning agencies, privately owned consulting firms, and universities. Representatives of the rating agencies also occasionally refer to Boston in newspaper interviews (for instance, as an example of a city with large, unfunded pension liabilities).

Full-time analysts who are self-employed, employed by financial institutions, or employed by a rating agency and every trader, underwriter, and investor who is a part-time analyst are exposed to some of this information. They may form an opinion of a small town at the time when they consider the quality of its security, but they already have some sort of opinion on every major city.

Part of their opinion may be from personal experience. Twenty-two percent of those who responded to the Perceptions Survey had lived in Boston or the Boston area. Another thirteen percent had visited it many times. Only twenty-one percent of the respondents had never been to Boston. Some included little notes about how they had loved the city when they lived in Boston until they retired and moved to Florida or how they had attended Harvard thirty years earlier. Because municipal bonds are bought by wealthy individuals and institutions, the same people who work and invest in the securities market are likely to have other investment experience. They may personally know people who are important in Boston's economy.

The results of this survey, and other diagnostic tools, may help show whether investors are getting the correct information and on what subjects they have not formed opinions.

One way in which Boston is different than other cities is the strength and size of its financial institutions. As the prospectus stated:

> "Boston's financial institutions manage about $80 billion in assets including more than a third of the nation's mutual fund industry assets. The city is the home of sixty major insurance companies, thirty national banks, and thirty savings institutions, and over a hundred co-operative banks." [8, p. 35]

The bond dealers surveyed seemed to be aware of this situation -- they gave an average future projection to "economic well-being of financial institutions" between "greater" and "current". They might have formed this impression from statements released by the city, from financial publications and business magazines, or through an acquaintance working in a financial institution. Another city, that did not have a thriving financial center, would probably have not mentioned it in its prospectus statement just as Boston did not discuss the status of its manufacturing industry (in its prospectus statement).

The status of "public safety" has a questionable relationship to bond security (although it might reflect attitude's of the community and be a factor in people's decision to move). This section discusses perception of crime rates, as data, because they were not included in the city's prospectus statement yet survey respondents had an opinion. Only 33 respondents (of the 146 who answered this question) did not "feel qualified to give an opinion". Of those who gave an opinion, 10% thought that the current situation of public safety in Boston is "good", 50% thought it is "average", and 30% thought it is "poor". Their perceptions are compatible with those of Massachusetts residents, as shown by the published results of a telephone survey. Of 1,000 people interviewed by telephone, 78% of those living in Boston who were called said that "crime and violence in the streets" is "a very serious problem". [4, p. 38] In fact, Boston has a reported victimization rate for all personal crimes of violence that is twice that of Washington, D.C. although other types of crime have relatively lower statistical incidences. [65] It is doubtful whether either the bond dealers or the citizens surveyed have ever seen crime statistics comparing incidence in Boston to that in other cities. Their perceptions must have been formed by a combination of personal experience, second-hand experience, and news coverage.

In at least one area, respondents to the Perceptions Survey were misinformed. As mentioned earlier, 9% thought that residential property values in Boston are rising faster than those in other cities, 42% thought that they are changing evenly with other cities, and 49% thought they are lagging behind other cities. In fact, U.S. Census Data shows that the median value of owner-occupied dwelling units in Boston rose in the period 1960-1970, bringing Boston's rank in this measure from tenth to fifth among the twenty largest cities (after San Francisco, Los Angeles, Chicago, and New Orleans) [57, Table 17] Boston's prospectus pointed out the increase. [8, p. 35] This fact appears more remarkable when viewed in light of Muller's finding, using Census data, that the average value of a single-family home increased by 48% between 1966 and 1971 in thirteen cities with increasing population and by only 27% in fourteen cities with decreasing population -- including Boston in the latter average. [32, p. 70] Information for investors, written in a more aggressive style, might have pointed out this paradox and attempted to explain it.

A planning document, of limited distribution, had this to say in 1975 about retail trade in Boston:

> "Retail trade has lagged behind the overall revival and growth in the city's economy over the past decade. While retail sales in the Boston metropolitan area have been expanding continuously since World War II, sales in the City of Boston have barely held their early postwar level, reaching a low point in the early 1960's and recovering only modestly since then. Retail sales in downtown Boston faired even poorer, but appear to have stabilized while gains in the neighborhoods have been modest. These trends reflect the shift in population to the suburbs and the development of shopping centers in the 1950's and 1960's. In recent years, growth in Downtown employment and residential population has counterbalanced the losses to the suburban market and resulted in a stabilization of sales in Downtown." [6, pp. 15 and 16]

This situation shows in a variety of statistics related to retail trade in Boston, such as trends of volumes of sales and retail employment or a list published by the Census of Retail Trade ranking 250 cities. /‾59, Table 7_/ Boston does not report in its prospectus to the securities market the situation of retail trade. Because the City does not have a retail sales tax, it is not and probably will not be obligated to report the volume of retail trade to bond buyers. This is another example of an indicator of the local economy that a city may report when it is to its advantage to do so. Albany, for instance, included in its prospectus survey data from Sales Management Magazine showing a striking increase in sales in the City in recent years. /‾7, p. 18_/ As mentioned earlier, the average survey projections over five years of the "economic well-being of major retail business" in the City of Boston fell between "current" and "less than". (Perceptions Survey) If City statisticians and economists felt they could build a reasonable case that the future of retail sales in Boston will improve, then ways to change and improve these investor perceptions could be explored.

As mentioned earlier, 55% of bond dealers responding to the Perceptions Survey thought the "population trends in Boston" are one of "significant out-migration to suburbs of Boston" and 22% thought that the population trends are one of "significant out-migration to other areas than the Boston area" (The respondent could have checked both answers). In fact, between 1950 and 1970 the population of Boston decreased by 21%. However, Massachusetts State Census data is contradictory showing a population increase of 21% in the period 1970-1975. /‾8, p. 32_/ Survey respondents might have formed their impressions on the basis of trends until 1970, from the most recent U.S. Census data, or from news coverage of some sort. Only 9% of the respondents to that question thought that there are stable population levels and only 1% thought that there is significant in-migration. Were these respondents aware of the contradictory data (which were included in the prospectus statements)?

The discrepancy in these data may possibly make a difference to an investor who knows of and takes the Muller findings very seriously. Muller's handling of the data is very convincing as he uses it to support his hypothesis that a decrease in population is causal, syptomatic, or in other ways correlated with a variety of economic and fiscal problems. After reading his paper, if someone has to decide between five or ten bond issues, it may seem very reasonable to eliminate those cities with decreasing population trends from further consideration.

In response to the question on the Perceptions Survey about population trends that was most recently mentioned, 18% checked that their perceptions are of "stable population levels, but significantly changing population composition" in Boston. In fact, the population composition has changed. Police department data indicated that between 1970 and 1972, there was a large increase in people between ages 25 and 34 and a decrease in people between ages 35 and 64. [6, Table II-1] U.S. Census data for Boston show that from 1950 to 1970 the population or unrelated individuals increased by about 8% while that of families decreased by the same. These results can also be considered in light of changes in the City's residential neighborhoods and schools.

Other population composition data may be considered relevant in light of results of some cities. Muller, for instance, also found that in the thirteen large cities showing population increases, 19% of the population is black; while in the fourteen large cities showing population decreases, more than 30% of the population is black. [32, p. 36] As mentioned earlier, one statistical study found that the most important characteristic of fiscal strain is the percentage of the population that is of Irish descent. [10, p. iii] Boston, and most other municipalities reviewed by this author, did not report any data on racial or ethnic composition. Such a reporting policy might draw criticism for a number of reasons.

Population composition and other social factors may or may not be important to a bond's security or intrinsic quality. However, the possibility of various American cities deteriorating is very unappealing. As mentioned earlier, the Perceptions Survey also asked the bond dealers how they would project the future in five years of "overall population levels" in the City of Boston, and the average of their responses was below "current" levels. A few months after those surveys were distributed, a Boston paper carried on the front page the results of a survey in Massachusetts about trends of Boston's population. Five hundred people were asked:

> "Some people say that during the next five to ten years most of the middle income families will move out of Boston, leaving the City with a mainly low-income population and even more serious problems in schools, housing, and lack of tax revenues. In your opinion, do you think this will definitely happen, probably happen, probably not happen, or definitely not happen?" [5, p. 1]

Of those questioned in Boston, 69% said that they thought that scenario definitely or probably will happen. Citizens and bond dealers, after all, are people who act of the basis of their opinions -- which may be well-considered or without factual basis.

Chart VI-3

Disclosure Recommendations for Nonfinancial Information

Recommending Report	General Description	Type of Government	Description of Industries	Names of Major taxpayers	Names of Major Employers	Population	School Census
1951 New York City Report	If special charter	Yes	Ambiguous	Ambiguous	Ambiguous	Yes	Yes
1963 IBA Format	No	Yes	Yes	Tentative	No	No	Yes
1965 State Technical Assistance Report	Yes	Yes	Yes	Tentative	No	Yes	Tentative
1976 MFOA Disclosure Guidelines	Yes	Yes	Tentative	Yes	No	Yes	Tentative
1976 Williams-Tower Bill	If required by the SEC	Yes	If required by the SEC	Yes	If required by the SEC	If required by the SEC	If required by the SEC

D. Disclosure of nonfinancial information

Although the Indicator Survey and the Perceptions Survey were answered by different people, the responding pools were almost identical having been chosen alternately from the same mailing list. Respondents to the Indicator Survey generally did not consider the types of information included in the Perceptions Survey to be important -- at least not in comparison with financial information. Respondents to the Indicator Survey were asked to rank the following items in importance in evaluating a city's credit worthiness:

Type of Information:	Count of Markings as Most Important	Count of Markings as Second in Importance
Analysis of debt and revenue structures:	144	14
Analysis of expenditures:	36	81
Analysis of economic trends:	27	51
Analysis of demographic trends:	10	20
Statement of bond counsel:	8	7

About half of the 74 indicators that respondents to the Indicator Survey were asked to rate in importance and in the usefulness of comparative data were related to the local economy and social factors. These were generally rated much lower than financial factors. The most important nonfinancial factors not including those describing the property tax base were "median household income" (14th out of 74), "unemployment rate" (19th out of 74) and "total population" (22nd out of 74). Some of the factors that Moak said are important were not ranked highly in this survey by the bond dealers. These include: "commuting trends" (63rd out of 74), "commercial bank deposits"

(37th out of 74), "educational level of population" (43rd out of 74), "population by age group" (60th out of 74), "average value of building permits" (33rd out of 74), and "trends in retail trade" (45th out of 74). Despite the fact that they say that nonfinancial information is not very important, it could be that such data predetermines their opinions and allows them to make only a superficial attempt to understand the financial factors.

A city's economy is much larger and more dynamic than the finances of its government. The interaction of the economy, social factors, and political factors with the finances of local government (as facilities and services are needed and revenues are generated), and with each other, is much more complicated than the details of debt, revenues, and expenditures discussed. Rabinowitz wrote that "a thorough job of credit analysis will cover the same topics that should be considered by local officials in determining debt policy for their governmental unit" [48, p. 137], but analysis such as Moak discussed would go far beyond the capabilities of most analysts and local officials.

The amount of information needed to describe the local economy and social factors is much larger than that needed to descrbie local government finances. Roderick M. Hills, Chairman, Securities and Exchange Commission, said that without mandatory disclosure requirements...

> "there will be a certain competition for disclosure, that around the country various underwriters, various rating services will seek to promote more and more kinds of disclosure, a kind of competition that will not necessarily aid the issuers, a kind of competition that is not necessary for the protection of investors." [63, p. 19]

The average length of prospectus statements of thirty large cities is 44 pages -- that of Philadelphia is 165 pages. (Survey of Financial Officers, See Appendix III) However, a detailed explanation of the local economy and social factors could easily run hundreds of pages for that alone.

The best information with which to analyze many factors of the local economy and social characteristics is currently unavailable. Substitute data, such as statistics collected for a metropolitan region by the U.S. Census or indicators that are substituted for intangible characteristics may be used. Some information is collected by some city and state agencies, but their technique and timing differences make it difficult to use their data for comparisons between cities. If much broader and standardized data collection were begun immediately, it would be years before the data could be meaningfully evaluated as to trends and its collections and anlysis would be expensive. Political conflicts would inevitably arise.

Although the disclosure guidelines cited throughout this thesis were generally specific as to which financial information should be reported, they are very general about reporting of nonfinancial information. All of the guidelines suggest that a general description of the community be given with the precise information involved to be judged by the issuer. The 1965 State Technical Assistance Report lists of great deal of information that is sometimes (or could be) reported but stops short of making decisive recommendations. (See Appendix IV)

Is it reasonable for the city administration to decide to put the city's economy in the most favorable light? For instance, in 1975 only four out of 174 issuers included data on the level or rate of unemployment. (Summary of Reporting Practices) [63, p. 271] Those municipalities probably had very low rates of unemployment. If a city has an unemployment rate that is several percentage points above the national average, will this affect the risk of its securities? Do the potential bond buyers have a right to this information? Does the city have the obligation to inform them?

The 1976 MFOA Disclosure Guidelines suggest, under "description of issuer":

> "Investors should be informed of factors which indicate the ability of the issuer to impose and collect, and the ability of the citizens' to pay, taxes and other receipts which can be used to discharge the issuer's obligations. Certain trends provide useful indications in these regards. Factors which may have a significant, though, indirect effect on these trends, such as types and levels of services provided by the issuer and demand for services, may also be helpful." [33, pp. 10 and 11]

Who is going to decide if such a condition has been adequately met? If disclosure continues to be pressured onto cities, but nominally voluntary, for the purpose of limiting the liability of participants in the securities offerings, then it may seem safer to underwriters to report on all poor points of the city's economy. If disclosure requirements are mandated by federal legislation and set by Congress or by an appointed board, what standards will they use to define what types of background information should be disclosed?

In 1968, Rabinowitz noted that:

> "The more one considers the rating problems, the more one realizes how intimately connected it is with our inability to date as a nation to come to grips with the 'urban problem' or to define adequately a 'good city'." [48, p. 89]

Whether information is given directly to the market or filtered through rating services, there is no reason to believe that a panel of experts appointed in 1977 could better define what areas of the local economy and population characteristics relate most to bond quality any better than experts who considered this problem in the past. Supposing the most important factor is the percentage of the population which is of Irish descent...Will this important fact never become clear because the idea of reporting this statistic seems ridiculous to a panel of experts in 1977? Will local governments take a special poll to find out what their ethnic-Irish population is? Will the few financially secure communities that have large Irish populations be unfairly forced to bear high inerest costs for capital improvements that are debt-financed?

E. <u>Summary and Conclusions</u>

Investors have mixed opinions of Boston, and probably of many other ities, that are not as good as the cities would like. Many of the respondents to the Perceptions Survey are misinformed or uninformed. What can Boston, or other such cities, do to improve their reputations? The disclosure recommendations cited provide little help in this respect. The results of the Indicator Survey and the advice of Lennox Moak contradict in the areas of reporting on subjects such as included in the Perceptions Survey.

There is also a dilemna in development of general disclosure policies for nonfinancial information. Research on how local economic and social factors affect local government finance is just beginning. As it stands, the research can shed little light on which economic and social factors should be considered in municipal credit analysis although it is clear that not everything can be considered because of research and reporting time and costs. Also, over-use of preliminary research may result in inequities for some local communities.

VII. Conclusions and Policy Recommendations

The history of the marketing of municipal securities, as described in Chapter II, shows how the market became reliant on the rating agencies to differentiate categories of securities in a way that is much more rigid than the competing analyses common in the marketing of corporate securities. Municipalities have supported this dependency by resisting federal regulation of municipal securities and by, until recently, maintaining policies of non-disclosure. A number of reasons had been advanced in favor of municipal disclosure policies including: to improve particular cities' reputations, to lessen market dependence on the ratings, to provide opportunity for competition in analysis and rating services, to be a safety check on municipal expenditures and borrowing through investors' reactions, and to provide opportunities for new inputs into municipal finance. However, the potential costs combined with lack of pressure from market participants and lack of initiative to inhibit development of disclosure policies.

Some of those recommending municipal disclosure developed guidelines and specific recommendations. Those cited in this thesis -- the 1951 New York City Report, the 1963 IBA Format, the 1965 State Technical Assistance Report, the 1976 MFOA Disclosure Guidelines, and the 1976 Williams-Tower Bill emphasized reporting information about debt structures and property tax revenues. The results of the Indicator Survey supported the validity of many of their recommendations but also showed that they are incomplete and inconsistent in many ways with investors needs for information.

In several situations arising in the 1970's (the discovery of large unfunded pension liabilities, the UDC default, the NYC default, and other municipal financial problems), it seemed that investors had been uninformed or misinformed and it became apparent that the rating agencies could not satisfactorily pre-identify high risk bonds. A series of federal suits involving principles of securities fraud had an adverse affect on the securities market. As an informal condition of purchase, long prospectus statements were demanded from most municipal issuers. Although they were hastily prepared and of inconsistent quality, they appeared to help to limit the liability of other market participants. Mandatory disclosure standards, primarily the 1976 Williams-Tower Bill before the U.S. Senate, were advanced as a way to facilitate national marketing of municipal securities and to limit competition between municipalities for greater disclosure.

None of the disclosure guidelines before or during the 1970's dealt specifically with the questions of costs to the municipality. These potential costs are the costs of compliance, economic costs, and political costs. The costs of compliance are those of gathering information, those of auditing beyond "normal" requirements, those of writing of the statement and contributing reports, and those of distribution. The economic costs include any damages awarded because of inaccuracies in the disclosure material, incidental suits that use the disclosure material as evidence, and possibly, increased interest costs for some cities because their relative positions in the quality spectrum may drop and the range of the spectrum expressed in interest rates may increase. Resulting political changes may be advantageous or detrimental and may include increased external pressures changing and standardizing reliance on tax sources, relations with state governments, collection of delinquent taxes, accounting practices, and contracts given to city employees, and pressures limiting services and new capital construction.

Whether disclosure is voluntary or mandatory, which information is suggested or required, and the extent of municipal liability are policies that will be formed in the money markets, Congress, and the courts through the interactions of many interest groups. Each city must make policy choices. On the one hand, it could disclose only the minimum necessary by law or to gain acceptance by the market. On the other hand, it could disclose more -- assuming that this will cause enough improvement in its relative market position to more than pay for the costs of the added reporting. Each city must weigh the costs against the benefits of disclosure. The federal government should weigh the disclosure costs of cities against the benefits to investors and securities professionals.

How and where may the costs to municipalities of disclosure policies be limited? If their liability is limited, savings may be considerable. Other ways, beside damage awards, may be found that might help to resolve situations in which the information in the prospectus turned out to be inaccurate or incomplete. If the error does not result in losses to investors and there is not evidence of "scienter", for instance, a requirement that the city publicize the correction would emphasize to all the importance of extreme care in statement preparation. If there is evidence of "scienter" or negligence in statement preparation and investors suffer losses, there should be someway to compensate them. Unfortunately, this would punish another group of innocents -- the taxpayers, who are often less able to bear the burden of higher taxes than securities holders can bear market losses. Obviously, the best approach is a preventative one in which the figures and wording would be carefully reviewed by independent professionals. However, policies should be developed so that this concern does not eliminate possibilities of aggresive marketing or provide a disincentive to broad disclosure (by increasing the expenses of reporting unrequired information).

In addition to damage costs, other compliance costs may be limited. The easiest ways to do so would be to charge for reports and to not include details that require special surveys or special auditing. Another way to limit compliance costs seems to be more compatible with other findings of the surveys. This is to use a tier system of reporting in which large mailing lists might receive very short statements noting that more detail is available on various subjects by request or through investor news services.

It is not clear how disclosure policies will affect the interest spread correlated with the quality spectrum of municipal securities. Often, comparisons of financial data of two cities show striking differences and this perception might increase the difference of the interest rates at which they are able to successfully market their securities. On the other hand, if disclosure policies encourage a greater variety of analysis techniques resulting in different perceptions of preference and quality, then many cities paying relatively high interest rates may find themselves in a more competitive position.

The political costs of disclosure may be the most difficult to predict. It is understandable that municipalities would resist any reporting policies that might undermine the powers of local political structures to determine internal policies. Certain information, such as procedures in collecting delinquent taxes or unfinalized plans for as yet unauthorized bond issues, is more politically sensitive. This should be considered when disclosure policies are developed.

How much more information do independent and institutinally-employed municiapl securities analysts want? How would detailed, standardized, delivered or detailed, unstandardized information affect their work? In 1968, Rabinowitz, a bond analyst, wrote:

> "In some cases the sheer mass of relevant data available, especially for major states and cities and their related governmental entities, requires a greater expenditure of research talent than the analyst's employer has made available to him." /_48, p. 138_/

He further speculated about how the state-of-the-art of municipal credit analysis might change:

> "The municipal credit analysts who work for the major underwriters and investing institutions... are faced with a number of operational problems for which there seeems to be no solutions at the present time, given the lack of substantive research about the nature of local development.
>
> Over the coming years the art of credit analysis is surely going to be improved by the application of a more scientific approach to the subject, most likely within the university research community using data collected by the states.
>
> We can predict that the bond analyst of the future will find himself immersed in the writing of these urban economists and regional scientists, for they are building new foundations for municipal fiscal policy.
>
> We may expect the conservative investor to put aside some of his rules of thumb and to grapple with the more sophisticated intuitions that his credit analysts will provide.
>
> Although the municipal bond analysts are generally concerned with the aggregate local public economy of "the problem of the cities," they are much more concerned with the qualitative measurement of individual governmental units, with the precepts under which they are governed, with the interactions, and with the response of the capital markets to their invitations for bids on issues of long-term bonds." /_48, pp. 138-145_/

Research into municipal finance would be facilitated by the existence of greater collection and standardization of information. However, although many experts have recommended development of a data bank, it has seemed to be too expensive. Rabinowitz suggests that research will be done in universities because:

> "There seems to be less likelihood that sustained research can be expected within the investment community with its divisions among types of competing institutions or within any of the levels of government (partly because of the concept of federalism that gives fiscal independence to local government) or among the many professional and industry-wide associations that serve these various interests". [48, p. 140]

The expense of such research is still a deterent. Recent experiences involving municipal financial crises have increased interest in fiscal strain within the universities, industry, and government so some research may be financed, but it seems doubtful that this research would be extensive enough to substantially affect either municipal financial management or municipal securities analysis unless it is accompanied by other forces such as mandatory municipal disclosure.

Clearly, events have changed the procedures of marketing municipal securities so much that it is vital to develop disclosure policies, now, without waiting for more extensive university studies. As mentioned earlier, 73% of the respondents to the Indicator Survey thought that the municipality with the inferior prospectus sill be forced to pay somewhat or signficantly higher interest rates. In fact, 74% of respondents claimed that the poor quality of information in a prospectus of a municipality has, independent of other inputs, detered them from purchasing a security.

Moak recommends that:

> "From the standpoint of the local government that has bonds in the market, the problem is to provide information on a timely and accurate basis which will enable the analyst and investor to maintain his data bank on the basis of facts and not semi-facts reaching him from secondary sources." [27, p. 271]

It is not at all clear, however, that most bond dealers, investors, and other market participants want the burden of reading, discussing, and responding to all the information that could be reported about cities' financial structures if disclosure costs were not a limiting factor. As mentioned before, in response to a question on the Indicator Survey, 62% of bond dealers claimed they usually spend less than one hour reviewing prospectus statements. They would like even shorter statements -- 86% checked "yes" when asked "Would a short document with notice of a bond sale and key information be useful to you if you also had access to a detailed prospectus?"

The results of the Indicator Survey show that although it is currently impossible to specify how a city or other municipal issuer should be analyzed and graded, types of information of interest to market participants can be defined and ranked by importance. The inability of the rating agencies and writers of pre-1970 disclosure recommendations to recognize the potential problems of pension liabilities shows a need for greater research in municipal finance. The results of the Perceptions Survey show that purchase decisions are sometimes made on the basis of incomplete and inaccurate information.

The President of Standard & Poor's Corporation said:

> "Disclosure must be a living thing and not an annual report that lies in some repository such as a town hall. The disclosure information must flow smoothly into the market place where it can be synthesized and distilled in a variety of ways that will make it palatable for a potential investor to digest. The needs of full disclosure will not be satisfied by producing bigger and bigger official statements and annual reports. The challenge is to develop a procedure through which full disclosure may be accomodated and at the same time sustain and improve market performance." /63, p. 111/

In keeping with the reasonableness of this advice, it may be appropriate to have one set of reports for bond dealers, investors, and the general market, another for analysts, and a third to facilitate research.

A policy limiting the material distributed to the general market is supported by the finding of the Indicator Survey that 56% of respondents will "obtain more information" instead of simply "not buy the bonds" if the sources of information which they usually rely upon still leave them uncertain as to whether to buy a specific issue. Most respondents would go to the underwriter or to the municipality that is issuing the bonds for more information. Several situations have been suggested in preceding chapters in which the city could distribute highly summarized information while making detailed information available to researchers, financial journals, independent rating services, and other interested partices upon request.

This thesis recommends a multi-tier reporting policy. The first tier of information should be widely distributed in official prospectus statements and annual reports. This basic information should consist of a simple description of sources of revenues, costs of services provided, the debt service schedule, a variety of debt-weighting ratios, and unfunded pension liabilities. This information should be based on independent auditor's reports. Because it is so important to compare financial information, serious consideration should be given to standardization of municipal accounting practices. A requirement that statements be prepared using certain accounting techniques might be enough pressure to accomplish this, especially if the federal government provided accounting consultants. Standardized reporting of basic information should help investors to become less dependent on the existing rating agencies.

This thesis recommends that a modified version of the Williams-Tower Bill be passed so that all cities must participate in at least the first of these reporting policies. Some participation from all cities is needed to modify existing procedures and regulation will help to clear up current confusion. As described in previous chapters, some of the requirements for information to be reported that are listed in the 1976 version of the Bill should be changed. Vesting the powers to modify disclosure requirements in a representative board would be preferable to their current definition in Congress. This board should have representatives of cities and other municipalities, market participants, and researchers in municipal finance. This thesis does not recommend that the SEC receive such powers because of the antagonism that has developed between its board and city advocates. It would be more appropriate to expand the administration of the MSRB to include more representatives and vest such powers in it, while developing compatible policies between it and the SEC.

The information that would be given to bond buyers in accordance with a modified version of the Williams-Tower Bill will not be understood by many of them. One article about New York City, for instance, states:

> "The city budget is more than $12 billion. The total assessed valuation of the whole town is only $80 billion. That's like if you were spending $8,000 a year to keep up a $40,000 house -- and one that was antiquated and crowded and kept getting more decrepit the more work you did on it. You'd have to be crazy. With $12 billion per year, in five years you could build a new city for eight million people anywhere you want." /_22, p. 198_/

This shows misunderstandings of the definition of "assessed valuation", what city funds are spent on, and the costs of new construction. Such misunderstandings should be countered public relations campaigns and by trained investment counselors.

More detailed information should be made available to those with the experience and inclination to further analyze it. Moak suggests that individuals are capable and do consider such information when up-to-date data helps by bringing:

> "into focus once again the greatest of all data system coordinators -- the alert, competent, trained, and disciplined human mind." /̲27, p. 170̲/

A representative from a prominent accounting firm says there exists...

> "a buildup of analysis capability within the private sector and in various banks, in various other institutions, who are going to try to pull together all the data." /̲63, p. 107̲/

If such new capabilities really exist, other use of information could be made by new rating services. Small independent consulting firms could register as investment counselors and develop opinion reports on certain issuers. These firms would be aided by broader, multi-tier disclosure policies. They would not have to rate all issuers. They could help investors compensate for their lack of understanding of municipal finances and for their time constraints. The operation of a number of such firms would lessen the dominance of Standard & Poor's Corporation and Moody's Investment Counsellors.

The most intense uses of data might be made by universities that are equiped to do large statistical studies, computer simulations, and in depth case studies. They would not have a vested interest in their conclusions and should nave fewer biases. In particular, studies on a generic "financial framework" and on indicators of financial stress would be helpful. Ideally, there would be an interplay between university research centers, independent and institutional analysts, and a federal municipal securities disclosure regulation board. In this way, the diversity of ideas of the analysts could be investigated by the research organiizations and, as municipal finance becomes more understood, the market can modify its criteria in assigning preferences or other ways can be developed to deal with an equitable acceptance of risk and determination of interest rates.

Cities could pursue active marketing policies that would try to reach investors through improving their perceptions instead of immersing them in financial details. They should try to diagnose their reputations with opinion surveys such as that about Boston. They should try to reach small buyers by mass mailings, luncheon discussions, and paid advertising. They should try to directly solicit suggestions and improve communication with investors by newsletters with question-and-answer columns. To be convincing, the tone of such material will have to be that of one backed up by facts and avoiding language associated with the hard-sell. The cities should coordinate releases from the financial offices with those from the mayor's office. In fact, it may be appropriate to have a small staff devoted to compiling and preparing these and other prospectus and detailed reports. Another effective marketing strategy might be to appoint an advisory board (before a financial crisis) of people who are influential in the securities market and to convince them of the city's financial stability and good management.

A multi-tiered reporting policy, such as this thesis recommends, will require that the cities not have full financial liability for all the information they release. They should be held responsible for the first tier of required information and they should not be allowed to use advertising that is clearly fraudulent. However, they should not be held responsible for the accuracy of all the information they give to researchers. They should be allowed to develop circulars for mass mailing, newspaper advertising, and other releases and print them with a statement cautioning investors that they are based on estimations or unaudited figures and that the city cannot be sued for damages if these statements turn out to be inaccurate.

If all of the cities and other municipal units in the nation made available more information for use as described, the security of all municipal bonds could be improved. If only very limited disclosure becomes the norm, investors may not receive information that is any more useful than what they have had in the past. Very defined standards would not uncover many potential problems or provide a basis for correcting misperceptions. If disclosure is extensive and the liability of cities is not limited and if the market reacts to the increased information by labelling the securities of many cities as speculative, then borrowing costs for cities may be increased to an unacceptable point. It is imperative, then, that some middle ground be found to balance between the two extremes so as to provide adequate information but at costs that are not excessive.

Appendix I

Survey Form and Tabulated Results of

The Indicator Survey

CITY OF BOSTON
OFFICE OF THE TREASURER
CITY HALL, BOSTON

JAMES V. YOUNG
TREASURER

June 23, 1976

Dear Municipal Bond Investor:

Earlier this year we asked you to complete a questionnaire identical to the one attached, to help us discover what information investors would like to get from municipal bond disclosure documents. As we noted then, the Treasury Department of the City of Boston is fortunate to have the assistance of a graduate student team from the Massachusetts Institute of Technology in carrying out this survey and analyzing the results. While we are heartened by the substantial response to our first mailing, we nevertheless would like to enlarge our data base and once again ask for your cooperation and encourage you to complete the questionnaire, not only because we would like to improve Boston's own disclosure information, but also because there is a growing movement toward requiring more extensive disclosure in the municipal bond area and the results of this survey may provide invaluable insight into what disclosure requirements should be.

We would prefer to receive your answers as soon as possible. Thank you for your cooperation.

Sincerely,

James V. Young

James V. Young
Collector-Treasurer
City of Boston

Kent Colton

Kent Colton
Assistant Professor of
Urban Studies and Planning
Massachusetts Institute of Technology

JVY/ja

INVESTOR NEEDS FOR INFORMATION IN MUNICIPAL PROSPECTUS STATEMENTS

Listed below are a number of items of information which a city might include in a prospectus statement. They are grouped into four categories: population and other indicators, financial statistics, economic statistics, and property indicators. Please mark each item with a value from "1" to "5" depending on the importance you feel it has, with "1" being very important and "5" being irrelevent. Check the "don't know" column if you do not feel qualified to give an opinion on the importance of that particular item. If you think that such items of information have significantly more meaning if they are compared to other cities, check "yes" in the column "would like a comparison with other cities". Since we would also like to obtain an idea as to which of these indicators you feel are most important, after each of the four area groupings is a question asking you to indicate which three you feel are most important.

****

	RANKING OF IMPORTANCE	DON'T KNOW	WOULD YOU LIKE A COMPARISON WITH OTHER CITIES? YES	NO
I.) POPULATION AND OTHER CHARACTERISTICS				
1.) Total population:	1 2 3 4 5	____	____	____
2.) Population by age group:	1 2 3 4 5	____	____	____
3.) Migratory trends by economic class:	1 2 3 4 5	____	____	____
4.) Population density:	1 2 3 4 5	____	____	____
5.) Educational level of population:	1 2 3 4 5	____	____	____
6.) Educational level and skill-training of workforce:	1 2 3 4 5	____	____	____
7.) Percentage of city work force living inside the city limits:	1 2 3 4 5	____	____	____
8.) Average commute by city workforce (by time, distance):	1 2 3 4 5	____	____	____
9.) Median household income:	1 2 3 4 5	____	____	____
10.) Percentage change in median household income in last five years:	1 2 3 4 5	____	____	____
11.) Percentage of census tracts with median incomes above city median:	1 2 3 4 5	____	____	____
12.) Crime rates:	1 2 3 4 5	____	____	____
13.) Air-quality readings:	1 2 3 4 5	____	____	____
14.) Racial distributions:	1 2 3 4 5	____	____	____
15.) Employment by the city and other governmental units over the last 5 years:	1 2 3 4 5	____	____	____

Of the fifteen population characteristics listed above, please list the numbers of the three which you think are the most important:

A.)_____ B.)_____ C.)_____

(cont.)

As before, circle "1" to "5" representing importance, with "1" representing very important and "5" representing irrelevent. Also check "yes" if you would like the data to be compared with other cities.

	RANKING OF IMPORTANCE	DON'T KNOW	WOULD YOU LIKE A COMPARISON WITH OTHER CITIES? YES	NO
II.) FINANCIAL STATISTICS				
1.) Total debt outstanding:	1 2 3 4 5	___	___	___
2.) Debt per capita ratio:	1 2 3 4 5	___	___	___
3.) Funded debt outside of legal debt limit:	1 2 3 4 5	___	___	___
4.) Combined debt as a percentage of market value:	1 2 3 4 5	___	___	___
5.) Projected capital expenditures for public facilities:	1 2 3 4 5	___	___	___
6.) Average age of public facilities:	1 2 3 4 5	___	___	___
7.) Total welfare:	1 2 3 4 5	___	___	___
8.) Changes in welfare expenditures in last 5 years:	1 2 3 4 5	___	___	___
9.) Pension liabilities and funding provisions:	1 2 3 4 5	___	___	___
10.) Net indebtedness:	1 2 3 4 5	___	___	___
11.) Total state and federal aid to city and as percentages:	1 2 3 4 5	___	___	___
12.) Summary of revenue sources for 5 years:	1 2 3 4 5	___	___	___
13.) Statement of assets and liabilities over 5 years:	1 2 3 4 5	___	___	___
14.) Growth of revenues by source over 5 years:	1 2 3 4 5	___	___	___
15.) Debt retirement schedule:	1 2 3 4 5	___	___	___
16.) Excesses in operating expenditures over originally approved budgets:	1 2 3 4 5	___	___	___
17.) Number of overlapping jurisdictions with debt issuing capacity:	1 2 3 4 5	___	___	___
18.) Records of tax collections compared to tax accruals:	1 2 3 4 5	___	___	___

Of the eighteen financial characteristics listed above, please list the numbers of the three which you think are most important:

A.)_____ B.)_____ C.)_____

(cont.)

As before, circle "1" to "5" representing importance, with "1" representing "very important" and "5" representing irrelevent. Also check "yes" if you would like the data to be compared with other cities.

	RANKING OF IMPORTANCE	DON'T KNOW	WOULD YOU LIKE A COMPARISON WITH OTHER CITIES? YES	NO
III.) ECONOMIC STATISTICS				
1.) Number of industries by type and dollar value which entered or opened in last 5 years:	1 2 3 4 5	____	____	____
2.) Number of industries by type and dollar value which left or closed in last 5 years:	1 2 3 4 5	____	____	____
3.) Ten largest industries in the city:	1 2 3 4 5	____	____	____
4.) Number of "Fortune 500" firms with representative offices in the city:	1 2 3 4 5	____	____	____
5.) Financial institutions with home offices in the city, by rank, type, size:	1 2 3 4 5	____	____	____
6.) Value of commercial bank deposits:	1 2 3 4 5	____	____	____
7.) Cost of living indicators:	1 2 3 4 5	____	____	____
8.) Number of strikes in city in last 5 years affecting major industries:	1 2 3 4 5	____	____	____
9.) Percentage of work force which is union affiliated:	1 2 3 4 5	____	____	____
10.) Worker productivity:	1 2 3 4 5	____	____	____
11.) Trends in wholesale trade:	1 2 3 4 5	____	____	____
12.) Trends in retail trade:	1 2 3 4 5	____	____	____
13.) Energy costs:	1 2 3 4 5	____	____	____
14.) Commuting trends:	1 2 3 4 5	____	____	____
15.) Air-flight tonnage and traffic:	1 2 3 4 5	____	____	____
16.) Rail tonnage and traffic:	1 2 3 4 5	____	____	____
17.) Shipping tonnage and traffic:	1 2 3 4 5	____	____	____
18.) Truck tonnage and traffic:	1 2 3 4 5	____	____	____
19.) Sector analysis of production:	1 2 3 4 5	____	____	____
20.) Unemployment rate:	1 2 3 4 5	____	____	____
21.) Labor participation rate:	1 2 3 4 5	____	____	____

Of the twenty-one economic characteristics listed above, please list the numbers of the three which you think are the most important:

A.)_____ B.)_____ C.)_____

(cont.)

As before, circle "1" to "5" representing importance, with "1" representing very important and "5" representing irrelevent. Also check "yes" if you would like the data to be compared with other cities.

	RANKING OF IMPORTANCE	DON'T KNOW	WOULD YOU LIKE A COMPARISON WITH OTHER CITIES? YES	NO
IV.) PROPERTY INDICATORS:				
1.) Percentage of land publicly owned:	1 2 3 4 5	____	____	____
2.) Trends in vacancy rates for commerical property:	1 2 3 4 5	____	____	____
3.) Trends in vacancy rates for residential property:	1 2 3 4 5	____	____	____
4.) Average annual absorption rate of commercial office space:	1 2 3 4 5	____	____	____
5.) Assessed taxable valuation of commercial property:	1 2 3 4 5	____	____	____
6.) Assessed taxable valuation of residential property:	1 2 3 4 5	____	____	____
7.) Estimated market value of commercial property:	1 2 3 4 5	____	____	____
8.) Estimated market value of residential property:	1 2 3 4 5	____	____	____
9.) Percentages of properties exempt from taxation by type of property and adjusted assessment:	1 2 3 4 5	____	____	____
10.) Age of residential housing stock:	1 2 3 4 5	____	____	____
11.) Volume of luxury and prestige housing:	1 2 3 4 5	____	____	____
12.) Percentage of rental housing which is owner occupied:	1 2 3 4 5	____	____	____
13.) Volume of rental housing:	1 2 3 4 5	____	____	____
14.) Changes in types of structures used for residential purposes:	1 2 3 4 5	____	____	____
15.) Changes in types of structures used for commercial purposes:	1 2 3 4 5	____	____	____
16.) Average investment in recently rehabilitated dwelling units:	1 2 3 4 5	____	____	____
17.) Average investment in recently rehabilitated office space:	1 2 3 4 5	____	____	____
18.) Average value of building permits by type and volume in last 5 years:	1 2 3 4 5	____	____	____
19.) Map showing locations of property uses:	1 2 3 4 5	____	____	____
20.) Assessment practice information:	1 2 3 4 5	____	____	____

Of the twenty property indicators listed above, please list the numbers of the three which you think are the most important:

A.)_____ B.)_____ C.)_____

(cont.)

The remainder of this survey is devoted to a few questions dealing with information. They are short and self-explanatory.

****

1.) Listed below are seven possible sources of information you may use to evaluate the credit worthiness of a city's specific debt issues. Please rank them in importance with "1" being the most important. If you are unable to decide which of two is more important, mark each item with the same number. (i.e. if both are the second most important items, both would receive a "2".)

____A.) Moody's and Standard & Poor's published bond ratings

____B.) The prospectus statement of the bond issue

____C.) Informal recommendations of colleagues

____D.) Limited circulation reports

____E.) In-house research

____F.) Yields of comparable issues

____G.) Other, please specify: ____________

2.) Listed below are major informational components of a municipal prospectus. Please rank the items in importance in evaluation of a city's credit worthiness with "1" being the most important group. As before, if you are unable to decide which of two is more important, mark each item with the same number.

____A.) Analysis of debt and revenue structures

____B.) Analysis of expenditures

____C.) Analysis of economic trends

____D.) Analysis of demographic tre

____E.) Statement of bond counsel

____F.) Other, please specify: ____________

3.) Has the poor quality of information in a prospectus issue of a municipality, independent of other inputs, ever detered you from purchasing a security? (check one)

____A.) YES ____B.) NO ____C.) UNCERTAIN

4.) If the sources of information which you usually rely upon still leave you uncertain as to whether to buy a specific issue, would you? (check one)

____A.) NOT BUY THE BONDS ____B.) OBTAIN MORE INFORMATION

5.) If you would obtain more information, what source(s) would you go to? (More than one answer may be appropriate. Check all those which apply.)

____A.) The underwriter

____B.) The municipality which is issuing the bonds

____C.) Other, please specify ____________

____D.) I would not bother to look for more information.

6.) Assume that the economic, social and political circumstances of two municipalities are essentially equivalent and that each is issuing a debt offering in the same time period. If the prospectus of one municipality is inferior in information content to that of the other, how do you think this will affect the relative interest rates? (check one)

____A.) The municipality with the inferior prospectus will be forced to pay significantly higher interest rates.

____B.) The municipality with the inferior prospectus will be forced to pay somewhat higher interest rates.

____C.) The difference in prospectus informational quality will not affect interest rates.

____D.) Other, please specify: ____________

7.) How much time do you, your staff and/or your client usually spend reviewing a prospectus? (check one)

____A.) Less than one hour ____B.) Several hours ____C.) More than several hours

Comments on above?

8.) Would a short document with notice of a bond sale and key information be useful to you if you also had access to a detailed prospectus? (check one)

_____A.) YES _____B.) NO _____C.) DON'T KNOW

9.) Regarding the composition of your municipal bond portfolio(s), would you please assign approximate percentages to the following categories: (The total should add to 100%)

_____A.) Holdings from the municipality (city or town) within which I am located.

_____B.) Holdings from other municipalities within my state and of my state itself.

_____C.) Holdings from state and local authorities outside of the state in which I am located.

_____D.) This question is not applicable.

10.) Further regarding the composition of your municipal bond portfolio(s), would you please assign approximate percentages to the following categories: (The total should add to 100%)

_____A.) Bond anticipation notes

_____B.) Tax anticipation notes

_____C.) Other revenue anticipation notes

_____D.) Revenue bonds

_____E.) Moral obligation bonds

_____F.) General obligation bonds of municipalities

_____G.) General obligation bonds of state governments or guaranteed by state governments

_____H.) This question is not applicable.

11.) Leaving aside considerations of yield and risk, are you more reluctant to buy if the issuing municipality is located outside of the region of the country in which you are located? (check one)

_____A.) I am much more reluctant to buy a bond if it is issued from a different area of the country.

_____B.) I am somewhat more reluctant to buy a bond if it is issued from a different area of the country.

_____C.) I am indifferent in deciding to buy a bond that it is issued from a different area of the country.

_____D.) This question is not applicable.

Thank you for the time and thought you have used in answering this survey.

Do you have any general or specific comments relating to any of the issues raised in this survey?

____

____

____

____

____

____

____

____

Table A-I (1)

Importance of Various Types of Information

According to Results of Indicator Survey

Indicator as listed on survey form	Relative Importance Ranking** (out of 74)	Adjusted Mean Importance Ranking*	Category
Total debt outstanding	1/74	1.2	financial
Debt per capita ratio	2/74	1.2	financial
Funded debt outside of legal debt limit	3/74	1.2	financial
Net indebtedness	4/74	1.3	financial
Records of tax collections compared to tax accruals	5/74	1.3	financial
Assessed taxable valuation of commercial property	6/74	1.4	property
Summary of revenues sources for five years	7/74	1.4	financial
Assessed taxable valuation of residential property	8/74	1.4	financial
Debt retirement schedule	9/74	1.4	financial
Excesses in operating expenditures over originally approved budgets	10/74	1.4	financial
Ten largest industries in the city	11/74	1.5	economic
Growth of revenues by source over five years	12/74	1.5	financial
Total state and federal aid to city and as percentages	13/74	1.6	financial
Median household income	14/74	1.6	social
Estimated market value of commercial property	15/74	1.6	property
Estimated market value of residential property	16/74	1.6	property

(cont.)

Table A-I (1) (cont.)

Indicator as listed on survey form	Relative Importance Ranking** (out of 74)	Adjusted Mean Importance Ranking*	Category
Combined debt as a percentage of market value	17/74	1.7	financial
Assessment practice information	18/74	1.7	property
Unemployment rate	19/74	1.7	economic
Projected capital expenditures for public facilities	20/74	1.7	financial
Pension liabilities and funding provisions	21/74	1.7	financial
Total population	22/74	1.7	social
Number of overlapping jurisdictions with debt issuing capacity	23/74	1.8	financial
Statement of assets and liabilities over five years	24/74	1.9	financial
Total welfare	25/74	1.9	financial
Changes in welfare expenditures in last five years	26/74	2.0	financial
Percentages of property exempt from taxation by type of property and adjusted assessment	27/74	2.0	property
Number of industries by type and dollar value that opened or entered in last five years	28/74	2.0	economic
Percentage change in median household income in last five years	29/74	2.1	social
Employment by the city and other governmental units over the last five years	30/74	2.1	social
Number of industries by type and dollar value that left or closed in last five years	31/74	2.1	economic
Trends in vacancy rate for commercial property	32/74	2.2	property

(cont.)

Table A-I (1) (cont.)

Indicator as listed on survey form	Relative Importance Ranking** (out of 74)	Adjusted Mean Importance Ranking**	Category
Average value of building permits by type and volume in last five years	33/74	2.2	property
Trends in vacancy rates for residential property	34/74	2.3	property
Racial distributions	35/74	2.5	social
Cost of living indicators	36/74	2.5	economic
Value of commercial bank deposits	37/74	2.5	economic
Financial institutions with home offices in the city, by rank, type, size	38/74	2.5	economic
Educational level and skilltraining of work force	39/74	2.6	social
Percentage of land publicly owned	40/74	2.6	property
Migratory trends by economic class	41/74	2.6	social
Energy costs	42/74	2.6	economic
Educational level of population	43/74	2.7	social
Average age of public facilities	44/74	2.7	financial
Trends in retail trade	45/74	2.7	economic
Number of strikes in city in last five years affecting major industries	46/74	2.7	economic
Age of residential housing stock	47/74	2.8	property
Labor participation rate	48/74	2.8	economic
Percentage of city work force living inside city limits	49/74	2.8	social
Average annual absorption rate of commercial office space	50/74	2.8	property
Trends in wholesale trade	51/74	2.8	economic
Educational level of population	52/74	2.8	social

(cont.)

Table A-I (1) (cont.)

Indicator as listed on survey form	Relative Importance Ranking** (out of 74)	Adjusted Mean Importance Ranking*	Category
Percentage of work force that is union affilitate	53/74	2.8	economic
Worker productivity	54/74	2.9	economic
Crime rates	55/74	2.9	social
Volume of luxury and prestige housing	56/74	3.0	property
Number of "Fortune 500" firms with representative offices in the city	57/74	3.0	economic
Percentage of rental housing that is owner occupied	58/74	3.0	property
Volume of rental housing	59/74	3.0	property
Population by age group	60/74	3.1	social
Percentage of census tracts with median incomes above city median	61/74	3.1	social
Sector analysis or production	62/74	3.3	economic
Commuting trends	63/74	3.3	economic
Average investment in recently rehabilitated dwelling units	66/74	3.4	property
Shipping tonnage and traffic	65/74	3.4	economic
Average investment in recently rehabilitated office space	66/74	3.4	property
Rail tonnage and traffic	67/74	3.4	economic
Map showing location of property uses	68/74	3.4	property
Truck tonnage and traffic	69/74	3.4	economic
Air-flight tonnage and traffic	70/74	3.4	economic
Changes in types of construction used for commercial purposes	71/74	3.4	property
Changes in types of construction used for residential purposes	72/74	3.5	property

(cont.)

Table A-I (1)(cont.)

Indicator as listed on survey form	Relative Importance Ranking** (out of 74)	Adjusted Mean Importance Ranking*	Category
Air-quality readings	73/74	3.8	social
Average commute by city work force	74/74	3.9	social

* The Adjusted Mean Importance Rankings were computed using the survey results of questions in which the respondents marked "1", "2", "3", "4", or "5" for the importance of each indicator with "1" representing "very important" and "5" representing "irrelevent". The mean was computed by averaging these values, excluding "don't know" responses, and rounded off to two significant digits.

** The Relative Importance Rankings were computed by ranking all seventy-four indicators by their adjusted mean importance rankings using those values in four significant figures.

Table A-I (2)

Information for which Comparisons with other Cities are Most Desired According to Results of Indicator Survey

	Indicator as listed on survey form	Proportion of Respondents Desiring Comparison (%)
(1)	Median household income*	80
(2)	Debt per capita ratio*	80
(3)	Unemployment rate*	70
(4)	Total debt outstanding*	67
(5)	Net indebtedness*	68
(6)	Total welfare	66
(7)	Cost of living indicators	65
(8)	Total state and federal aid to the city and as percentages	65
(9)	Combined debt as a percentage of market value	64
(10)	Pension liabilities and funding provisions	62
(11)	Employment by the city and other governmental units over the last five years	58
(12)	Records of tax collections compared to tax accruals*	58
(13)	Funded debt outside of legal debt limit*	56
(14)	Crime rates	56
(15)	Changes in welfare expenditures in the last five years	55
(16)	Trends in vacancy rates for commercial property	54
(17)	Educational level of population	54
(18)	Energy costs	54
(19)	Total population	54
(20)	Percentage of property exempt from taxation by type of property and adjusted assessment	52

(cont.)

Table A-I (2) (cont.)

Indicator as listed on survey form

Indicator as listed on survey form	Proportion of Respondents Desiring Comparisons (%)
(21) Assessed taxabke valuation of commercial property*	52
(22) Population by age group	51
(23) Assessed taxable valuation of residential property*	51
(24) Educational level and skill-training of work force	51
(25) Trends in vacancy rate for residential property	50

* Was also rated as one of the twenty-four most important indicators out of the seventy-four indicators on the survey form

Table A-I (3)

Comparisons of Indicator Survey Results of Relative Importance Rankings and Frequencies of Mentions as Among Most Important Social Information

Relative Importance Ranking* (out of 15)	Indicator as listed on survey form	Relative Frequency of Mentions** (out of 15)	Indicator as listed on survey form
1/15	Median household income	1/15	Median household income
2/15	Total population	2/15	Total population
3/15	Percentage change in median household income in last five years	3/15	Percentage change in median household income in last five years
4/15	Employment by the city and other governmental units over the last five years	4/15	Employment by the city and other governmental units over the last five years
5/15	Racial distributions	5/15	Migratory trends by economic class
6/15	Educational level and skilltraining of the work force	6/15	Racial distributions
7/15	Migratory trends by economic class	7/15	Educational level and skilltraining of the work force
8/15	Educational level of the population	8/15	Educational level of the population
9/15	Percentage of city work force living inside city limits	9/15	Population by age group
10/15	Population density	10/15	Percentage of city work force living inside city limits

(cont.)

Table A-I (3) (cont.)

Relative Importance Ranking* (out of 15)	Indicator as listed on survey form	Relative Frequency of Mentions** (out of 15)	Indicator as listed on survey form
11/15	Crime rates	11/15	Crime rates
12/15	Population by age group	12/15	Population density
13/15	Air-quality readings	13 and 14/15	Air-quality readings
14/15	Average commute by city work force		Percentage of census tracts with median income above city average
15/15	Percentage of census tracts with median income above city average	15/15	Average commute by city work force

* The Relative Importance Rankings were computed by ranking the indicators by their adjusted mean importance ratings in each section of the survey.

** The Relative Frequencies of Mentions were computed by dividing the number of respondents who listed each indicator as one of the three most important indicators in each of the four sections of the survey by the number of respondents who had answered the question that asked them to rate the importance of that indicator.

Table A-I (4)

Importance Ratings of Social Information According to Results of Indicator Survey

	Indicator as listed on survey form	Number of Answers[1]	Adjusted Mean Importance Rating[2]	Standard Deviation Importance Rating[3]	Number Mentions as Most Important[4]	Adjusted Frequency Mentions as Most Important[5]
(1)	Total population	169	1.7	1.07	96	.49
(2)	Population by age group	167	3.1	1.23	23	.14
(3)	Migratory trends by economic class	165	2.6	1.41	43	.26
(4)	Population density	164	2.8	1.21	15	.09
(5)	Educational level of population	168	2.7	1.22	27	.16
(6)	Educational level and skilltraining of work force	168	2.6	1.20	33	.20
(7)	Percentage of city work force living inside city limits	168	2.8	1.28	20	.12
(8)	Average commute by city work force	166	3.9	1.03	0	0
(9)	Median household income	168	1.6	.79	104	.62
(10)	Percentage change in median household income in last five years	168	2.1	1.10	66	.39
(11)	Percentage of census tracts with median incomes above city median	165	3.1	1.27	4	.02
(12)	Crime rates	168	2.9	1.29	17	.10

(cont.)

Table A-I (4) (cont.)

	Indicator as listed on survey form	Number of Answers[1]	Adjusted Mean Importance Rating[2]	Standard Deviation Importance Rating[3]	Number Mentions as Most Important[4]	Adjusted Frequency Mentions as Most Important[5]
(13)	Air-quality readings	168	3.8	1.17	4	.02
(14)	Racial distributions	73	2.5	1.26	16	.22
(15)	Employment by the city and other governmental units over the last five years	72	2.1	1.15	22	.31

1 When asked to rate the indicator's importance on a 1-5 scale

2 Excludes "Don't Know" responses and uses a gradient from "1"="most important" to "5"="irrelevent"

3 Computed using the adjusted mean importance rating and the frequencies of each response from "1" to "5" representing importance

4 In response to a question at the end of the social indicators section asking which three of the fifteen population and other indicators are the most important

5 Number of mentions as one of the three most important divided by the number of answers to the question asking respondents to rate the importance of that indicator

Table A-I (5)

Indicator Survey Results on the Desirability of Comparing Social and other Characteristics with other Cities

Indicator as listed on survey form	Number of Answers	/ Count / YES	NO	/ Frequency / YES(%)	NO(%)
(1) Total population	108	58	50	54	46
(2) Population by age group	105	54	51	51	49
(3) Migratory trends by economic class	99	45	54	45	55
(4) Population density	96	46	50	48	52
(5) Eductional level of population	105	57	48	54	46
(6) Educational level and skill-training of work force	101	51	50	51	50
(7) Percentage of city work force living inside city limits	102	50	52	49	51
(8) Average commute by city work force	88	18	70	20	80
(9) Median household income	119	95	24	80	20
(10) Percentage change in median household income in last five years	113	75	38	66	34
(11) Percentage of census tracts with median incomes above city median	86	31	55	36	64
(12) Crime rates	99	55	44	56	44
(13) Air-quality readings	96	34	62	35	65

(cont.)

Table A-I (5) (cont.)

Indicator as listed on survey form	Number of Answers	Count		Frequency	
		YES	NO	YES(%)	NO(%)
(14) Racial distributions*	44	21	23	48	52
(15) Employment by the city an other governmental units over the last five years*	48	28	20	58	42

* Listed on the survey form on only the second mailing

Table A-I (6)

Comparisons of Indicator Survey Results of Relative Importance Rankings

and Frequencies of Mentions as Among Most Important Financial Information

Relative Importance Ranking* (out of 18)	Indicator as listed on survey form	Relative Frequency of Mentions** (out of 18)	Indicator as listed on survey form
1/18	Total debt outstanding	1/18	Total debt outstanding
2/18	Debt per capita ratio	2 and 3/18	Debt per capita ratio
3/18	Funded debt outside of legal debt limit		Net indebtedness
4/18	Net indebtedness	4,5, and 6/18	Combined debt as a percentage of market value
5/18	Records of tax collections compared to tax accruals		Summary of revenue sources over five years
6/18	Summary of revenue sources over five years		Excesses in operating expenditures over originally approved budgets
7/18	Debt retirement schedule	7/18	Number of overlapping jurisdictions with debt-issuing capacity
8/18	Excesses in operating expenditures over originally approved budgets	8,9,10, and 11/18	Records of tax collections compared to tax accruals
9/18	Growth of revenues by source over five years		Debt retirement schedule
10/18	Total state and federal aid to the city and as percentages		Funded debt outside of legal debt limit

(cont.)

Table A-I (6) (cont.)

Relative Importance Ranking* (out of 18)	Indicator as listed on survey form	Relative Frequency of Mentions** (out of 18)	Indicator as listed on survey form
11/18	Combined debt as a percentage of market value	11/18	Pension liabilities and funding provisions
12/18	Projected capital expenditures for public facilities	12/18	Growth of revenues by source over five years
13/18	Pension liabilities and funding provisions	13/18	Statement of assets and liabilities over five years
14/18	Number of overlapping jurisdictions with debt issuing capacity	14/18	Total state and federal aid to the city and as percentages
15/18	Statement of assets and liabilities over five years	15/18	Projected capital expenditures for public facilities
16/18	Total welfare	16/18	Total welfare
17/18	Changes in welfare expenditures in last five years	17/18	Changes in welfare expenditures in last five years
18/18	Average age of public facilities	18/18	Average age of public facilities

* The Relative Importance Rankings were computed by ranking the indicators by their adjusted mean importance ratings in each section of the survey.

** The Relative Frequencies of Mentions were computed by dividing the number of respondents who listed each indicator as one of the three most important indicators of each of the four sections of the survey by the number of respondents who had answered the question that asked them to rate the importance of that indicator.

Table A-I (7)

Importance Ratings of Financial Information According to Results of Indicator Survey

	Indicator as listed on survey form	Number of Answers[1]	Adjusted Mean Importance Rating[2]	Standard Deviation Importance Rating[3]	Number Mentions as Most Important[4]	Adjusted Frequency Mentions as Most Important[5]
(1)	Total debt outstanding	166	1.2	.52	86	.52
(2)	Debt per capita ratio	167	1.2	.51	42	.25
(3)	Funded debt outside of legal debt limit	165	1.3	.56	24	.15
(4)	Combined debt as a percentage of market value	167	1.7	1.04	34	.20
(5)	Projected capital expenditures for public facilities	167	1.7	.78	14	.08
(6)	Average age of public facilities	166	2.7	.98	4	.02
(7)	Total welfare	165	2.0	1.03	8	.05
(8)	Change in welfare expenditures in last five years	164	2.0	1.11	6	.04
(9)	Pension liabilities and funding provisions	166	1.7	.92	24	.14
(10)	Net indebtedness	166	1.3	.65	42	.25
(11)	Total state and federal aid to city and as percentages	165	1.6	.74	14	.08
(12)	Summary of revenue sources for five years	166	1.4	.67	33	.20

(cpnt.)

Table A-I (7) (cont.)

	Indicator as listed on survey form	Number of Answers[1]	Adjusted Mean Importance Rating[2]	Standard Deviation Importance Rating[3]	Number Mentions as Most Important[4]	Adjusted Frequency Mentions as Most Important[5]
(13)	Statement of assets and liabilities over five years	166	1.9	1.06	17	.10
(14)	Growth of revenues by source over five years	166	1.5	.68	19	.11
(15)	Debt retirement schedule	166	1.4	.64	25	.15
(16)	Excesses in operating expenditures over originally approved budgets	167	1.4	.67	33	.20
(17)	Numbers of overlapping jurisdictions with debt issuing capacity	166	1.8	1.01	10	.16
(18)	Records of tax collections compared to tax accruals	77	1.3	.57	20	.15

[1] When asked to rate the indicator's importance on a 1-5 scale

[2] Excludes "Don't Know" responses and uses a gradient from "1"="most important" to "5"="irrelevent"

[3] Computed using the adjusted mean importance rating and the frequencies of each response from "1" to "5" representing importance

[4] In response to a question at the end of the financial indicators section asking which three of the eighteen financial indicators are the most important

[5] Number of mentions as one of the three most important divided by the number of answers to the question asking respondents to rate the importance of that indicator

Table A=I (8)

Indicator Survey Results on the Desirability of Comparing Financial Indicators with other Cities

	Indicator as listed on survey form	Number of Answers	Count YES	Count NO	Frequency YES(%)	Frequency NO(%)
(1)	Total debt outstanding	98	66	32	67	33
(2)	Debt per capita ratio	112	89	23	80	21
(3)	Funded debt outside of legal debt limit	91	51	40	56	44
(4)	Combined debt as a percentage of market value	98	63	35	64	36
(5)	Projected capital expenditures for public relations	86	33	53	39	62
(6)	Average age of public facilties	82	26	56	32	68
(7)	Total welfare	96	63	33	66	34
(8)	Changes in welfare expenditures in last five years	92	51	41	55	45
(9)	Pension liabilities and funding provisions	96	59	37	62	39
(10)	Net indebtedness	98	67	31	68	32
(11)	Total state and federal aid to city and as percentages	101	66	35	65	35
(12)	Summary of revenue sources for five years	88	42	46	48	52
(13)	Statement of assets and liabilities over five years	87	31	56	36	64

(cont.)

Table A-I (8) (cont.)

Indicator as listed on survey form	Number of Answers	Count YES	Count NO	Frequency YES(%)	Frequency NO(%)
(14) Growth of revenues by source over five years	89	40	49	45	55
(15) Debt retirement schedule	86	38	48	44	56
(16) Excesses in operating expenditures over originally approved budgets	85	33	52	39	61
(17) Number of overlapping jurisdictions with debt issuing capacity	81	26	55	32	78
(18) Records of tax collections compared to tax accruals *	45	26	19	58	42

* Listed on the survey form on only the second mailing

Table A-I (9)

Comparisons of Indicator Survey Results of Relative Importance Rankings and Frequencies of Mentions as Among Most Important Economic Information

Relative Importance Ranking* (out of 21)	Indicator as listed on survey form	Relative Frequency of Mentions** (out of 21)	Indicator as listed on survey form
1/21	Ten largest industries in the city	1/21	Ten largest industries in the city
2/21	Unemployment rate	2/21	Unemployment rate
3/21	Number of industries by type and dollar value that opened or entered in last five years	3/21	Number of industries by type and dollar value that opened or entered in last five years
4/21	Number of industries by type and dollar value that left or closed in last five years	4/21	Number of industries by type and dollar value that left or closed in last five years
5/21	Cost of living indicators	5/21	Cost of living indicators
6/21	Value of commercial bank deposits	6/21	Value of commercial bank deposits
7/21	Financial institutions with home offices in the city, by rank, type, size	7/21	Financial institutions with home offices in the city, by rank, type, size
8/21	Energy costs	8/21	Worker productivity
9/21	Trends in retail trade	9/21	Number of strikes in city in last five years affecting major industries

(cont.)

Table A-I (9) (cont.)

Relative Importance Ranking* (out of 21)	Indicator as listed on survey form	Relative Frequency of Mentions** (out of 21)	Indicator as listed on survey form
10/21	Number of strikes in last five years affecting major industries	10 and 11/21	Energy costs
11/21	Labor participation rate		Number of "Fortune 500" firms with representative offices in the city
12/21	Trends in wholesale trade	12/21	Percentage of work force that is union affiliated
13/21	Percentage of work force that is union affiliated	13 and 14/21	Sector analysis of production
14/21	Worker productivity		Labor participation rate
15/21	Number of "Fortune 500" firms with representative offices in the city	15/21	Trends in retail trade
16/21	Sector analysis of production	16/21	Trends in wholesale trade
17/21	Commuting trends	17,18, and 19/21	Commuting trends
18/21	Shipping tonnage and traffic		Air-flight tonnage and traffic
19/21	Rail tonnage and traffic		Rail tonnage and traffic

(cont.)

Table A-I (9) (cont.)

Relative Importance Ranking* (out of 21)	Indicator as listed on survey form	Relative Frequency of Mentions** (out of 21)	Indicator as listed on survey form
20/21	Truck tonnage and traffic	20/21	Shipping tonnage and traffic
21/21	Air-flight tonnage	21/21	Truck tonnage and traffic

* The Relative Importance Rankings were computed by ranking the indicators by their adjusted mean importance ratings in each section of the survey

** The Relative Frequencies of Mentions were computed by dividing the number of respondents who listed each indicator as one of the three most important indicators of each of the four sections of the survey by the number of respondents who had answered the question that asked them to rate the importance of that indicator.

Table A-I (10)

Importance Ratings of Economic Information According to Results of Indicator Survey

	Indicator as listed on survey form	Number of Answers[1]	Adjusted Mean Importance Rating[2]	Standard Deviation Importance Rating[3]	Number Mentions as Most Important[4]	Adjusted Frequency Mentions as Most Important[5]
(1)	Number of industries by type and dollar value that opened or entered in last five years	167	2.1	.99	68	.41
(2)	Number of industries by type and dollar value that left or closed in last five years	165	2.1	1.07	51	.31
(3)	Ten largest industries in the city	166	1.5	.86	113	.68
(4)	Number of "Fortune 500" firms with representative offices in the city, by rank, type, size	164	3.0	1.26	15	.09
(5)	Financial institutions with home offices in the city, be rank, type, size	165	2.5	1.10	24	.15
(6)	Value of commercial bank deposits	167	2.5	1.10	16	.16
(7)	Cost of living indicators	166	2.5	1.17	28	.17
(8)	Number of strikes in city in last five years affecting major industries	167	2.7	1.16	24	.14
(9)	Percentage of work force that is union affiliated	167	2.8	1.22	23	.07
(10)	Worker productivity	166	2.9	1.26	20	.12

(cont.)

Table A-I (10) (cont.)

	Indicator as listed on survey form	Number of Answers[1]	Adjusted Mean Importance Rating[2]	Standard Deviation Importance Rating[3]	Number Mentions as Most Important[4]	Adjusted Frequency Mentions as Most Important[5]
(11)	Trends in wholesale trade	167	2.8	1.12	5	.03
(12)	Trends in retail trade	167	2.7	1.15	6	.04
(13)	Energy costs	167	2.6	1.18	15	.09
(14)	Commuting trends	166	3.3	1.14	2	.01
(15)	Air flight tonnage and traffic	167	3.4	1.16	2	.01
(16)	Rail tonnage and traffic	167	3.4	1.16	2	.01
(17)	Shipping tonnage and traffic	167	3.4	1.17	0	0
(18)	Truck tonnage and traffic	166	3.4	1.16	0	0
(19)	Sector analysis of production	166	3.3	1.30	8	.05
(20)	Unemployment rate	74	1.7	.91	35	.47
(21)	Labor participation rate	73	2.8	1.25	4	.05

(cont.)

Table A-I (10) (cont.)

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1 When asked to rate the indicator's importance on a 1-5 scale

2 Excludes "Don't Know" responses and uses a gradient from "1"="most important" to "5"="irrelevent"

3 Computed using the adjusted mean importance rating and the frequencies of each response from "1" to "5" representing importance

4 In response to a question at the end of the economic indicators section asking which three of the twenty-one economic indicators are the most important

5 Number of mentions as one of the three most important divided by the number of answers to the question asking respondents to rate the importance of that indicator

Table A-I (11)

Indicator Survey Results on the Desirability of Comparing Economic Indicators with other Cities

	Indicator as listed on survey form	Number of Answers	Count		Frequency	
			YES	NO	YES(%)	NO(%)
(1)	Number of industries by type and dollar value that opened or entered in last five years	87	39	48	45	55
(2)	Number of industries by type and dollar value that left or closed in last five years	88	39	49	45	55
(3)	Ten largest industries in the city	79	27	52	34	66
(4)	Number of "Fortune 500" firms with representative offices in the city	78	22	56	28	72
(5)	Financial instituions with home offices in the city, by rank, type, size	79	21	58	27	73
(6)	Value of commercial bank deposits	81	35	46	43	57
(7)	Cost of living indicators	95	62	33	65	35
(8)	Number of strikes in city in last five years affecting major industries	83	34	49	41	59
(9)	Percentage of work-force that is union-affiliated	83	35	48	42	58
(10)	Worker productivity	82	31	51	38	62
(11)	Trends in wholesale trade	86	37	49	43	57

(cont.)

Table A-I (11) (cont.)

Indicator as listed on survey form	Number of Answers	Count		Frequency	
		YES	NO	YES(%)	NO(%)
(12) Trends in retail trade	86	37	49	43	57
(13) Energy costs	89	48	41	54	46
(14) Commuting trends	76	17	59	22	78
(15) Air-flight tonnage and traffic	77	24	53	31	69
(16) Rail tonnage and traffic	77	23	54	30	70
(17) Shipping tonnage and traffic	77	23	54	30	70
(18) Truck tonnage and traffic	75	21	54	28	72
(19) Sector analysis of production	75	22	53	29	71
(20) Unemployment rate*	46	32	14	70	30
(21) Labor participation rate*	41	18	23	44	56

* Listed on the survey form on only the second mailing

Table A-I (12)

Comparisons of Indicator Survey Results of Relative Importance Rankings and Frequencies of Mentions as Among Most Important Property Information

Relative Importance Ranking* (out of 20)	Indicator as listed on survey form	Relative Frequency of Mentions** (out of 20)	Indicator as listed on survey form
1/20	Assessed taxable valuation of commercial property	1/20	Assessed taxable valuation of commercial property
2/20	Assessed taxable valuation of residential property	2/20	Assessed taxable valuation of residential property
3 and 4/20	Estimated market value of commercial property	3/20	Estimated market value of commercial property
	Estimated market value of residential property	4/20	Assessment practice information
5/20	Assessment practice information	5 and 6/20	Trends in vacancy rates for commercial property
6/20	Percentages of property exempt from taxation by type of property and adjusted assessment		Estimated market value of commercial property
7/20	Trends in vacancy rates for commercial property	7/20	Percentages of property exempt from taxation by type of property and adjusted assessment
8/20	Average value of building permits by type and volume in last five years	8/20	Average value of building permits by type and volume in last five years

(cont.)

Table A-I (12) (cont.)

Relative Importance Ranking* (out of 20)	Indicator as listed on survey form
9/20	Trends in vacancy rates for residential property
10/20	Percentage of land publicly owned
11/20	Percentage of land publicly owned
12/20	Average annual absorption rate for commercial office space
13/20	Volume of luxury and prestige housing
14/20	Percentage of rental housing that is owner occupied
15/20	Volume of rental housing
16/20	Average investment in recently rehabilitated office space
17/20	Average investment in recently dwelling units
18/20	Map showing location of property uses

Relative Frequency of Mentions** (out of 20)	Indicator as listed on survey form
9 and 10/20	Percentage of land publicly owned
	Trends in vacancy rates for residential property
11 and 12/20	Age of residential housing stock
	Average annual absorption rate for commercial office space
13/20	Average investment in recently rehabilitated office space
14,15,16, and 17/20	Percentage of rental housing that is owner occupied
	Volume of rental housing
	Average investment in recently rehabilitated dwelling units
	Map showing location of property uses
18/20	Changes in types of structures used for commercial purposes

(cont.)

Table A-I (12) (cont.)

Relative Importance Ranking* (out of 20)	Indicator as listed on survey form
19/20	Changes in types of structures used for commercial purposes
20/20	Changes in types of structures used for residential purposes

Relative Frequency of Mentions** (out of 20)	Indicator as listed on survey form
19 and 20/20	Changes in types of structures used for residential purposes
	Changes in types of structures used for commercial purposes

* The Relative Importance Rankings were computed by ranking the indicators by their adjusted mean importance ratings in each section of the survey.

** The Relative Frequencies of Mentions were computed by dividing the number of respondents who listed each indicator as one of the three most important indicators in each of the four sections of the survey by the number of respondents who had answered the question that asked them to rate the importance of that indicator.

Table A-I (13)

Importance Ratings of Property Information According to Results of Indicator Survey

	Indicator as listed on survey form	Number of Answers[1]	Adjusted Mean Importance Rating[2]	Standard Deviation Importance Rating[3]	Number Mentions as Most Important[4]	Adjusted Frequency Mentions as Most Important[5]
(1)	Percentage of land publicly owned	165	2.6		20	.12
(2)	Trends in vacancy rates for commercial property	165	2.2	1.12	35	.21
(3)	Trends in vacancy rates for residential property	169	2.3	1.11	20	.12
(4)	Average annual absorption rate of commercial office space	170	2.8	1.10	6	.04
(5)	Assessed taxable valuation of commercial property	165	1.4	.70	88	.53
(6)	Assessed taxable valuation of residential property	153	1.4	.73	79	.52
(7)	Estimated market value of commercial property	165	1.6	.90	58	.35
(8)	Estimated market value of residential property	165	1.6	.90	35	.21
(9)	Percentages of property exempt from taxation by type of property and adjusted assessment	163	2.0	1.07	33	.20

(cont.)

Table A-I (13) (cont.)

	Indicator as listed on survey form	Number of Answers[1]	Adjusted Mean Importance Rating[2]	Standard Deviation Importance Rating[3]	Number Mentions as Most Important[4]	Adjusted Frequency Mentions as Most Important[5]
(10)	Age of residential housing stock	165	2.8	1.05	7	.04
(11)	Volume of luxury and prestige housing	164	3.0	1.02	0	0
(12)	Percentage of rental housing that is owner-occupied	160	3.0	1.15	2	.01
(13)	Volume of rental housing	163	3.0	1.03	2	.01
(14)	Changes in types of structures used for residential purposes	164	3.5	.98	0	0
(15)	Changes in types of structures used for commercial purposes	164	3.5	1.06	1	.01
(16)	Average investment in recently rehabilitated dwelling units	164	3.4	.08	2	.01
(17)	Average investment in recently rehabilitated office space	162	3.3	2.08	3	.02
(18)	Average value of building permits by type and volume in last five years	164	2.2	1.13	27	.16

(cont.)

Table A-I (13) (cont.)

	Indicator as listed on survey form	Number of Answers[1]	Adjusted Mean Importance Rating[2]	Standard Deviation Importance Rating[3]	Number Mentions as Most Important[4]	Adjusted Frequency Mentions as Most Important[5]
(19)	Map showing location of property uses	162	3.4	1.31	2	.01
(20)	Assessment Practice Information	70	1.7	.98	21	.30

---

1 When asked to rate the indicator's importance on a 1-5 scale

2 Excludes "Don't Know" responses and uses a gradient from "1"="most important" to "5"="irrelevent"

3 Computed using the adjusted mean importance rating and the frequencies of each response from "1" to "5" representing importance

4 In response to a question at the end of the property indicators section asking which of the twenty property indicators are most important

5 Number of mentions as one of the three most important divided by the number of answers to the question asking respondents to rate the importance of that indicator

Table A-I (14)

Indicator Survey Results on the Desirability of Comparing Property Indicators with other Cities

	Indicator as listed on survey form	Number of Answers	[Count] YES	NO	[Frequency] YES(%)	NO(%)
(1)	Percentage of land publicly owned	91	41	50	45	55
(2)	Trends in vacancy rates for commercial property	94	51	43	54	46
(3)	Trends in vacancy rates for residential property	92	46	46	50	50
(4)	Average annual absorption rate of commercial office space	79	26	53	33	67
(5)	Assessed taxable valuation of commercial property	86	45	41	52	48
(6)	Assessed taxable valuation of residential property	80	41	39	51	49
(7)	Estimated market value of commercial property	86	39	47	45	55
(8)	Estimated market value of residential property	86	40	46	47	54
(9)	Percentages of property exempt from taxation by type of property and adjusted assessment	89	47	42	53	47
(10)	Age of residential housing stock	81	31	50	38	62
(11)	Volume of luxury and prestige housing	78	21	57	27	73
(12)	Percentage of rental housing that is owner-occupied	77	28	49	36	64

(cont.)

Table A-I (14) (cont.)

Indicator as listed on survey form	Number of Answers	[Count] YES	NO	[Frequency] YES(%)	NO(%)
(13) Volume of rental housing	79	24	55	30	70
(14) Changes in types of structures used for residential purposes	74	13	61	17	82
(15) Changes in types of structures used for commercial purposes	74	14	60	19	81
(16) Average investment in recently rehabilitated dwelling units	77	22	55	29	71
(17) Average investment in recently rehabilitated office space	76	24	52	32	68
(18) Average value of building permits by type and volume in last five years	89	44	45	49	51
(19) Map showing location of property uses	76	14	62	18	82
(20) Assessment practice information*	40	18	22	45	55

* Listed on the survey form on only the second mailing

Table A-I (15)

Results of Questions on the Indicator Survey

Concerning Information Use

(1) Listed below are seven possible sources of information you may use to evaluate the credit worthiness of a city's specific bond issues. Please rank them in importance with "1" being the most important. If you are unable to decide which of two is more important, mark each item with the same number (i.e. if both are the most important items, both would receive a "2".)

(A) Moody's and Standard & Poor's published bond ratings:

Mean = 2.25, Standard Deviation = 1.30

	Count	Frequency (%)
Citations as importance of "1"	59	36
Citations as importance of "2"	47	28
Citations as importance of "3"	34	20
Citations as importance of "4"	18	11
Citations as importance of "5"	3	2
Citations as importance of "6"	3	2
Citations as importance of "7"	2	1

(B) The prospectus statement of the bond issue:

Mean = 1.51, Standard Deviation = .94

	Count	Frequency (%)
Citations as importance of "1"	110	110
Citations as importance of "2"	36	22
Citations as importance of "3"	11	7
Citations as importance of "4"	3	2
Citations as importance of "5"	1	1
Citations as importance of "6"	1	1
Citations as importance of "7"	1	1

(C) Informal recommendations of colleagues:

Mean = 4.44, Standard Deviation = 1.62

	Count	Frequency (%)
Citations as importance of "1"	1	1
Citations as importance of "2"	13	10
Citations as importance of "3"	18	14
Citations as importance of "4"	33	25
Citations as importance of "5"	43	33
Citations as importance of "6"	22	17
Citations as importance of "7"	2	2

(cont.)

Table A-I (15) (cont.)

(1) (D) Limited circulation reports:

Mean = 4.06, Standard Deviation = 1.44

	Count	Frequency (%)
Citations as importance of "1"	7	5
Citations as importance of "2"	15	12
Citations as importance of "3"	22	17
Citations as importance of "4"	29	21
Citations as importance of "5"	40	31
Citations as importance of "6"	19	15
Citations as importance of "7"	1	1

(E) In-house research:

Mean = 2.80, Standard Deviation = 1.32

	Count	Frequency (%)
Citations as importance of "1"	20	14
Citations as importance of "2"	49	34
Citations as importance of "3"	42	29
Citations as importance of "4"	18	12
Citations as importance of "5"	10	7
Citations as importance of "6"	6	4
Citations as importance of "7"	1	1

(F) Yields of comparable issues:

Mean = 3.97, Standard Deviation = 2.22

	Count	Frequency (%)
Citations as importance of "1"	5	4
Citations as importance of "2"	17	12
Citations as importance of "3"	36	26
Citations as importance of "4"	31	23
Citations as importance of "5"	18	13
Citations as importance of "6"	27	20
Citations as importance of "7"	3	2

(G) Other:

	Count	Frequency (%)
Citations as importance of "1"	4	40
Citations as importance of "2"	3	30
Citations as importance of "3"	3	30

(cont.)

Table A-I (15) (cont.)

(2) Listed below are the major informational components of a municipal prospectus. Please rank the items in importance in evaluation of a city's credit worthiness with "1" being the most important group. As before, if you are unable to decide which of two is more important, mark each item with the same number.

(A) Analysis of debt and revenue structure:

Mean = 1.16, Standard Deviation = .46

	Count	Frequency (%)
Citations as importance of "1"	144	88
Citations as importance of "2"	14	9
Citations as importance of "3"	6	4

(B) Analysis of expenditures:

Mean = 2.12, Standard Deviation = .81

	Count	Frequency (%)
Citations as importance of "1"	36	22
Citations as importance of "2"	81	50
Citations as importance of "3"	37	23
Citations as importance of "4"	9	5

(C) Analysis of economic trends:

Mean = 2.44, Standard Deviation = .90

	Count	Frequency (%)
Citations as importance of "1"	27	17
Citations as importance of "2"	51	32
Citations as importance of "3"	68	43
Citations as importance of "4"	12	8
Citations as importance of "5"	2	1

(D) Analysis of demographic trends:

Mean = 3.49, Standard Deviation = 1.13

	Count	Frequency (%)
Citations as importance of "1"	10	7
Citations as importance of "2"	20	14
Citations as importance of "3"	26	18
Citations as importance of "4"	68	47
Citations as importance of "5"	20	14
Citations as importance of "6"	1	1

(cont.)

Table A-I (15) (cont.)

(2) (D) Statement of bond counsel:

Mean = 4.14, Standard Deviation = 1.23

	Count	Frequency (%)
Citations as importance of "1"	8	6
Citations as importance of "2"	7	5
Citations as importance of "3"	17	13
Citations as importance of "4"	26	20
Citations as importance of "5"	67	52
Citations as importance of "6"	3	2

(E) Other:

	Count	Frequency (%)
Citations as importance of "1"	3	17
Citations as importance of "2"	2	11
Citations as importance of "3"	1	6
Citations as importance of "4"	0	0
Citations as importance of "5"	2	11
Citations as importance of "6"	10	57

(3) Has the poor quality of information in a prospectus issue of a municipality, independent of other inputs, ever detered you from purchasing a security?

Response	Count	Frequency (%)
Yes	120	74
No	22	13
Uncertain	23	13

(4) If the sources of information which you usually rely upon still leave you encertain as to whether to buy a specific issue, would you?

Response	Count	Frequency (%)
Not buy the bonds	73	44
Obtain more information	92	56

(cont.)

Table A-I (15) (cont.)

(5) If you would obtain more information, what source(s) would you go to? (More than one answer may be appropriate. Check all those which apply.)

Response	Count	Frequency (%)	Proportion of Respondents Citing as Source (%)
The underwriter	118	43	98
The municipality that is issuing the bonds	110	40	91
Other	27	10	22
Would not bother to look for more information:	18	7	15

(6) Assume that the economic, social, and political circumstances of two municipalities are essentially equivalent and that each is issuing a debt offering in the same time period. If the propsectus of one municipality is inferior in information content to that of the other, how do you think this will affect the relative interest rates? (check one)

Response	Count	Frequency (%)
The municipality with the inferior prospectus will be forced to pay significantly higher interest rates.	30	19
The municipality with the inferior prospectus will be forced to pay somewhat higher interest rates	91	54
The difference in prospectus quality will not affect interest rates	27	17
Other	12	8

(cont.)

Table A-1 (15) (cont.)

(7)* How much time do you, your staff, and/or you client usually spend reviewing a prospectus? (check one)

Response	Count	Frequency (%)
Less than one hour	41	62
Several hours	22	33
More than several hours	3	5

(8)* Would a short document with notice of a bond sale and key information be useful to you if you also had access to a detailed prospectus? (check one)

Response	Count	Frequency (%)
Yes	65	85
No	5	7
Don't know	6	8

(9) Regarding the composition of your municipal bond portfolio(s), would you please assign approximate percentages to the following categories: (The total should add to 100%)

(A) Holdings from the municipality (city or two) within which I am located.
(B) Holdings from other municipalities within my state and of my state itself.
(C) Holdings from state and local authorities outside of the state in which I am located.
(D) This question is not applicable.

Results: This question received a wide range of responses showing no particular biases with most holding a large proportion of nonlocal bonds.

* These questions were included on the survey form in only the second mailing.

(cont.)

Table A-1 (15) (cont.)

(10) Further regarding the composition of your municipal bond portfolio(s), would you please assing approximate percentages to the following categories: (The total should add to 100%)

- (A) Bond anticipation notes
- (B) Tax anticipation notes
- (C) Other revenue anticipation notes
- (D) Revenue bonds
- (E) Moral obligation bonds
- (F) General obligation bonds of municipalities
- (G) General obligation bonds of state governments or guaranteed by state governments
- (H) This question is not applicable.

Results: This question received a wide range of responses showing no particular biases, with most holding a large proportion of revenue bonds and general obligation bonds of municipalities.

(11) Leaving aside considerations of yield and risk, are you more reluctant to buy if the issuing municipality is located outside of the region of the country in which you are located? (check one)

Response	Count	Frequency (%)
I am somewhat more reluctant to buy a bond if it is issued from a different area of the country.	24	16
I am much more reluctant to buy a bond if it is issued from a different area of the country	45	34
I am indifferent in deciding to buy a bond that it is issued from a different area of the country	65	49

Appendix II

Survey Form and Tabulated Results of The Perceptions Survey

CITY OF BOSTON
OFFICE OF THE TREASURER
CITY HALL, BOSTON

BOSTONIA CONDITA 1630

JAMES V. YOUNG
TREASURER

June 23, 1976

Dear Municipal Bond Investor:

Earlier this year we asked you to complete a questionnaire identical to the one attached, to help us identify investor perceptions of the City of Boston. As we ncted then, the Treasury Department of the City of Boston is fortunate to have the assistance of a graduate student team from the Massachusetts Institute of Technology in carrying out this survey and analyzing the results. While we are heartened by the substantial response to our first mailing, we nevertheless would like to enlarge our data base, and once again ask for your cooperation and encourage you to complete the questionnaire as the results of this survey will help Boston shape and strengthen the disclosure information which accompanies its municipal bond issues.

We would prefer to receive your answers as soon as possible. Thank you for your cooperation.

Sincerely,

James V. Young
Collector-Treasurer
City of Boston

Kent Colton
Assistant Professor of
Urban Studies and Planning
Massachusetts Institute of Technology

JVY/ja

SURVEY OF INVESTOR PERCEPTIONS OF BOSTON

This survey is intended to find out what investors think about Boston. Its purpose is to see if Boston could present itself more accurately in prospectus statements and other literature. All data will be analyzed in aggregate form in confidence. Most of the questions ask only your opinion.

1.) Have you ever been to Boston? (check one)

_____A.) MANY TIMES _____B.) SEVERAL TIMES _____C.) ONCE _____D.) NEVER

_____E.) HAVE LIVED IN BOSTON OR BOSTON AREA

2.) What are your perceptions about how the city of Boston's property values in residential neighborhoods are changing relative to property values in other cities? (check one)

_____A.) Residential property values in the city of Boston are rising faster than those in other cities.

_____B.) Residential property values in the city of Boston are changing evenly with those in other cities.

_____C.) Residential property values in the city of Boston are lagging behind those in other cities.

3.) How attractive do you consider investments in real property in the city of Boston to be? (check one)

_____A.) Investments in real property in the city of Boston are more attractive than those in other cities.

_____B.) Investments in real property in the city of Boston are on par with those in other cities.

_____C.) Investments in real property in the city of Boston are less attractive than those in other cities.

4.) Which, if any, do you perceive as significant problems which the city of Boston must resolve to maintain economic prosperiety? (check "problem" if you think the factor is a problem, check "not a problem" if you think that the factor is not a problem, or check "don't know" if you don't feel qualified to give an opinion.)

	PROBLEM	NOT A PROBLEM	DON'T KNOW
A.) Decline in manufacturing:	_____	_____	_____
B.) Revaluation issues:	_____	_____	_____
C.) Pension liabilities of city employees:	_____	_____	_____
D.) Federal and state aid cutbacks:	_____	_____	_____
E.) Cutbacks in military facilities:	_____	_____	_____
F.) Carrying costs on existing city debt:	_____	_____	_____
G.) School administration and desegregation:	_____	_____	_____

H.) Other, please specify ______________________________________

(cont.)

5.) How would you rate the current situations in the following areas in the city of Boston? (Circle "1" if you rate to situation to be "very good", circle "5" if you rate the situation to be "very poor", circle "2", "3", or "4" if you rate the situation to be "good", "average compared to other cities", or "poor". Check "don't know" if you don't feel qualified to give an opinion.)

	VERY GOOD	GOOD	AVER-AGE	POOR	VERY POOR	DON'T KNOW
A.) Business activities:	1	2	3	4	5	_____
B.) Public safety:	1	2	3	4	5	_____
C.) Educational levels:	1	2	3	4	5	_____
D.) Medical care facilities:	1	2	3	4	5	_____
E.) Effectiveness of city government:	1	2	3	4	5	_____
F.) Quality of life/environment:	1	2	3	4	5	_____
G.) Recreation, cultural facilities, art:	1	2	3	4	5	_____
H.) Transportation and road systems:	1	2	3	4	5	_____

6.) How do you perceive population trends in Boston? (check all appropriate categories)

_____A.) Significant out-migration to suburbs of Boston

_____B.) Significant in-migration

_____C.) Stable population levels

_____D.) Significant out-migration to other areas than Boston area

_____E.) Stable population levels, but significantly changing population composition

_____F.) Don't know

7.) Are Boston's environmental qualities an economic asset? _____A.) YES, _____B.) NO, _____C.) DON'T KNOW

If you answered "YES" to the above, could you give an example?____

____

8.) Are Boston's cultural amenities an economic asset? _____A.) YES, _____B.) NO, _____C.) DON'T KNOW,

If you answered "YES" to the above, could you give an example?____

____

(cont.)

9.) Please compare Boston to the following cities on general economic characteristics: (check "better" if you think that Boston's economy is generally better than the economy of that city, check "worse" if you think that Boston's economy is not as good as that city's, check "similar" if the general characteristics of Boston's economy and that of the other city's seem to balance out, or check "don't know" if you don't feel qualified to give an opinion.)

	BETTER	WORSE	SIMILAR	DON'T KNOW		BETTER	WORSE	SIMILAR	DON'T KNOW
A.) Atlanta	____	____	____	____	H.) Milwaukee	____	____	____	____
B.) Cincinnati	____	____	____	____	I.) New Orleans	____	____	____	____
C.) Cleveland	____	____	____	____	J.) Newark	____	____	____	____
D.) Dallas	____	____	____	____	K.) Philadelphia	____	____	____	____
E.) Detroit	____	____	____	____	L.) Pittsburg	____	____	____	____
F.) Houston	____	____	____	____	M.) St. Louis	____	____	____	____
G.) Kansas City	____	____	____	____	N.) San Francisco	____	____	____	____

10.) Please compare Boston to the following cities on general quality of life as a city to live, work, or visit in: (check "better if you think that the quality of life in Boston is generally better than the quality of life in the other city, check "worse" if you think that Boston's life qualities are not as good as that of the other city, check "similar" if the general characteristics of Boston's life qualities and that of the other city seem to balance out, or check "don't know" if you don't feel qualified to give an opinion.)

	BETTER	WORSE	SIMILAR	DON'T KNOW		BETTER	WORSE	SIMILAR	DON'T KNOW
A.) Atlanta	____	____	____	____	H.) Milwaukee	____	____	____	____
B.) Cincinnati	____	____	____	____	I.) New Orleans	____	____	____	____
C.) Cleveland	____	____	____	____	J.) Newark	____	____	____	____
D.) Dallas	____	____	____	____	K.) Philadelphia	____	____	____	____
E.) Detroit	____	____	____	____	L.) Pittsburg	____	____	____	____
F.) Houston	____	____	____	____	M.) St. Louis	____	____	____	____
G.) Kansas City	____	____	____	____	N.) San Francisco	____	____	____	____

(cont.)

11.) How would you project the following factors in the city of Boston in the next five years? (check "much greater" if you expect it to be much greater than current levels, "greater" if you expect it to be so, "current" if you expect it to be very similar to the current situation, or "don't know" if you don't feel qualified to give an opinion.)

	MUCH GREATER	GREATER	CURRENT	LESS THAN	DON'T KNOW
A.) Economic well-being of major retail business:	___	___	___	___	___
B.) Economic well-being of manufactoring industries:	___	___	___	___	___
C.) Economic well-being of financial institutions:	___	___	___	___	___
D.) Economic well-being of high technology, R.&D. industries and specialized consulting firms:	___	___	___	___	___
E.) Popularity as a convention location:	___	___	___	___	___
F.) Popularity as a home office location:	___	___	___	___	___
G.) Overall population levels:	___	___	___	___	___

12.) Would you consider buying a new issue of Boston's bonds if you were in the market for municipal bonds?

_____A.) YES _____B.) NO _____C.) UNCERTAIN

13.) In making your decision as to whether or not to buy, how would each of the following factors (in addition to bond yield) affect your decision? (check "important", "unimportant", or "don't know".)

	IMPORTANT	UNIMPORTANT	DON'T KNOW
A.) Your personal confidence in the city of Boston:	___	___	___
B.) Your estimation of the quality of the city's finances:	___	___	___
C.) The goodwill of city politicians:	___	___	___
D.) A colleague's recommendation:	___	___	___
E.) Aspects of the city's prospectus:	___	___	___

F.) Other, please specify:____

(cont.)

14.) How would you rate the security of Boston's bonds compared to those of other cities?

_____A.) MORE SECURE, _____B.) AS SECURE, _____C.) LESS SECURE, _____D.) DON'T KNOW,

15.) How would you rate the security of Boston's bonds compared to other municipalities in Massachusetts?

_____A.) MORE SECURE, _____B.) AS SECURE, _____C.) LESS SECURE, _____D.) DON'T KNOW,

16.) How would you rate the security of Boston's bonds compared to state and suburban issues not in Massachusetts?

_____A.) MORE SECURE, _____B.) AS SECURE, _____C.) LESS SECURE, _____D.) DON'T KNOW,

17.) If you are familiar with previous prospectus statements for new bond issues by Boston, where and how could the material be most improved?

_____A.) Presentation of Boston's demographic characteristics

_____B.) Presentation of characteristics of Boston's economy

_____C.) Presentation of Boston's expenditures and revenue structure

_____E.) Presentation of Boston's debt structure

Comments on above ____

____

18.) How do you think that news coverage of the city of Boston's school desegregation order and related events have affected the city's financial reputation with potential investors? (check one)

_____A.) The financial reputation which Boston has with potential investors has not been significantly affected.

_____B.) The financial reputation which Boston has with potential investors has been improved.

_____C.) The financial reputation which Boston has with potential investors has been somewhat damaged.

_____D.) The financial reputation which Boston has with potential investors has been greatly damaged.

_____E.) DON'T KNOW

(cont.)

19.) If you are familiar with the city of Boston's policy making and administration, please rate the city in these areas: (check the appropriate category)

		GOOD	ADEQUATE	POOR	DON'T KNOW
A.)	Negotiating arrangements with municipal unions and public employees:	____	____	____	____
B.)	Planning for educational programs and facilities and implementation of desegregation order:	____	____	____	____
C.)	Optimization of economic impacts of health care industry:	____	____	____	____
D.)	Provision of police and fire protection services:	____	____	____	____
E.)	Maintenance and improvement of roads, sewers, parks:	____	____	____	____
F.)	Input into decisions of the Massachusetts Port Authority regarding its financing and operation of facilities such as Logan airport and the harbor:	____	____	____	____
G.)	Input into decisions of the Metropolitan Boston Transit Authority regarding its financing, service levels, and capital improvements:	____	____	____	____
H.)	Negotiating in securing federal funds:	____	____	____	____
I.)	Negotiating tax abatements at reasonable levels for city interests:	____	____	____	____

J.) Do you have any additional comments on any, all, or missing items under the above?____________________

____

The time and thought you have put into answering this survey are greatly appreciated.

Do you have any general or specific comments relating to any of the issues raised in this survey?

____

____

____

____

____

____

____

____

Results of Perceptions Survey

(1) Have you ever been to Boston? (check one)

Response	Count	Frequency (%)
(A) Many times	19	13
(B) Several times:	37	24
(C) Once:	31	20
(D) Never:	32	21
(E) Lived in Boston or Boston area:	34	22

(2) What are your perceptions about how the city of Boston's property values in residential neighborhoods are changing relative to property values in other cities? (check one)

Response	Count	Frequency (%)
(A) Residential property values in the city of Boston are rising faster than those in other cities:	12	9
(B) Residential property values in the city of Boston are changing evenly with those in other cities:	58	42
(C) Residential property values in the city of Boston are lagging behind those in other cities:	68	49

(3) How attractive do you consider investments in real property in the city of Boston to be? (check one)

Response	Count	Frequency (%)
(A) Investments in real property in the city of Boston are more attractive than those in other cities:	4	3
(B) Investments in real property in the city of Boston are on a par with those of other cities:	45	31
(C) Investments in real property in the city of Boston are less attractive than those in other cities:	94	66

(cont.)

(4) Which, if any, do you perceive as significant problems which the city of Boston must resolve to maintain economic prosperity?

	Count			Frequency (%)		
Response	Problem	Not a Problem	Do Not Know	Problem	Not a Problem	Do Not Know
(A) Decline in manufacturing:	71	18	54	50	13	38
(B) Revaluation issues:	54	6	84	38	4	58
(C) Pension liabilities of city employees:	102	1	45	69	1	30
(D) Federal and state aid cutbacks:	76	12	55	53	8	38
(E) Cutbacks in military facilities:	43	30	67	31	21	48
(F) Carrying costs on existing city debt:	111	9	28	75	6	19
(G) School administration and desegregation:	143	0	4	97	0	3

(5) How would you rate the current situations in the following areas in the city of Boston?

(A) Business activities:
Adjusted mean = 3.32

	Count	Adjusted frequency (%)
1 = Very good	6	5
2 = Good	42	33
3 = Average	65	51
4 = Poor	14	11
5 = Very poor	1	1
Don't know	21	--

(cont.)

(5) (B) Public safety:
Adjusted mean = 3.32

	Count	Adjusted frequency (%)
1 = Very good	2	2
2 = Good	12	10
3 = Average	56	50
4 = Poor	14	30
5 = Very poor	1	1
Don't know	21	--

(C) Education levels:
Adjusted mean = 2.86

	Count	Adjusted frequency (%)
1 = Very good	15	12
2 = Good	34	27
3 = Average	56	30
4 = Poor	29	30
5 = Very poor	9	7
Don't know	23	--

(D) Medical care facilities:
Adjusted mean = 1.83

	Count	Adjusted frequency (%)
1 = Very good	50	46
2 = Good	33	30
3 = Average	21	19
4 = Poor	5	5
5 = Very poor	0	0
Don't know	36	--

(cont.)

(5) (E) Effectiveness of city government: Adjusted mean = 3.35

	Count	Adjusted frequency (%)
1 = Very good	1	1
2 = Good	10	9
3 = Average	64	55
4 = Poor	31	26
5 = Very poor	11	9
Don't know	29	--

(F) Quality of life/environment: Adjusted mean = 2.92

	Count	Adjusted frequency (%)
1 = Very good	7	5
2 = Good	37	28
3 = Average	53	40
4 = Poor	34	25
5 = Very poor	3	2
Don't know	3	--

(G) Recreation, cultural facilities, art: Adjusted mean = 1.81

	Count	Adjusted frequency (%)
1 = Very good	46	36
2 = Good	63	49
3 = Average	16	13
4 = Poor	3	2
5 = Very poor	0	0
Don't know	19	--

(cont.)

(5) (H) Transportation and road systems:
Adjusted mean = 2.63

Transportation and road systems	Count	Adjusted frequency (%)
1 = Very good	9	7
2 = Good	50	41
3 = Average	46	37
4 = Poor	14	11
5 = Very poor	4	3
Don't know	25	--

(6) How do you perceive trends in Boston? (check all appropriate categories)

Response:	Count	Frequency (%)
(A) Significant out migration to suburbs of Boston:	83	55
(B) Significant in migration:	2	1
(C) Stable population levels:	14	9
(D) Significant out migration to other areas than the Boston area:	39	22
(E) Stable population levels, but significantly changing population composition:	26	18
(F) Don't know	22	15

(7) Are Boston's environmental qualities an economic asset?

Response	Count	Frequency (%)
Yes	42	29
No	38	26
Don't know	65	45

(cont.)

(8) Are Boston's cultural amenities an economic asset?

Response:	Count	Frequency (%)
Yes	101	69
No	17	12
Don't know	29	20

Examples given for questions (7) and (8) included: the Boston Pops, the Commons and Public Gardens, Harvard, M.I.T., and the schools in the area, the proximity to the ocean, and the architecture.

(9) Please compare Boston to the following cities on general economic characteristics:

City of comparison:	Count				Adjusted
	Better	Worse	Similar	Don't Know	Mean*
Atlanta	6	118	11	10	1.17
Cincinnati	10	79	37	18	1.45
Cleveland	41	23	68	13	2.14
Dallas	6	130	3	7	1.11
Detroit	84	9	44	8	2.55
Houston	7	131	1	6	1.11
Kansas City	11	98	12	23	1.28
Milwaukee	7	93	22	23	1.30
New Orleans	11	82	27	24	1.41
Newark	99	10	27	9	2.65
Philadelphia	54	14	68	9	2.29
Pittsburgh	15	54	53	22	1.68
St. Louis	21	53	49	22	1.74
San Francisco	7	107	22	9	1.26

*Adjusted mean computed using: 3 = better, 2 = similar, and 1 = worse.

(cont.)

(10) Please compare Boston to the following cities on general quality of life as a city in which to live, work, or visit:

City of comparison:	Count				Adjusted Mean*
	Better	Worse	Similar	Don't Know	
Atlanta	8	106	22	9	1.28
Cincinnati	18	71	42	17	1.60
Cleveland	75	13	43	17	2.47
Dallas	22	92	18	16	1.47
Detroit	94	6	37	10	2.74
Houston	22	89	23	13	1.50
Kansas City	31	65	22	29	1.71
Milwaukee	33	65	27	22	1.74
New Orleans	20	74	32	19	1.57
Newark	112	6	18	11	2.78
Philadelphia	55	13	67	12	2.31
Pittsburg	57	26	44	18	2.24
St. Louis	42	34	43	26	2.07
San Francisco	9	98	27	11	1.35

*Adjusted mean computed using: 3 = better, 2 = similar, and 1 = worse.

(11) How would you project the following factors in the city of Boston in the next five years?

(A) Economic well-being of major retail business:
Adjusted mean = 1.87**

	Count	Adjusted Frequency (%)
Much greater	0	0
Greater	22	19
Current	59	50
Less than	37	31
Don't know	31	--

**Adjusted mean was computed using: 4 = much greater, 3 = greater, 2 = current, 1 = less than.

(cont.)

(11) (B) Economic well-being of manufacturing industries: Adjusted mean = 1.62*

	Count	Adjusted frequency (%)
Much greater	0	0
Greater	12	12
Current	36	37
Less than	49	51
Don't know	25	--

(C) Economic well-being of financial institutions: Adjusted mean = 2.23*

	Count	Adjusted frequency (%)
Much greater	2	2
Greater	45	36
Current	63	50
Less than	19	15
Don't know	17	--

(D) Economic well-being of high technology, R&D industries and specialized consulting firms: Adjusted mean = 2.34*

	Count	Adjusted frequency (%)
Much greater	5	4
Greater	51	42
Current	46	16
Less than	20	19
Don't know	23	--

---

*Adjusted mean was computed using: 4 = much greater, 3 = greater, 2 = current, 1 = less than.

(cont.)

(11) (E) Popularity as a convention location: Adjusted mean = 1.84*

	Count	Adjusted frequency (%)
Much greater	0	0
Greater	27	22
Current	51	41
Less than	47	38
Don't know	23	--

(F) Popularity as a home office: Adjusted mean = 1.67*

	Count	Adjusted frequency (%)
Much greater	6	5
Greater	7	5
Current	45	35
Less than	71	55
Don't know	19	--

(G) Overall population levels: Adjusted mean = 1.65*

	Count	Adjusted frequency (%)
Much greater	6	5
Greater	8	6
Current	50	39
Less than	65	47
Don't know	14	--

---

*Adjusted mean was computed using: 4 = much greater, 3 = greater, 2 = current, 1 = less than.

(12) Would you consider buying a new issue of Boston's bonds if you were in the market for municipal bonds?

	Count	Frequency (%)
Yes	26	18
No	85	59
Uncertain	34	23

(cont.)

(13) In making your decision as to whether or not to buy, how would each of the following factors (in addition to bond yield) affect your decision?

(A) Your personal confidence in the City of Boston:

	Count	Frequency (%)
Important	125	85
Unimportant	16	11
Don't know	6	4

(B) Your estimation of the quality of the City's finances:

	Count	Frequency (%)
Important	144	97
Unimportant	2	1
Don't know	3	2

(C) The goodwill of City politicians:

	Count	Frequency (%)
Important	64	44
Unimportant	59	40
Don't know	23	16

(D) A colleague's recommendation:

	Count	Frequency (%)
Important	33	23
Unimportant	85	60
Don't know	23	16

(E) Aspects of the City's prospectus:

	Count	Frequency (%)
Important	121	85
Unimportant	7	5
Don't know	15	10

(cont.)

(14) How would you rate the security of Boston's bonds compared to those of other cities?

	Count	Frequency (%)
More secure	2	1
As secure	31	22
Less secure	95	68
Don't know	11	8

(15) How would you rate the security of Boston's bonds compared to other municipalities in Massachusetts?

	Count	Frequency (%)
More secure	2	1
As secure	42	33
Less secure	76	53
Don't know	21	15

(16) How would you rate the security of Boston's bonds compared to state and suburban issues not in Massachusetts?

	Count	Frequency (%)
More secure	3	2
As secure	15	11
Less secure	101	73
Don't know	20	14

(17) If you are familiar with previous prospectus statements for new bond issues by Boston, where and how could the material be most improved?

Response	Number of checks
Presentation of Boston's demographic characteristics	27
Presentation of the characteristics of Boston's economy	42
Presentation of Boston's expenditures and revenue structure	55
Presentation of Boston's debt structure	48

(cont.)

**(18) How do you think that news coverage of the city of Boston's school desegregation order and related events has affected the city's financial reputation with potential investors?

	Response	Count	Frequency (%)
(A)	Has not been significantly affected	3	4
(B)	Has been improved	1	1
(C)	Has been somewhat damaged	39	48
(D)	Has been greatly damaged	38	46
(E)	Don't know	1	1
			100% TOTAL

(19) If you are familiar with the City of Boston's policy making and administration, please rate the City in these areas:

(A) Negotiating arrangements with muncipal unions and public employees:

Adjusted mean=1.35*

Response	Count	Frequency (%)
Good	2	5
Adequate	10	25
Poor	28	70
Don't know	60	-

(B) Planning for educational programs and facilities and implementation of the desegregation order:

Adjusted mean=1.53*

Response	Count	Frequency (%)
Good	7	16
Adequate	10	22
Poor	28	62
Don't know	60	-

---

*Adjusted mean was computed using: 3 = good, 2 = adequate, 1 = poor
**This question was included on the survey form on only the second mailing.

(cont.)

(19) (C) Optimization of economic impacts of health care industry:

Adjusted mean=2.08*

Response	Count	Frequency (%)
Good	55	50
Adequate	9	16
Poor	46	42
Don't know	45	-

(D) Provisions of police and fire protection services:

Adjusted mean=1.97*

Response	Count	Frequency (%)
Good	8	24
Adequate	17	50
Poor	9	26
Don't know	66	-

(E) Maintenance and improvement of roads, sewers, parks:

Adjusted mean=1.72*

Response	Count	Frequency (%)
Good	4	9
Adequate	25	54
Poor	17	17
Don't know	57	-

*Adjusted mean was computed using: 3 = good, 2 = adequate, 1 = poor

(cont.)

(19) (F) Input into decisons of the Massachusetts Port Authority regarding its financing and operation of facilities such as Logan Airport and the harbor:

Adjusted mean=1.85*

Response	Count	Frequency (%)
Good	8	24
Adequate	12	36
Poor	13	39
Don't know	66	-

(G) Input into decisions of the Metropolitan Transit Authority regarding its financing, service levels, and capital improvements:

Adjusted mean=1.82*

Response	Count	Frequency (%)
Good	8	24
Adequate	11	33
Poor	14	42
Don't know	67	-

(H) Negotiating in securing federal funds:

Adjusted mean=1.66*

Response	Count	Frequency (%)
Good	5	19
Adequate	17	65
Poor	4	15
Don't know	75	-

*Adjusted mean was computed using: 3 = good, 2 = adequate, 1 = poor

(cont.)

(19) (I) Negotiating tax abatements at reasonable levels for city interests:

Adjusted mean=1.60*

Response	Count	Frequency (%)
Good	2	8
Adequate	11	44
Poor	12	48
Don't know	74	-

*Adjusted mean was computed using: 3 = good, 2 = adeqate, 1 = poor.

Appendix III

Survey Form and Tabulated Results of The Survey of Financial Officers

JSP

Department of Urban Studies and Planning

Room 9-521
Massachusetts Institute of Technology

Cambridge Massachusetts 02139

Phone 617 253- 7736

August 29, 1976

[name and address of financial officer]

Dear [name of financial officer]

We are currently doing a study of the sources of information for investors who are interested in municipal bonds. We are interested in the financial information which is compiled and made available by large cities and this survey addresses this question. Your cooperation in answering the attached questions would be very helpful. It should take you only about ten minutes. The sooner we receive your response, the more opportunity we will have to integrate it with other research. Please take a few minutes to fill out the questionaire today and mail it in the enclosed envelope. If you have any additionalcomments on this subject, they would certainly be appreciated.

Sincerely,

Kent Colton

Kent Colton
Associate Professor
Department of Urban Studies
and Planning, MIT

Kay Anderson

Kay Anderson
Graduate student
Department of Urban Studies
and Planning, MIT

Cities Responding to the Survey of Financial Officers

Atlanta	Milwaukee
Baltimore	Minneapolis
Boston	Nashville
Chicago	New Orleans
Cincinnati	Oakland
Columbus	Oklahoma City
Dallas	Philadelphia
Denver	Phoenix
Detroit	Pittsburgh
Fort Worth	Portland
Jacksonville	San Antonio
Kansas City	Seattle
Long Beach	St. Louis
Los Angeles	San Fransisco
Louisville	Toledo
Memphis	

Table A-III-1

Results of Survey of Financial Officers

(1) Did the city send out an annual report last year?

Response	Count	Frequency (%)
Yes	30	100
No	0	0

(2) Who wrote the City's last annual financial report? (check one)

Response	Count	Frequency (%)
Primarily, the City Treasury staff	5	16
Primarily, the staff of the underwriter of the last bond issue	1	3
A combination of the staff of the City Treasury and staff of the underwriter	1	3
Other, please specify*	23	78

* Most specified either the comptroller's office or an auditor.

(3) How completely and by whom was the annual financial report autited?

	Count responding	
	Checked Complete Report	Checked City Financial Section
An independent auditor	4	13
An auditor who is a city employee	1	3
An auditor who is a state employee	6	6

(4) To whom was the annual report distributed? (check all which apply)

Response	Count (out of 30)
To local banks	29
To nonlocal banks	22
To local bond dealers	26
To a few local citizens	17
To many local citizens	7
To more than a few nonlocal citizens	14

(In addition to these choices, a few respondents wrote in local journal, local libraries, mailing list, and municipal and state governments).

(cont.)

Table A-III-1 (cont.)

(5) About how many copies of the annual financial report were distributed?

Mean = 369 copies, Range = 100 to 850 copies

(6) Who wrote the prospectus statement for the city's last bond issue?

Response	Count	Frequency (%)
Primarily, the City Treasury staff	5	12
Primarily, the staff of the underwriter of the last bond issue	3	10
A combination of the staff of the City Treasury and staff of the underwriter	3	10
Other, please specify*	19	68

*Responses included the bond counsel, financial consultant, and auditor.

(7) About how many pages was the latest prospectus statement?

Mean = 44 pages, Range = 4 to 165 pages (Philadelphia had the longest)

(8) About how many copies of the prospectus statement were distributed?

Mean = 467**, Range = 57 to 1800 and 3,000 copies

** Mean was computed not including distribution by Boston of 3,000 copies.

(9) Do you have a mailing list to which you regularly mail propsectus statements?

Response	Count	Frequency (%)
Yes	29	90
No	1	10

(cont.)

Table A-III-1 (cont.)

(10) How completely and by whom was the prospectus statement audited?

	Count responding	
	Checked Complete Report	Checked City Financial Section
An independent auditor	2	10
An auditor who is a city employee	23	16
An auditor who is a state employee	1	6

(11) Was there significant input from ths state government into how the prospectus statement should be written or what information should be included? If so, please explain briefly:

Responses: Pittsburgh used a Pennsylvanis Guiding Statute; other states provided no input.

(12) Does the city utilize any sort of occasional or regular newsletters to bond buyers?

Response	Count	Frequency (%)
Yes*	1	3
No	29	97
No	29	97

*Philadelphia (see reference in bibliography to Moak, Lennox L. "Statement of Lennox L. Moak Concerning Initiation of Series to be Known as 'Financial Releases'". (August]9, 1975))

(cont.)

Table A-III-1 (cont.)

(13) What interest rate did the city pay on your last long-term debt offering? (please give % and date)

City	Rate (%)	Date	City	Rate (%)	Date
Minneapolis	4.45	4/76	Oklahoma City	4.83	8/76
Kansas City	4.96	1/76	Dallas	5.13	5/76
Louisville	5.17	9/73	Jacksonville	5.18	72
Milwaukee	5.19	5/76	Portland	5.24	4/76
San Antonio	5.34	5/76	San Francisco	5.42	9/76
Fort Worth	5.58	2/76	Toledo	5.66	9/76
Atlanta	5.71	6/76	Phoenix	5.72	7/76
Denver	5.86	12/74	Memphis	5.87	--
Long Beach	5.93	8/73	Oakland	6.00	5/74
Chicago	6.02	7/76	Columbus	6.12	6/76
Baltimore	6.14	5/76	New Orleans	6.25	6/74
Seattle	6.30	5/76	Nashville	6.3	9/76
Cincinnati	6.50	4/76	St. Louis	6.52	1/76
Los Angeles	6.69	5/76	Pittsburgh	6.77	9/76
Philadelphia	7.69	9/76	Boston	7.86	6/76
Detroit	9.78	6/76			

(14) What interest rate did the city pay on your last short-term debt offering? (please give % and date)

City	Rate (%)	Date	City	Rate (%)	Date
Minneapolis	--	--	Oklahoma City	4.75	4/76
Kansas City	3.19	4/76	Dallas	--	--
Louisville	--	--	Jacksonville	--	--
Milwaukee	4.32	5/76	Portland	4.45	7/76
San Antonio	--	--	San Francisco	--	--
Fort Worth	--	--	Toledo	4.00	9/76
Atlanta	4.25	6/76	Phoenix	6.13	7/76
Denver	--	--	Memphis	5.48	4/74
Long Beach	3.74	--	Oakland	7.00	9/76
Chicago	3.98	1/76	Columbus	3.37	6/76
Baltimore	--	--	New Orleans	--	--
Seattle	4.75	6/76	Nashville	4.50	8/76
Cincinnati	3.50	4/76	St. Louis	6.52	2/76
Los Angeles	4.25	2/74	Pittsburgh	4.50	7/76
Philadelphia	8.07	7/76	Boston	7.00	7/76
Detroit	7.00	7/76			

(15) In the last two years, has the city ever been unable to place all of a bond issue? If so, why do you think this problem occurred?

Responses: Chicago and Detroit were the only two answering affirmatively and said that they were unable to sell at an acceptable interest rate because of the New York City situation.

Appendix IV

Key Sources Used --

Historical Disclosure Recommendations and the Summary of Reporting Practices

Table A-IV-(1)

Summary of Reporting Practices (in a Survey of Official Statements)

	Type of Information	Number of Statements: Reporting	Number of Statements: Not Reporting	Number of Statements: Not Relevant
(1)	Statement of Direct Debt Outstanding Dated within 120 Days of Sale Date:	149	25	-
(2)	Direct Debt Statement Dated in 1975:	165	9	-
(3)	Statement of Overlapping Debt Dated in 1975:	138	20	16
(4)	Statement of Direct Debt for Prior 5 Year Period:	7	167	-
(5)	Statement of Annual Debt Service Requirements for all Direct Debt			
	(A) Principal Only:	66	108	-
	(B) Principal and Interest:	36	138	-
(6)	Audited Financial Reports:	17	157	-
(7)	Accounting Methods Identified:	7	167	-
(8)	Operating Statement of Revenues and Expenditures for Most Recent Completed Fiscal Year:	44	130	-
(9)	Detailed statement or Explanation of Sources of Revenues and Expenditures:	25	149	-
(10)	Current Year Assessed Valuation of Taxable Property:	139	22	3
(11)	Current Property Tax Rate:	109	60	5
(12)	1975 Population:	110	64	-

Table A-IV-(1) (cont.)

	Type of Information	Number of Statements: Reporting	Not Reporting	Not Relevant
(13)	1970 Population:	114	60	-
(14)	Data on Number of Employed Persons in Major Employment Categories:	10	164	-
(15)	Data on Level or Rate of Unemployment:	4	170	-
(16)	List of Major Industrial Firms Located in Area (with Employment Figures):	50	119	5
(17)	Personal Income Data			
	(A) Median Family Income -- Own Unit:	20	154	-
	(B) Median Family Income -- Standard Metropolitan Statistical Area:	3	168	3
	(C) Total Personal Income of Residents:	14	160	-

Source: (Taken directly from) Forbes, Professor Ronald. "Summary of Reporting Practices", as quoted in U.S. Congress, Senate. Committee on Banking, Housing, and Urban Affairs. Hearings before the Subcommittee on Securities on S. 2969 to Amend the Securities Exchange Act of 1934 to Require the Preparation of Annual Reports and Distribution Statement by Issuers of Municipal Securities, and for Other Purposes, S. 2574 To Amend The Securities Act of 1933 to Provide for the Registration of Securities Issued by State and Local Governments, February 24, 25, and 26, 1976. 94TH Congress, Second Session, Washington, D.C.: U.S. Government Printing Office. 1976, p. 271.

The Disclosure Recommendations of the 1951 New York City Report

Minimum standards prescribed:

(1) Description of community -- Population for four years (census or estimated); school census; area; citation of any special charter; type of community in which bond issuer is located; and public and private facilities in the area.

(2) Trends for preceding five years -- Debt as to total amount, deductible items, and net debt; expenditure by major character classes; assessed valuation of real estate (personal property exempt); state equalization ratio of assessed to full value; real estate tax rate and levy; other revenue, by major class.

(3) Selected tax detail -- Three-year record of property tax collections and delinquencies; description of tax collection machinery, especially regarding delinquencies, penalties, and tax sales; itemization of local nonproperty tax revenue for three years.

(4) Assets of funds -- As of specified dates, assets of sinking, capital reserve, repair reserve, tax stabilization, debt reserve, and other funds.

(5) Bond principal maturities -- Amounts maturing in each of next ten years, excluding and including the bond issue to be sold.

(6) Revenue producing enterprises -- Confined to showing (a) principal maturities for such enterprises excluded by State Comptroller's approval from debt subject to limitation.

(7) Finances of overlying or related units -- For large cities fiscally responsible for shcools, a separate itemization of school debt, expenditure, debt service, and taxes; itemization of net debt of special districts situated in a city, village, or town; special improvement district debt included in town debt; optional reporting of debt and tax records of all other overlying school and special districts.

(8) Other information -- Statutory authority for the purpose for which bonds are to be issued; statement whether any debt principal or interest is past due; statement whether procedure for validation of bonds has been or is to be complied with.

Source: (Taken directly from) Advisory Commission on Intergovernmental Relations. "State Technical Assistance to Local Debt Management". Washington, D.C.: U.S. Government Printing Office, 1965, pp. 37-38.

The Disclosure Recommendations of the

1963 IBA Format

REPORT ON FINANCES - MUNICIPAL GENERAL OBLIGATION BONDS

Municipality or political subdivision ______________________________
County ____________________ State ____________________

Form of Government (Commission, Mayor-Council, Manager, etc.) ____________________
Fiscal year begins ____________________
U. S. Census 19__: __________ State Census 19__: __________ Present Estimate: __________
Has this issuer defaulted on any debt obligation since 1930? ___
If so, give full particulars in a separate statement.

Part 1. Property Valuation (as of __________ 19__)

	Current Year: Assessed	Current Year: Actual	Current Year: Ratio of assessed to actual value	Previous Year: Assessed	Previous Year: Actual
1. Real estate	$	$	%	$	$
2. Personal property					
3. Public utility					
4. Other (specify) ____________					

Part 2. Bonded Debt and Related Information (as of __________ 19__)

	Amount	Sinking Funds
1. General obligations (not listed below)	$	$
2. Special assessments secured also by general tax		
3. Utility and public enterprise debt secured also by general tax:		
(a) Water		
(b) Sewer		
(c) Light and Power		
(d) Other (specify)		
Total General Obligation Bonds		
4. Special assessments only		
5. Utility and public enterprise revenue only:*		
(a) Water		
(b) Sewer		
(c) Light and Power		
(d) Other (specify)		
Total Other Than General Obligations		

*For utility and other public enterprise revenue bonds, please submit separate reports on report form for municipal revenue bonds.

6. Legal debt limit of this issuer? __% of (describe base) ____________________; $________
7. Debt outstanding chargeable to debt limit? $________ Unused borrowing margin? $________
8. Bonds authorized but not issued: Purpose ____________________ Amount $________
9. Are utility and public enterprise bonds reported in item 3 fully supported by earnings of the facilities? ___ If not, what proportion of general taxes was necessary for debt service on such bonds in the last fiscal year? ____________
10. Total general obligation bonds outstanding year ago? $________ Two years ago? $________
11. Amount of refunding bonds issued within last two years for the following purposes:
    (a) To refund maturing bonds $____________ Maturities ____________
    (b) To refund callable bonds $____________ Maturities ____________

Part 3. Overlapping Debt

That Part of Debt of Overlapping Entities (School or Special Districts, Counties, etc.) Payable by Taxes Levied in this Municipality or Political Subdivision

Name of Overlapping Entity	Debt Limit %	Gross Debt Less Sinking Fund	This Issuer's Share
		$	$

(cont.)

Part 4. Unfunded Debt Outstanding

	Amount	Due
1. Tax Anticipation Notes	$	
2. Delinquent Tax Notes	$	
3. Bond Anticipation Notes	$	
4. Bank Loans	$	
5. Warrants	$	
6. Judgments	$	
7. Unpaid Bills 60 Days Past Due	$	
8. Miscellaneous Items	$	
Total	$	

9. Unfunded Debt One Year Ago $__________; Two Years Ago $__________

Part 5. Composition of Sinking Funds

1. Cash on hand or in banks	$
2. United States Government securities	$
3. Bonds of this municipality	$
4. Bonds of states and other municipalities	$
5. Other investments (specify nature)	$
Total	$
6. Amount of Term Bonds for Which Sinking Funds Are Required	$

Part 6. Debt Service Requirements For Next Five Years
(For principal, interest and sinking fund installments)

Authorized Source of Payment	Fiscal Year Beginning				
	19__	19__	19__	19__	19__
1. General Taxation	$	$	$	$	$
2. Special Assessments and General Taxation	$	$	$	$	$
3. Utility Revenues and General Taxation	$	$	$	$	$
4. Special Assessments Only	$	$	$	$	$
5. Utility Revenues Only	$	$	$	$	$

Part 7. Comparative Statement of Operating Revenues and Expenditures.
Do not include municipally operated utilities or public enterprises, unless surplus revenues therefrom are transferred to general fund (in revenues) or debt service on general obligations issued therefor are paid from general fund (in expenditures).

	Fiscal Year Beginning		
	19__	19__	19__
1. Cash Balance at beginning of year	$	$	$
2. Revenues:			
(a) Proceeds from notes and bonds	$	$	$
(b) From ad valorem taxes	$	$	$
(c) From other taxes	$	$	$
(d) From federal or state aid	$	$	$
(e) From other sources	$	$	$
Total Revenues	$	$	$
3. Expenditures:			
(a) Government operating expenses	$	$	$
(b) Expenditures from bond proceeds	$	$	$
(c) Bond principal	$	$	$
(d) Bond interest	$	$	$
(e) Sinking Funds	$	$	$
(f) All other purposes	$	$	$
Total Expenditures	$	$	$
4. Cash Balance at end of year	$	$	$

(cont.)

Part 8. Tax Data

(a) Tax Collection Report - Ad Valorem or General Property Tax
For last 3 years. For tax or fiscal year ending________
Omit levies of other entities and special assessments.

	Amount of Levy By This Issuer	Uncollected at End of Year	Uncollected Latest Available Date	Delinquent Taxes From Prior Years Collected During Year
19__	$________	$________	$________	$________
19__	$________	$________	$________	$________
19__	$________	$________	$________	$________

(b) Total Current Levy
For tax or fiscal year beginning________________
Include levies of other entities which are part of general property tax

		Amount Levied	Rate Per $100 of Assessed Value*
Total general property tax (or ad valorem tax) is composed of:	This Issuer	$________	$________
	School	$________	$________
	County	$________	$________
	State	$________	$________
	Other________	$________	$________
	________	$________	$________
	Total	$________	$________

*If any property included in your taxable assessed valuation is taxed at rate different from real estate, specify________________________________

(c) General Tax Information

1. Taxes for fiscal year are due:____________ Became delinquent:____________
2. If payable in installments give particulars________________________
3. Discounts for prepayment and when applied?________________________
4. Specific practice for delinquency?________________________
5. Explain in detail any modifications of practice during the past two years________
____
6. How are uncollected taxes handled?
   (a) Anticipated as revenue in next year's budget?___If yes, what percentage?______
   (b) Turned over to other governing bodies?____If yes, when?____________
   (c) Sale of tax certificates?____If yes, when?____________
   (d) Other methods________________________
7. Has tax sale period been extended in last two years?____If yes, explain________
8. Accumulated total of uncollected taxes for fiscal years prior to those reported above $__________
9. Are tax title liens included in uncollected tax totals above?______
   How much? $__________
10. Total tax title liens owned by municipality (years 19__to 19__inclusive) $________
11. Is there a tax rate limit?___How Much?________Statutory or Constitutional?________
12. Do tax rate limits apply to debt service?____If yes, what are the limits?________
13. Do you levy taxes in excess of actual requirements to provide margin against delinquences? Yes___No____
    If yes, what ratio? Current year?______%; Previous year?______%; 2 years ago?______

Part 9. Supplementary Information

Please furnish in a separate statement information regarding the location and economic background of the issuer, the general character of industries and transportation facilities in the area, and any other pertinent data or comments. If additional space is needed to report fully the information requested in this form, please attach separate sheets with appropriate cross references.

Signed________________________

Official Title____________________

Date________________________

Source: Advisory Commission on Intergovernmental Relations. "State Technical Assistance to Local Debt Management". Washington, D.C.: U.S. Government Printing Office, 1965, pp. 64-66.

The Disclosure Recommendations of the

1965 State Technical Assistance Report

Recommended for inclusion in all bond prospectuses:

(1) Legal authority and debt incurring power -- Common to all standard forms should be the citation of the legal authority to borrow and spend money for the purpose for which the bonds are to be sold. For general obligations, a summary of debt incurring power could be confined to a comparison of the amount permissible under the debt limit with the gross debt, allowable deductions, and net limited debt. The bond attorney's favorable opinion of the legality of the issue, even if preliminary, should be either cited or summarized.

(2) Summary of past financial trends -- To depict the trend the financial condition of the local unit is taking, the forms should summarize basic data for selected prior years by showing total debt as to character of liability, revenue and expenditure as to major category, total assessed and full valuation, property tax rates and levies, property tax collections and delinquencies, and the record as to any defaults or refundings to avert defaults. Trend data obviously differ among types of debt liability. Meaningful trends are disclosed by comparisons of the tenth and fifth previous years with the last two years.

(3) Detail for latest completed year -- The borrowing unit can readily report detail, provided it is confined to the latest year, and the credit analyst is helped by an itemization of outstanding issues, showing amount, purpose, interest rate, and principal and interest due. For a metropolitan center, however, the debt detail should be reserved for an accompanying annual report. For all borrowing units, the revenue side for the previous year requires itemization of each main source to reveal in particular the relative size of each nonproperty tax, and revenue from State and Federal governments classified as to use for operation, capital outlay, and debt service. On the expenditure side, the credit analyst needs to learn not merely aggregates by character (i.e. operation, capital outlay, etc.) but the extent to which responsibility has been assumed for individual functions in the previous year.

(4) Future trends -- Since the bonds to be sold will be paid in the future, many credit reports now set forth the future debt service on outstanding debt and on the bonds to be sold. While an itemization for all years during which bonds will mature has advantages, a listing for the next 10 years would be acceptable because of the likelihood that later issues will change the maturity schedule. In any States adopting plans for the review of prospective bond issues...the inclusion of a future capital budget would be feasible in all credit reports. In the absence of the adoption of the suggested plans, the credit report should (a) specify all bonds authorized but not issued, and (b) summarize all capital improvements and bond issues that are likely during the next six years. Indispensable to the

(cont.)

sale of revenue bonds is an engineering estimate for the next six years of revenue from the facility or service operating cost, other charges against revenue, and the anticipated surplus margin.

(5) Overlying, coterminous, and underlying local units -- Usually credit reports depict the net general debt, tax rate, and tax levy not only for the borrowing unit but for all units levying taxes on the property within the boundaries of the borrower. For municipalities and school districts, except county systems, the additional data are for shares of overlying units; for counties and county school districts, the added data are the totals for underlying units,and in some cases, usually municipalities and districts, added data may be for coterminous units.

In a simple governmental structure, the local officials alone can obtain the aggregate statistics. In complex structures, and especially for county brochures showing underlying units, the State agency should -- as for any other aspect of the credit report -- cooperate with the local officials by making data available form State files. With the increasing importance of local nonproperty tax revenue and intergovernmental revenue, a realistic report would set forth similar summaries of classified revenue and expenditure.

(6) Physical volume of services -- With standard forms tailored to fit types of government, liability, and selected functions, credit reports would acquire an added dimension by showing the physical volume of services. For example, the debt prospectus outline for the Michigan Department of Public Instruction calls for the concise analysis of present and future school building needs of a school district. Elementary and junior and senior high schools are separately reported as to capacity of (a) existing adequate school houses. (b) existing unsatisfactory school houses, (c) school houses under construction, and (d) school houses to be financed by proposed bond issues. Additional school houses required during the next two periods of five years are recapitualated as to number of buildings and classrooms, capacity, and estimated cost.

Utility services are reported as to physical volume in some, though far from all, credit brochures. Interyear comparions are feasible for electric power systems as to KWH's generated, purchased, and classified number of consumers. Highway and street mileage, classified by type of existing construction and compared with programs for future surfacing, may be summarized in many counties and cities.

(7) Economic characteristics of the community -- Local governments are handicapped in working up the necessary economic bace data for evaluating debt and fiscal loacs. While the typical prospectus shows assessed valuation (and should set forth estimated full valuation), the swing to nonproperty taxes now requires the reporting of other economic characteristics both for general obligations and revenue bonds. Conventional reporting involves the identification of chief industries, if possible by dollar value of production, and at times by the listing of the names and property value of the leading companies. Transportation facilities are often listed.

(cont.)

Among the assortment of data that have been urged for reporting and sometimes used to good advantage are retail and wholesale sales, service establishment receipts, consumption and number of consumers of publicly and privately owned utilities, and the number and value of building permits. Local nonproperty taxes and State taxes derived from the local community are often overlooked. Economic indicators are more often available on a countywide basis than for smaller areas.

To the customary reporting of total population for several Census years and an estimate for the latest year may well be added a classification by age group, school enrollment, and in some areas of the employment and unemployment rates. Mention of the area and density of population indicates the compactness of the jurisdiction and the probable extent of development of the area. Interyear comparisons, at times on a per capita basis, are helpful in evaluating the stability, volatility, and diversity of the economy, and prospect of economic growth of the community.

(8) <u>Quality of public administration</u> -- A debt prospectus can provide some clues as to the general character of the local government and the quality of its administration. Among these are: an indication of the nature of the local government organization and financial administration, especially as to accounting and debt management responsibility, the existence or absence of planning and zoning ordinances and agencies, the accounting basis (cash, accrual, or combination thereof), and tax and revenue collection methods and the handling of tax delinquency.

Source: (Taken directly from) Advisory Commission on Intergovernmental Relations. "State Technical Assistance to Local Debt Management". Washington, D.C.: U.S. Government Printing Office, 1965. pp. 41-43.

The Disclosure Recommendations of the

1976 MFOA Disclosure Guidelines

...These guidelines suggest disclosure of information that is most likely to be material to investors. It is possible that other information, not suggested herein, may at times be material and in such cases should be provided.

In addition to the information suggested, there should be added such further material information as may be necessary so as to make any statements made not misleading under the circumstances. Care should be taken to review the financial, historical, and other factual information as given so as to determine whether qualifications or additional information should be stated. If reliable information is available which indicates material changes in trends or other disclosures, such information should be presented....

In some cases certain specific suggested information will not be material under the circumstances. In such instances, there is no need to report... The degree of detail may be related to the term of the obligations...If reliable information is unknown and not reasonably available, the information may be omitted...Financial and accounting information should be prepared and presented in accordance with generally accepted accounting principles...

Furnish appropriate financial statements of the issuer, or in the case of an offering of revenue securities, the enterprise, to indicate the issuer's financial ability to fulfill its obligations to the holders of the securities being offered....Those financial statements reflecting assets and liabilities should be presented as of the end of each of the last two fiscal years, and those financial statements relating to operations should be presented for each of the last five fiscal years. In the case of an offering of revenue securities, interim financial statements reflecting assets and liabilities should also be presented as of a date within the last 120 days and as of the comparable date in the preceding fiscal year, and those financial statements relating to operations should be presented for the interim period between the end of the last fiscal year and the date of the interim financial statements reflecting assets and liabilities and for the comparable period of the preceding fiscal year. Receipts and assets which cannot be used to discharge the issuer's obligations to the holders of the securites being offered and expenditures chargeable against such receipts should be clearly indicated....

The financial information should reflect the retroactive adjustment of any material items affecting the comparability of the results. State the basis on which the financial statements have been prepared, such as a cash, accrual or modified accrual basis. Data for all undertakings which individually or together are material sources of payment for the principal of or interest on the securities being offered should be shown on a consolidated basis, and where informative, may also be shown separately for specific undertakings or groups of undertakings...

(cont.)

Disclose the effects in dollar amounts of extraordinary receipts or expenditures and describe the nature and purpose of the receipts or expenditures...

In connection with the financial statements, whenever necessary, reflect information or explanations of material significance to investors in appraising the results shown, including analyses of material increases or decreases in significant categories during the last two fiscal years and any comparative period.

In an offering of general obligation securities, if more than 15 percent of the receipts of the issuer in either of its two most recent fiscal years comes from a single enterprise owned or operated by the issuer (such as a public utility or transportation system), or a number of such enterprise(s) engaging in essentially similar functions or operating as a integrated enterprise, and if the receipts from such enterprise(s) may be used for payment of principal of or interest on the securities being offered, provide an appropriate financial summary regarding such enterprise(s).

If payment of principal or of interest or premium on the securities being offered is guaranteed or insured in any respect, furnish appropriate financial or other information as to the guarantor or insurer. Under normal circumstances, it is unnecessary to include more than a very brief financial summary as to a state guarantor...

Furnish the information called for by the following table as to appropriate categories of long-term and short-term securities and other indebtedness of the issuer (other than unpaid bills fewer than 90 days past due):
...

Category of indebtedness	Amount authorized	Amount outstanding as of (date) (less sinking fund installments paid to such date)	Amount to be outstanding

Debt should be regarded as "authorized" when all material discretionary legal steps have been taken by the issuer for its authorization for issuance, such as required approval of the city council council or the voters. Actions tending to be of a ministerial or judicial nature, such as validation in some jurisdictions, should not be regarded as discretionary for this purpose...

Furnish a debt service schedule for total principal, interest and premium requirements of the issuer under outstanding indebtedness, and where appropriate, under authorized indebtedness, to the final maturity date of all outstanding securities. Include debt service on the securities being offered. Indicate in footnotes to the schedule any assumptions, such as interest rates on authorized but unissued debt, on which information in the schedule is based. The schedule may be presented in substantially the following tabular form:

(cont.)

Fiscal year ending (date)	General obligation indebtednes	Special assessment indebtedness	Utility revenue indebtedness	Other indebtedness (describe)	Total

State the total amounts of indebtedness of the issuer outstanding as of the end of each of its last five fiscal years.

Describe any legal debt or tax limit of the issuer, the legal source of the limit, the indebtedness or tax rates of the issuer chargeable to the limit, and the unused borrowing or taxation margin. Describe legal requirements, such as voter approval, which must be met in connection with debt issuance.

If any refunding securities have been issued by the issuer within the last 25 years for the purpose of preventing a default in principal or interest payments on securities then outstanding, describe the circumstances giving rise to the issuance, including the amounts involved.

If any securities of the issuer have been in default as to principal or interest payments or in other material respects at any time in the last 25 years, state the circumstances giving rise to each default, including descriptions of the relevant provisions of the securities and authorizing and governing instruments and the amounts involved. State whether such default has been terminated or waived, and if so, the manner of such termination or waiver.

If any outstanding revenue, special assessment, or limited obligation securities have not been fully supported by earnings of the relevant facilities or by other relevant receipts at any time in the last ten years, state for each such year in which additional general receipts of the issuer were used or required to be used for payments on such securities, the amount due on such securities and the amount of such additional funds. Describe any contract or arrangement, such as a lease, services contract or deficiency subsidy agreement, requiring application of general tax or other receipts of the issuer for the benefit of other governmental entities.

If the proceeds from the sale of any securities (other than tax anticipation notes issued against revenues of a current fiscal year) have been used for current operating expenses at any time in the last ten years, describe the circumstances giving rise to such use, including the amount used in each of such years.

Describe briefly the issuer's or the enterprise's pension and other employee retirement plans and the methods by and basis (e.g. actuarial or "pay-as-you-go") on which the plans are funded. State the issuer's or the enterprise's contributions to the plans for, and the unfunded accrued pension liability as of the end of, each of the last five years. State the annual

(cont.)

benefit payments, net of employee contributions and interest earnings of the plans, for each of the last five fiscal years, unless the plans are fully funded. State the date of the most recent actuarial study, if any, and describe briefly the assumptions upon which the study was based. If contributions are made on an actuarial basis, state the year in which such basis was first used to determine contributions prior to such times have been eliminated.

Describe briefly the manner in which property valuations and assessments are determined and principal taxes are levied and collected. Include descriptions of (i) the manner in which delinquent taxes are collected; (ii) the interest charged on delinquent taxes; (iii) important changes during the last five fiscal years and as of a recent date. Describe briefly the procedures followed in foreclosure, including extension of foreclosure dates. Describe the priority of tax claims of the issuer over other indebtedness of taxpayers.

Give in tabular or other appropriate form with respect to the issuer as of the end of each of its last five fiscal years and as of a recent date, information as to (i) its assessed valuation of taxable real property; (ii) its estimated true valuation of taxable real property; (iii) its assessed valuation of taxable personal property; (iv) the assessed valuation of taxable real property expressed as a percentage of the estimated true valuation thereof. Segregate such information as to industrial, commercial, utility and residential properties.

Give information as of the end of each of the isssuer's last five fiscal years andas of a recent date in respect of the issuer's (1) debt per capita; (ii) debt expressed as a percentage of total assessed valuation of taxable real and personal property; (iii) debt expressed as a percentage of estimated per capita income of individual taxpayers residing in the jurisdiction.

State whether real estate, sales, income or other taxes are levied in excess of actual requirements to provide a margin against delinquencies and, if so, give the amount of such excess taxes expressed as a percentage of total taxes levied for the issuer's last fiscal year. State in tabular or other appropriate form the total tax levy and the accumulated amount of delinquent taxes as of the end of each of the issuer's last fiscal year. State in tabular or other appropriate form the total tax levy and the accumulated amount of delinquent taxes as of the end of each of the issuer's last five fiscal years and as of a recent date and the tax delinquency rate for each of such fiscal years and for the current fiscal year to date. Describe any anticipation of collection of delinquent taxes in budgets for current or future years. State whether borrowing is made against delinquent taxes, and if so, state the percentage of delinquent taxes so financed as of the end of such prior fiscal years and as of a recent date. Describe the accounting principles applied in writing-off delinquent taxes, and state the period for which delinquent taxes are reflected on the issuer's books before they are written off.

Name every taxpayer providing through tax payments more than 10% of the tax receipts of the issuer in the issuer's most recent fiscal year. State the amount of taxes levied against each such taxpayer and the percentage of

(cont.)

the total tax levy represented by such amount.

Furnish the information called for by the following table as to indebtedness of overlapping governmental entities.

Name of overlapping entity	Amount of authorized debt as of (date)	Amount of outstanding debt (less sinking fund) as of (date)	Percent of outstanding debt chargeable to persons or property in issuer's boundaries

.....

State the year in which the issuer was established, give the name of the state or other jurisdiction under the laws of which it was established, describe its form of government, such as mayor-council or city manager, and if the issuer is a municipality, state the county in which it is located....

State the principal purposes for which the net proceeds of the offering are authorized or proposed to be used and the approximate amount authorized or proposed for each purpose...

If any material amounts of other funds are to be used in conjunction with the proceeds, state the amounts and sources of such other funds...

Sufficient information should be given to provide background and general information concerning the issuer. At times, data on other population areas in the issuer's vicinity may be informative, either in addition to or, where information on the issuer is unavailable, in subsitution for information on the issuer. Investors should be informed of factors which indicate the ability of the issuer to impose and collect, and the ability of its citizens to pay, taxes and other receipts which can be used to discharge the issuer's obligations. Certain trends provide useful indications in these regards. Factors which may have a significant, though indirect, effect on these trends, such as the types and levels of services provided by the issuer and demands for services, may also be helpful. In many cases, information suggested in this Section is available in reports of the U.S. Government. Indicate information obtained from sources other than the issuer. Examples of the types of information which may be appropriate when reliable and reasonably available are:

(1) The last official estimate, and the most recent estimate, of the issuer's population, school enrollment, per capita income, median age, and unemployment rate, and the number and value of residential and nonresidential contruction permits issued during each of the issuer's last five fiscal years and the current fiscal year to date.

(2) A brief statement or description of (i) the principal industries and commerical entities in the issuer's immediate geographical area; (ii) the number of persons employed by such industries or entities; (iii) the economic stability of such industries or entities; and (iv) the economic effects of any addition or loss or major industrial or commercial entities in

(cont.)

the last five years.

(3) A brief description of (i) the principal governmental services performed by the issuer; (ii) the extent to which similar or differing governmental services are performed by overlapping governmental entities; and (iii) major changes in such services in the last five years...

State briefly the general character of the principal facilities of the issuer...If any such property is leased or otherwise not held in fee or is held subject to any major encumbrace, so state and briefly describe how held....

Briefly describe any pending legal proceedings to which the issuer... is a party or to which any of its property is subject and which may materially affect the issuer's ability to perform its obligations to the holders of the securities being offered...Include the name of the court or agency in which the proceedings are pending, the date instituted, the principal parties thereto, a description of the factual basis alleged to underlie the proceedings, and the relief sought. Include similar information as to legal proceedings which have been threatened to a degree which constitutes a material possibility that they will be instigated. An opinion of counsel with respect to such legal proceedings may, with the consent of counsel, be included or summarized in the official statement. State the name and address of such counsel.

Describe the manner in which the governing body and executive officials of the issuer...are chosen, their respective terms, the general means by which policy and executive decisions are made on behalf of the issuer... and the parties possessing the authority to make such decisions. Name each executive official...

Describe briefly any priority of claims available to citizens in respect of services performed by the issuer, to employees in respect of wages, or to any other party which would require expenditures of funds of the issuer prior to payment of principal of or interest or premium on the securities....

State all ratings of the securities being offered and the names of the rating agencies. If the ratings are provisional, that should be stated. In addition, there should be stated ratings of any other outstanding securities of the issuer secured similarly to the securities being offered. If no ratings have been obtained on any such securities, a statement should be made to such effect. Changes in any ratings of any securities of the issuer during the preceding two years should be described.

Source: (Excerpted from) Municipal Finance Officers Association, "Disclosure Guidelines for Offerings of Securities by State and Local Governments", Chicago, Illinios: MFOA, (November 10, 1975). (Recommendatons for disclosure of information pertaining to revenue bonds, enterprise finance, and security provisions not cited here.)

The Proposed Disclosure Requirements of the

1976 Williams-Tower Bill

Sec. 13A (a)(1) Any issuer of municipal securities which has outstanding during any portion of a fiscal year an aggregate principal amount of municipal securities exceeding $50,000,000 shall prepare for such fiscal year an annual report and reports of events of default in accordance with such rules as the Commission may prescribe as being necessary or appropriate in the public interest or for the protection of investors.

"(2) The annual report required by paragraph (1) shall contain the following information, if applicable:

"(A) An identification and description of the issuer of the securities outstanding;

"(B) A description of any legal limitation on the incurrence of indebtedness by the issuer or the taxing authority of the issuer;

"(C) A description of the issuer's debt structure, including information with respect to amounts of authorized and outstanding funded debt, estimated amount of short-term debt, character of amortization provisions of funded debt, sinking fund requirements, security for debt, nature and extent of guaranteed debt, and debt service requirements;

"(D) A description of the nature and extent of other material contingent liabilities or commitments of the issuer;

"(E) If any payment of principal or interest on any security of the issuer or any predecessor thereof has been defaulted on, or has been postponed or delayed, within the past twenty years, a description of the date, amounts, and circumstances of such event and of the terms of any succeeding arrangements thereof;

"(F) A description of the issuer's tax authority and structure over the past five years including the nature of taxes levied, tax rates, property (real and personal) valuation and assessments, amounts of tax levies, amounts of tax collections and delinquent tax procedures and experience;

"(G) A description of the issuer's major taxpayers;

"(H) A description of the principal governmental and other services provided or performed by the issuer, the extent to which similar or differing services are performed by other governmental entities which serve the same geographic area and any major changes in such services in the last ten years;

"(I) A description of the nature and extent of Federal or other assistance programs available to the issuer;

"(J) Financial statements of the issuer in such detail and form and for such periods beginning not earlier than the fifth previous fiscal year as the Commission may prescribe, which statements for any fiscal year commencing on or after December 31, 1978 shall be audited and reported on by an independent public or certified accountant in such manner as the Commission may prescribe.

"(3) The reports of events of default referred to in paragraph (1) shall contain such of the information required by paragraph (2) as the Commission may by rule or regulation prescribe.

(cont.)

"(4) The reports required by paragraph (1) shall, in addition, contain such other similar and specific information as the Commission may by rule or regulation prescrive as being necessary or appropriate in the public interest or for the proection of investors.

"(b)(1) Except as provided in subsection (c), any issuer that offers or sells an issue of municipal securities, the aggregate principal amount of which exceeds $5,000,000 to or through a municipal securities broker, municipal securities dealer, or bank acting acting as agent, shall, prior to such offer or sale, prepare a distribution statement in accordance with such rules and regulations as the Commission may prescribe as being necessary or appropriate in the public interest or the protection of investors.

"(2) The distribution statement required by paragraph (1) shall contain such of the information pertaining to the issuer required by subsection (a)(2) as the Commission may by rule or regulation prescribe, and the following:

"(A) A description of the offering, including amount to be offered, price, plan of distribution, and underwriting arrangements and compensation;

"(B) A description of the security to be offered, including provisions as to security, events of default, payment of principal and interest, sinking fund, redemption, debt reserve funds, priority, legality and authorization for issue and rights of security holders to bring suit against issuers;

"(C) A description of any project or enterprise of the issuer to be financed from the proceeds of revenue or special assessment securities, and any engineering or financial flexibility reports or studies on the construction and operations of the project or enterprise;

"(D) A description of the intended use of the proceeds of the offering;

"(E) A statement of counsel's opinion as to the legality of the issuance of the securities to be offered;

"(F) A statement of the availability of the reports required by this section; and

"(G) Such other similar and specific information as the Commission may by rules or regulations require as necessary or appropriate in the public interest or for the protection of investors; except that, prior to any sale, the information specified in subparagraphs (A), (B), and (E) may be set forth in preliminary form.

"(C) The provisions of subsection (b) shall not apply to an issuer soley by reason of an offer or sale of municipal securities --

"(1) the disclosure with respect to which has been approved, after hearing, as adequate for the protection of investors by a State governmental authority (other than the issuer) expressly authorized by law or granted such approval, or

"(2) which would meet the criteria set forth in sections 3(a)(9), 3(a)(10), 4(1), 4(2), 4(3), 4(4) of The Securities Act of 1933 if such offer or sale were not within the scope of section 3(a)(2) thereof.

"(d) The Commission may from time to time by its rules and regulations, and subject to such terms and conditions as may be prescribed therein, change the minimum amounts set forth in subsections (a)(1) and (b)(1) if, giving due regard to such factors as general economic conditions, costs involved, and the nature of the distribution system for municipal securities, such change is deemed to be appropriate in the public interest;

(cont.)

"(e) The Commission may prescribe, in regard to reports and distribution statements made pursuant to this section, the form or forms in which the required information, including the financial statements, shall be set forth, and the accounting methods to be followed in the preparation of financial statements.

"(f)(1) The issuer shall make the reports required by subsection (a)(1) of this section available upon request to security holders at the issuer's expense and to others at their expense and shall give appropriate public notice of such availability.

"(2) The issuer shall make the distribution statement required by subsection (b)(1) of this section available to municipal securities brokers, municipal securities dealers, and banks acting as agent for delivery to prospective purchasers in accordance withsuch rules and regulations as the Commission may prescribe in the public interest or for the protection of investors.

"(3) The reports and distribution statement required by this section shall also be maintained by the issuer at a designated location for examination by the public in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors. The Commission may also contract to establish a central repository which shall receive and maintain such reports, and may require the contractor to adhere to such rules and regulations as the Commission may prescribe in furtherance of the purposes of this section. Each person subject to the requirements of this section shall, upon the establishment of any such repository, thereafter file copies of reports and distribution statements required to be prepared by this section with the repository in accordance with such rules and regulations as the Commission finds are necessary or appropriate in the public interest.

"(g) In no event shall any underwriter of an issue of municipal securities (unless such underwriter shall have knowingly received from the issuer for acting as an underwriter some benefit, directly or indirectly, in which all other underwriters similarly situated did not share in proportion to their respective interest in the underwriting) be liable in, or as a consequence of, any suit for damages in excess of the total price at which the issue was sold by it to the public."

Source: (Taken directly from) U.S. Congress, Senate. Committee on Banking, Housing, and Urban Affairs. Hearings before the Subcommittee on Securities on S. 2969 to Amend the Securities Exchange Act of 1934 to Require the Preparation of Annual Reports and Distribution Statements by Issuers of Municipal Securities, and for Other Purposes, S. 2574 to Amend the Securities Act of 1933 to Provide for the Registration of Securities Issued by State and Local Governments, February 24, 25, and 26, 1976. 94th Congress, Second Session, Washington, D.C.: U.S. Government Printing Office, 1976, pp. 5-13.

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