

CITY OF MADISON
INTER-DEPARTMENTAL
CORRESPONDENCE

DATE: October 14, 2005

TO: Alder Noel Radomski

FROM: Dean Brassler, City Comptroller

SUBJECT: **Future Overture Center Operating Costs**

In you October 11th e-mail to Mayor Cieslewicz, you asked for a “fiscal note” regarding the future budgetary implications of his recommendation that the City decline participation in the proposed refinancing and take ownership of the Overture Center building. This memo is an attempt to provide that information to the extent available.

As background, I would call your attention to a couple of documents that have been discussed at one or both of the special Board of Estimates meetings recently held to consider the Overture refinancing issue. The first is an October 6th memo from Assistant City Attorney Anne Zellhoefer that explains some of the organizational and operational consequences of ownership transfer. The second is a spreadsheet entitled “Overture Center Operating Budget Projection,” dated September 9, 2005. This spreadsheet summarizes the best available estimates of what it will cost to operate the Overture Center over the next several years.

Operating Projection

That operating pro-forma includes the most current estimates of operating expenses and operating revenues based on the recently completed first season of Overture Hall, and projects future revenues based on the performances and events scheduled for 2006 and the anticipated completion of Phase 2 construction. The budget projection also assumes a continuation of program grants, interest income and the current annual \$1,600,000 City operating subsidy, all with modest inflationary increases into the future. No provision is included for significant capital replacements or debt service during the 7-year term of this projection.

The result indicates a break-even condition for 2006, with increasing positive cash flows annually, reaching about \$500,000 per year by the end of the term. If this projection holds true, the total operating reserve of the Overture Center would grow from the predicted balance of \$1,000,000 at the end of 2005 to approximately \$2,900,000 by the end of 2012.

Again, this operating result does not take into account any capital replacement costs that may arise during the period, and any needed repairs would, of course, result in additional costs. To date, there has been no rigorous evaluation of future capital needs. The building is unique in nature and not fully completed. Any estimates of capital replacement needs at this point are highly speculative in nature. However, using the experience of Monona Terrace as a rough basis for comparison, rudimentary estimates have been made suggesting that average annual capital costs could fall within a range of \$1,000,000 to \$2,000,000 per year during the next 10 to 20 years. By their very nature, capital replacement needs will not occur at an even pace over time. More modest amounts should be needed in the earliest years, with larger expenditures required in the second decade of the building’s life, as major building systems first begin to require upgrade or replacement.

Transferred Ownership – Costs and Revenues

The transfer of ownership from Overture Development Corporation (ODC) to either the City or to the Madison Cultural Arts District (MCAD) would not materially alter the expected operating costs or operating revenues of the Overture Center. Regardless of which entity holds title to the building, it is likely that the current operating structure would remain in place. All three entities are tax-exempt from the standpoint of purchasing goods and services. City employees currently staff the Overture Center. Many core administrative systems such as human resources, labor relations, payroll, accounting, and information technology are currently integrated with existing City systems. Therefore, it is unlikely that the center's cost or operating revenue structure would be changed if building ownership were to be transferred. The cost of future capital replacements would also be unaffected by a change in ownership.

Transferred Ownership – Responsibility and Authority

The real changes associated with a transfer of ownership of the Overture building to the City are not reflected in the costs and revenues needed to run the facility. Rather, they are in the level of direct responsibility the City assumes for the continuing operation, as well as the level of authority or control over operating decisions.

Under the financing model that has been in place since 2001, the City has had a contractual obligation to provide continuing operating support of \$1,600,000 per year, Overture Development Corporation has been fully responsible for all debt related to the Overture Center, and operating authority has rested with the Madison Cultural Arts District.

If the proposed refinancing is approved, the City will retain its contractual obligation to provide operating support of \$1,600,000 per year and assume a contingent liability for a portion of the outstanding debt. If the refinancing were successful, the City would incur no additional costs beyond the current structure, the operating authority for Overture Center would continue to rest with MCAD, and future capital costs could be paid through MCAST investment earnings. Essentially, existing responsibility and authority would remain unchanged. In the circumstance where the refinancing were not successful, however, the City could be responsible for debt service costs of anywhere from \$-0- to \$10,000,000 in addition to its continued operating support, and would likely need to assume some responsibility for future Overture capital replacement costs averaging \$1,000,000 to \$2,000,000 per year.

If the proposed refinancing is not approved and the MCAST investment structure is dissolved, the City could elect to take ownership of the building. In this scenario, the City would remain responsible for the continuing operating support of \$1,600,000, and face responsibility for all capital replacement costs averaging \$1,000,000 to \$2,000,000 per year in the future. This fundamental change in financial responsibility would likely precipitate the dissolution of the Madison Cultural Arts District, as the City Council would assume authority for all operating and budgetary decisions of the Overture Center.

I hope this discussion is helpful and I look forward to answering any other questions you may have.

Sincerely,

Dean Brassler, City Comptroller