

SUPREME COURT : STATE OF NEW YORK
COUNTY OF ALBANY

LEE BORDELEAU, et al.,

Plaintiffs,

**PLAINTIFFS' REPLY
MEMORANDUM
OF LAW**

Index No. 6582-08

-against-

The STATE OF NEW YORK, et al.,

Defendants.

INTRODUCTION

These conclusions can be drawn from a review of the defendants' answering papers:

1. There is no appellate case that holds that cash grants to private firms for economic development are constitutional.
2. The defendants have nothing to say about the legislative history of the ban on giving state funds to private firms.
3. The defendants have told the Court what the Constitution doesn't ban but have not told the court what the Constitution does ban.
4. The defendants apparently think this is a condemnation case.
5. The defendants cannot explain why eminent legal scholars thought it necessary to amend the Constitution in 1967 to legalize cash grants to private firms for economic development.

Since there is no binding case law, the Court should base its ruling on the plain language of the Constitution and its undisputed historical background. There is no denying the fact that Article VII, § 8, paragraph 1 was prompted by the disastrous consequences of state subsidies to private firms for economic development in the early part of the 19th Century. Ignoring that evidence, the defendants now boldly ask the Court to ignore that constitutional history.

The defendants also ask the Court to ignore the plain language of the Constitution. They spend little time parsing that language. Rather, they simply pretend it doesn't exist. There is an analogy between this case and *District of Columbia v. Heller*, 554 U.S. ____ (2008). I had told my college-level constitutional law class in the fall of 2007 that the Supreme Court would uphold an individual right to bear arms because no court would so blatantly disregard the plain language of the Constitution. The Supreme Court would not say that the "right of the people to bear arms" means that the people do not have the right to bear arms. Similarly, this Court should not sign an order that says, in effect, that the words "The money of the state shall not be given or loaned to or in aid of any private corporation or association, or private undertaking" *really mean* that the money of the state may be given to private undertakings.

If, based on no clear appellate holding, the defendants are asking this Court to ignore the plain language and plain history of the Constitution, what authority do they cite? Eminent domain cases. *Yonkers Community Dev. Agency v. Morris*, 37 NY 2d 478, 483 (1975); *NYS Urban Development Corporation v. Vanderlex*, 98 Misc. 2d 264, 269, 272-274 (Sup Ct NY Co1979); *Waldo's v. Village of Johnson City*, 74 NY 2d 718 (1989). Obviously, this case is not about condemnation of private property. There are explicit constitutional provisions that govern litigation over eminent domain. Both the state and federal constitutions require that the courts find a "public use" before allowing a taking of private property. U. S. Constitution, 5th and 14th

Amendments; N. Y. Constitution, Article 1, § 7, (a). Thus, it is no surprise that in condemnation cases, courts determine whether a public purpose exists. They must do so by explicit constitutional direction!

Here, the opposite condition prevails. Not only is there no constitutional mandate to find a public use or purpose, *but the provision in question omits such a requirement*. By omission, the Constitution implicitly forbids the superimposition of such a requirement as that would constitute amendment of the constitution by judicial fiat. *People v. Westchester County Bank*, 231 NY 465, 474-475 (1921).

Only one defendant addresses our point about the 1967 Constitutional Convention and that defendant, International Business Machines, misses the point. It doesn't matter why the voters rejected the proposed amendment allowing for cash grants to private firms for economic development. What matters is they did reject it. And what matters even more is that eminent legal scholars of the time believed it was necessary to amend the Constitution to allow for such subsidies that had been previously and clearly banned by the Constitution of 1846 and subsequent amendments.

In addition to the failed amendment of 1967, there is other persuasive circumstantial evidence that grants are illegal under New York law. First, the general rule against grants is subject to an exception directly related to economic development. Article VII, Section 8(3) allows the state to loan money for economic development under certain circumstances. If there was not a general prohibition on corporate subsidies under paragraph 1, there would have been no need to carve out an exception for certain types of loans.

Also, several cases or formal opinions have held that *federal funds* may be given to private firms. *Kradjian v. City of Binghamton*, 104 AD2d 16 (3rd Dept. 1984); *Tri-County*

Taxpayers Association, Inc. v. Town of Bolton, 165 AD2d 451 (3rd Dept. 1991); Opinion of the State Comptroller No. 76-18 (1976); Opinion of the State Comptroller No. 88-79 (1988). Again, this exception reinforces the main rule that bars the use of *state funds* for corporate subsidies.

I. THE STATE MAY NOT USE PUBLIC CORPORATIONS TO FUNNEL FUNDS TO PRIVATE FIRMS FOR ECONOMIC DEVELOPMENT.

The defendants' main argument on appeal is that the state may use a public corporation as a middle man to dole out grants that the state itself could not. Not only do they cite no appellate case that says so but this tactic runs afoul of the principle that the Constitution may not be evaded by indirect means. See, *Wein v. State of New York*, 39 NY2d 136, 145 (1976). It also ignores key language in the Constitution itself. The Constitution states that "The money of the state shall not be given or loaned to or in aid of any private corporation or association, or private undertaking. . . ." Article VII, § 8, paragraph 1 (emphasis added). The words "in aid of" foreclose the tactic of giving money to a public corporation for the benefit of private firms.

The State should not be allowed to create entities so that constitutional mandates can be avoided. For example, the State should not be allowed to create a public corporation to run court operations so that the Bill of Rights need not be respected.

Advance Micro Devices, Inc. argues that the activities of the UDC in this context are justified by Article XVIII of the Constitution. That Article, however pertains only to low-income housing and nursing homes and it states:

"nothing in this article contained shall be deemed to authorize or empower the state, or any city, town, village or public corporation to engage in any private business or enterprise other than the building and operation of low rent dwelling houses for persons of low income as defined by law, or the loaning of money to owners of existing multiple dwellings as herein provided." (Section § 10).

Finally, the defendants' argument is refuted by Article VII, § 8, paragraph 3 which allows the legislature to loan the money of the state to a "public corporation" to make loans to private firms for economic development. Clearly, the drafters and ratifiers of this provision believed that the state's use of a public corporation middle man for economic development loans *had previously been illegal*. Obviously, the Constitution has never been amended to allow for *cash grants* to public corporation middlemen though they did try to do so in 1967.

II. THE BAN ON GIVING THE MONEY OF THE STATE SHOULD NOT BE NARROWLY CONSTRUED.

The defendants argue for a narrow interpretation of the term "give" such that only actual common law gifts are banned. However, the text of the constitution uses the term "give," not "gift," which has a narrower definition. The use of the phrase "in aid of" also requires a broad interpretation of this clause. Even if there was slight and contrived consideration for a grant of millions of dollars to a private firm, such grant would nevertheless be "in aid of" such firm and therefore barred. The essence of improper giving is the "subsidization" of private undertakings. *Schulz v. McCall*, 86 NY2d 225, 233 (1995). The fact that "loans" are also barred demonstrates that the constitutional ban is broadly intended to end state subsidies to private business, whether or not there is a token of "consideration" under contract law. See, *People v. Westchester County Bank*, 231 NY 465, 483 (1921), Judge Cardozo (dissenting) ("The purpose was to put an end to the use of the credit of the state in fostering the growth of private enterprise and business.")

Likewise, the mere fact that grant recipients sign contracts that impose certain obligations on them does not rescue such grants from the constitutional prohibition. For example, in *Schulz v. McCall*, *supra*, the mere fact that a partisan newsletter contained some valuable and nonpartisan

information for voters—the “consideration”--did not save that expenditure from being deemed unlawful under Article VII, Section 8 (1).

Neither does the history of the clause support the defendants’ interpretation. Surely, the loans that the State gave to private firms in the 1830’s and 1840’s that led to economic chaos and to the enactment of the initial ban on the use of the state’s credit for private purposes, were governed by written contracts that featured consideration such that they would not be deemed to be “gifts.” See, “Problems Relating to Taxation and Finance,” New York State Constitutional Convention Committee (1938), Volume X, page 107. Like the present grants, those transactions contemplated the improvement of the economy by developing railroads and canals and other infrastructure. Thus, the defendants urge upon the Court a meaning of the clause that ignores its original purpose and negates its meaning.

III. THE DEFENDANTS HAVE FAILED TO DEMONSTRATE THAT CASH GRANTS TO PRIVATE FIRMS SERVE A PUBLIC PURPOSE.

The defendants ask the Court to find that economic development grants serve a public purpose. However, they fail to provide any expert testimony to that effect. Their primary proposed witness is Douglas G. Wehrle, an employee of Empire State Development Corporation. He fails to state his qualifications to opine on economics and a Google search has failed to disclose any information that would shed light on his qualifications.

The Court should totally disregard his vague and unsupported opinions as to the beneficial effects of economic development grants.

The plaintiffs, in contrast, have retained Professor Thomas J. DiLorenzo, a professor of economics at Loyola College in Maryland as an expert witness. Professor DiLorenzo is one of the leading economic historians in the United States and also has expertise in the area of

economic development and corporate subsidies. He is presently traveling and we are asking the Court for permission to submit his affidavit by Monday, October 13th.

IV. THERE IS AN ISSUE OF FACT WHETHER CASH GRANTS TO PRIVATE FIRMS SERVE A PUBLIC PURPOSE.

If the Court holds that the defendants have provided sufficient evidence of a public purpose, we will, on the submission of an affidavit by Professor Thomas DiLorenzo, ask the Court find triable issues of fact in that regard. I anticipate that Professor DiLorenzo will submit his expert opinion that such grants actually harm the economy. We would request a trial to present that evidence and other evidence that will show there is no public purpose here, simply a transfer of wealth from taxpayers to private firms that leaves the economy in worse condition. See, *Denihan Enterprises, Inc. v. O'Dwyer*, 302 NY 451, 459-460 (1951).

V. THE COMPLAINT SHOULD NOT BE DISMISSED FOR FAILURE TO JOIN NECESSARY PARTIES.

The State defendants ask the Court to dismiss the complaint with respect to certain grant recipients not named as parties. Plaintiffs do not seek any relief with respect to funds already disbursed to those entities. With respect to promised grants not already disbursed, it is our position that those entities are not necessary parties. Even if they are deemed to be necessary parties with respect to grants “in the pipeline,” the remedy is not dismissal but leave to amend the pleadings if we choose to do so. In no event, however, would this issue affect the Court’s ability to grant an injunction against future grants. Obviously, the recipients of future grants, by definition, are unknown and could not be deemed to be necessary parties.

The State’s brief states:

“Obviously, a determination by the Court that an entity named in the complaint but not made a party to the action directing that entity to disgorge funds owed for goods and services rendered could inequitably affect those entities and their operations.”

However, plaintiffs do not seek that relief. *We do not seek the return of funds given to any non-party.* Our primary concern in this case is not return of funds but a ban on subsidies in the future. With respect to that issue, we have joined all the parties that could be joined. Of course, this case has been well-publicized in the media and there is nothing stopping interested groups, companies or individuals from moving to intervene or to file *amicus curae* briefs.

VI. THE COMPLAINT STATES A CAUSE OF ACTION AGAINST INTERNATIONAL BUSINESS MACHINES.

The defendant International Business Machines (IBM) claims that there are insufficient allegations in the complaint to sustain an action. The complaint states:

“41. It has also been reported that the Hyatt Hotel in Buffalo (WEST GENESEE HOTEL ASSOCIATES) and INTERNATIONAL BUSINESS MACHINES CORPORATION (IBM) will be receiving large grants from the state budget or from state funds.

“42. Though we cannot find such grants in the current state budget and two freedom of information requests to state agencies were ignored, these grants are apparently in that category of grants that are not disclosed in the state budget. (See, paragraphs 57-68 below.)

Since the State violates its own constitution in failing to specify grant recipients in their budget, and its economic development agencies tend to ignore FOIL requests, the lack of availability of more information in this regard is no surprise. Nevertheless, there is an allegation in the verified complaint that IBM will be receiving large grants. In their reply papers, they make no effort to deny this and they demonstrate that they are fully capable of defending this case even at the pleading stage.

It turns out that our verified complaint was correct. The affidavit of Douglas G. Wehrle submitted on behalf of the State Defendants, states:

“40. International Business Machines Corporation -- **\$65,000,000** W285 Capital Grant Incentive Proposal accepted July 2008; ESDC Directors approval anticipated in September 2008. No disbursements to date. IBM, The Research Foundation for State University of New York on behalf of the College of Nanoscale Science and Engineering of the University at Albany Nanotech Complex ("CNSEIANT"), and NYS intend to expand nanotechnology research, development and manufacturing activities within the State of New York in the form of substantial on-chip (semiconductor) and off-chip (packaging) related investment at IBM's East Fishkill facilities and at CNSEIANT. IBM will invest \$1.5 billion in semiconductor & packaging capital and research & development

expenses in New York State from 2008 through 2011 to expand IBM and NYS's leadership in nanotechnology. IBM will retain 1,400 semiconductor positions at the East Fishkill facility. Without ESDC assistance, the East Fishkill site may not have been chosen for this significant investment, which instead could have been made in competitive locations in Canada, Europe or Southeast Asia.” (emphasis added).

The budget appropriations are as follows:

Current Commitment:

New York State committed **\$140 million** to support the construction of a wafer packaging facility and continued research and development efforts between Albany Nanotech (ANT) and IBM. The State's investment of \$140 million will leverage a \$1.54 billion investment by IBM, and result in the creation of at least 675 jobs at the Wafer Packaging Facility; 325 jobs at Albany Nanotech; and retention of 1400 jobs at IBM's East Fishkill facility.

The budget appropriations are located in A.9803, page 882 lines 2-21 and page 884 lines 17-27.

Historical Commitments:

2000 Deal:

IBM invested over \$2.5 billion to construct a new semiconductor manufacturing plant in the Hudson Valley Research Park (HVRP) in East Fishkill, which resulted in the creation 1,000 new jobs and retention 5,048 through 12/31/04. As a result of this investment, IBM was eligible to receive the following:

- Up to \$475 million in Empire Zone credits; however, employment reductions elsewhere in the State (notably the divestiture of their Binghamton operation) resulted in no Empire Zone real property credits being claimed.

- **\$28.75 million** in grants and loans from a variety of State sources to IBM and Dutchess County. ESDC provided direct incentives of \$17.5 million and the remaining \$11.25 million was provided through Environmental Facilities Corporation (EFC's) Pipeline for Jobs program.

- Up to \$156 million in local tax benefits/exemptions. State has no documentation on these benefits, as it was benefits offered to IBM by the Town of East Fishkill and Dutchess County.

2005:

New York State provided **\$150 million** to establish the Center for Semiconductor Research, a joint partnership between IBM and Albany Nanotech. As part of the State's \$150 million commitment, IBM received \$130 million for the expansion of their East Fishkill facility and Albany Nanotech received \$20 million for equipment purchases.

The budget appropriations are located in A.9805, page 840, lines 16-29, New York State Economic Development Program (NYSEDP). See attached MOU.

41. International Computer Chip Research and Development Center--

\$300,000.000

Background: New York State provided \$300 million towards the \$600 million expansion of SEMATECH, the international consortium of semiconductor manufacturers, existing research and development program at the Center of Excellence in Nanoelectronics and Nanotechnology at the University at Albany

Nanotech Complex. The expansion will firmly establish New York as a global leader in research and development of the next generation of computer chips. New York State's \$300 million will be made available over five years to help SEMATECH purchase advanced semiconductor process equipment, and result in the creation of 450 new jobs and retention of 250 jobs establish as part of the 2003 SEMATECH North agreement.

State Funding: \$300 million in Capital funding approved by the Legislature in May 2007 to purchase of machinery and equipment for use by SEMATECH and Albany Nanotech. The budget appropriations are located in A.9805, Page 830-31, line 39-45 and 1-5.

VII. THE STATE BUDGET VIOLATES THE CONSTITUTION BY FAILING TO SPECIFY THE SUM APPROPRIATED AND THE PURPOSE OF THE APPROPRIATION.

The defendants argue, based on *Saxton v. Carey*, 44 NY2d 545 (1978), that the courts may not inquire into the degree of itemization in a budget. However, the same court states that the budgetary process is not always beyond the realm of judicial consideration. This is such a case as what we complain of here is the wholesale delegation of the power to appropriate billions of dollars to three state officials or their designees that results in *zero itemization!* This is the extreme case, the reduction to the absurd that, if not remedied, essentially erases the constitutional clause at issue, Article VII, § 7: appropriations should be limited to those authorized by “appropriation by law” that “distinctly specif[ies] the sum appropriated, and the object or purpose to which it is to be applied. . . .”

I invite the Court to carefully review the affidavit of Mr. Wehrle and especially its exhibits to see the full measure of shenanigans that the present practice leads to.

One example should suffice here. There is a memo from some fellow named Craig J. Miller from Senator Dale Volker’s office to Jeffrey Lovell of “Senate Finance” asking *him* or Senator Bruno to inform the Empire State Development Corporation that “the State Senate agrees to

commit \$1.7 million for the renovations of the Hyatt Regency Hotel in Buffalo...” That is simply incredible. Here is an unelected man unknown to the public directing the expenditure of state funds on behalf of an entity, the State Senate, that has no constitutional authority to make appropriations!

This is the extreme case where the courts must step in to halt this unconstitutional practice.

CONCLUSION

The Court should deny all motions to dismiss and should direct the defendants to answer the complaint and grant such other and further relief as the Court deems proper including an order expediting this proceeding.

Dated: Buffalo, New York
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