

**CITY OF MADISON
OFFICE OF THE CITY ATTORNEY
Room 401, CCB
266-4511**

Date: October 6, 2005

MEMORANDUM

TO: Members of the Board of Estimates

FROM: Anne Zellhoefer, Assistant City Attorney

RE: **OVERTURE DEVELOPMENT CORPORATION REFINANCING**

In June of 2001, Overture Development Corporation (“ODC”) borrowed \$115,000,000 through bonds issued by the Community Development Authority of the City of Madison (the “Bonds”) as part of the financing of Phase I construction of the Overture Center. Debt service on the Bonds, which is interest only until the Bonds mature in 2036, is the sole obligation of ODC; neither the City nor the CDA have any legal, contractual or moral obligation to pay debt service. ODC has secured repayment of the Bonds through a letter of credit which is further backed by the gift from W. Jerome Frautschi and additional temporarily pledged assets from Mr. Frautschi and from Overture Foundation (collectively, the “Pledged Assets”). The intent at the time of the Bonds’ issuance was that investment income from the Pledged Assets would be used to fund operating grants of up to \$1.4 million annually to support the Overture Center operations, beginning in 2004. To date, the Pledged Assets have not generated sufficient revenue, and no operating grants were made in either 2004 or 2005 to support the Center’s operations.

ODC has recently raised the possibility that it may redeem the Bonds in full before the end of 2005. ODC has also proposed an alternative scenario under which the Bonds would be refinanced, and in effect divided into a Series A (approximately \$87,000,000 of principal) and a Series B (approximately \$27,700,000 of principal). Under this refinancing proposal, parties in addition to ODC, including the City, would be responsible for paying debt service on the Series B bonds. In order to assist the Board of Estimates in analyzing and ultimately recommending a course of action, I’ve set forth below a summary of responses to the following questions.

1. What are the consequences to the City and the operation of the Center if ODC opts to pay the Bonds in full this year?
2. What happens if the City does not exercise its option to purchase the Center?
3. What is the effect of refinancing or early redemption of the Bonds on City employees who work on behalf of the District to operate the Center?

4. What happens to the District if the Bonds are paid in full and the City exercises its option to purchase the Center?

1. **What are the consequences to the City and the operation of the Center if ODC opts to pay the Bonds in full this year?**

In 2001, the City and ODC entered into an Option Agreement, under which the City has the right to purchase the Center (land and improvements) for one dollar when the Bonds are fully paid. The Overture Center is leased by ODC to the Madison Cultural Arts District (the "District") which manages and operates the facility pursuant to an Operation and Cooperation Agreement with the City (the "City/District Agreement"). The District is a governmental entity, and has a limited power of eminent domain but no power to tax. If the City does not exercise its option to purchase the facility for one dollar, ODC shall transfer ownership to the District.

If the Bonds are paid in full the City may exercise its option to purchase the Center from ODC for one dollar by providing written notice to ODC not later than the date the Bonds are redeemed. This notice deadline may be extended by up to thirty (30) days, by written notice from the City to ODC, in order to accommodate public meeting schedules.

By exercising its option, the City will assume all of the regular obligations of ownership, such as insurance, liability and maintenance and operations costs. It will also assume all of ODC's and/or the District's obligations under any surviving leases and contracts that are not terminable upon transfer. If it chooses, the City may unilaterally terminate the City/District Agreement. The effect of such a termination would be negligible on the day to day functions of the Center, since experienced incumbent City employees are in place to continue with its operation and maintenance. The wages, salaries and benefits of these employees are already included each year in the City's operating budget, as is the annual City subsidy to the District, which is estimated to be \$1,613,374 for 2006. Upon termination of the City/District Agreement, the City would no longer be contractually obligated to make this payment to the District. With ownership, the City would be directly and solely responsible for the cost of any capital improvements and repairs.

2. **What happens if the City does not exercise its option to purchase the facility?**

If the City does not exercise its option to purchase the Center for one dollar, the Center shall be transferred by ODC to the District. The District will acquire the Center subject to the City's reversionary interest, and will therefore be obligated to operate the Center as a public cultural arts facility. The City/District Agreement will remain in effect upon transfer of the Center to the District unless the City opts to terminate it. In addition to collecting the City subsidy and the revenue generated by the Center, the District has the

ability to fundraise and the statutory power to issue its own revenue bonds whose proceeds could be used to operate and maintain the Center. As owner, it could also mortgage the Center as collateral for loans. Since Mr. Frautschi's Pledged Assets will be used to redeem the Bonds, no investment income from these Assets will be available to fund operating grants to the District.

3. What is the effect of refinancing or early redemption of the Bonds on City employees who work on behalf of the District to operate the Center?

The City/District Agreement governs the use of City employees to provide staff for the District's operation and maintenance of the Center. The City/District Agreement provides that the operation and management of the Overture Center are to be performed by City employees on behalf of and under the direction and control of the District. The District reimburses the City in full for the cost of the services of the City employees, including wages, benefits and salaries. The City determines the selection, hiring, firing, wages, benefits and all labor relations for the City employees, and provides certain administrative services related thereto, such as human resources, at no charge to the District. The City/District Agreement provides that at any time on or after June 28, 2006, the District may offer employment by the District to all City employees who are then assigned to work for the District, provided that such offers include employment benefits and rights at least equal to City employment benefits and rights. Currently the District is not authorized to participate in the Wisconsin Retirement System. A statutory change would be needed to make WRS benefits available to district employees.

The latest refinancing proposal would not alter the arrangement regarding the District's use of City employees to manage and operate the Center. If the Bonds are redeemed and the City exercises its option to acquire the Center, City employees will continue to operate and maintain the Center, but it is likely they will be doing so on behalf of the City and not under the direction and control of the District. If the Bonds are redeemed and the District owns the Center, City employees will operate and maintain the Center until either: (a) the City terminates the City/District Agreement; or (b) the District offers employment to the City employees under the terms described above and such offer is accepted.

4. What happens to the District if the Bonds are paid in full and the City exercises its option to purchase the facility?

According to the statute which provided for the District's creation, the District may be dissolved by either enactment of a law by the legislature, or by the unanimous consent of the District Board. Dissolution in either circumstance would be subject to the District providing for payment of its incurred debts and the performance of its other contractual obligations. The City does not have the power to cause the District's dissolution. If the Bonds are redeemed early and if the City exercises its option to acquire the Center and terminates the City/District Agreement, the District will have no remaining functions to perform in the operation and maintenance of the Overture Center.