

Overture Refinancing Proposal

Board of Estimates

October 10, 2005

Endowment Fund Balance Thresholds to Watch

If fair market value is over \$104 million, the endowment fund will provide:

- Debt service on the original loan
- Debt service on “Series B” (up to \$2.5 million)
- Operations subsidy (\$1.4 million)

Between \$100 million and \$104 million:

- Debt service on the original loan
- Debt service on “Series B” (up to \$2.5 million)
- Operations subsidy on a sliding scale

Below \$100 million:

- Only debt service on the original loan
- Firewalls and City called on to cover “Series B” debt service
- No operating subsidy may be made

Below \$97 million:

- Endowment must be moved to more liquid and less risky investments to maintain collateralization of the original loan

Market Volatility

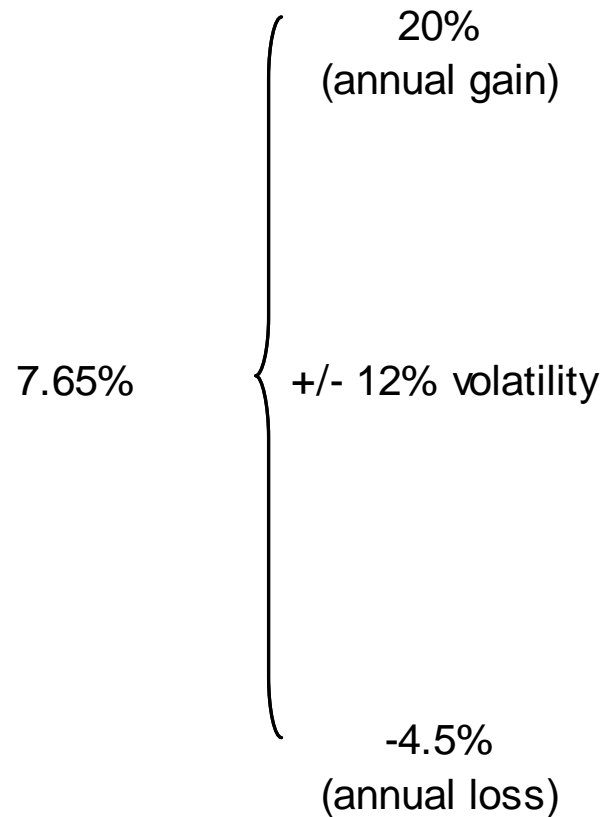
The most significant factor for the City when considering the refinancing proposal is the endowment's rate of return.

- Market volatility will determine the City's coverage of "Series B" debt service payments up to \$2.5 million per year.
- The pro forma presented on September 19 illustrates the need for an average rate of return of 8.23% or more.
- This average rate may be realized over a 35-year period, but the City's moral obligation is limited to six years.

Average vs. Annual Rates of Return

Based on its current portfolio, the endowment may be expected to earn 7.65%. However, this rate may be expected to fluctuate by plus or minus 12.02%.

This means the annual rate of return could range from a gain of approximately 20% to a loss of 4.5%.



Averages are Unreliable for Short-term Investments

The endowment's weighted average rate of return for the last five years is 3.17%.

- During that time the fund annually gained as much as 24.08% and lost as much as 20.41%.

Custer Investments provided actual rates of return of the American Balanced Fund, which represents a relevant comparison because of its diverse blend of investments.

- The American Balanced Fund's average rate of return for the last six years is 7.59%
- During that time, the fund annually gained as much as 18.42% and lost as much as 10.26%.

Scenario 1 – Repeat of Endowment’s Most Recent Rates of Return

In \$1,000s

	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>Notes</u>
Opening balance	107,140	105,473	93,876	69,006	80,073	80,507	79,770	
Debt service subsidy -- 2001 series loan	100	3,300	5,100	5,100	5,100	5,100	5,100	
Debt service subsidy -- Series B loan	602	1,824	0	0	0	0	0	1
Operating subsidy	1,400	1,400	0	0	0	0	0	
Annual rate of return	6.07%	-4.16%	-20.41%	24.08%	7.56%	6.07%	3.17%	2

1. "Series B" debt service subsidy is not awarded if fund balance less than \$100 million. Firewalls and City would be called on if subsidy not awarded.
2. Actual annual returns of MCAST's investments of the endowment fund. Five-year average used for 2011.

Firewalls

The City would be partially protected by two proposed firewalls:

- First, Mr. Frautschi has pledged up to \$5.0 million for the first four-year period with an annual maximum of \$2.5 million.
- If this firewall is called upon early, the \$5.0 million cap may be exhausted prior to the third or fourth year.
- Second, the Madison Cultural Arts District has pledged to reallocate sufficient funding if needed for one additional year up to \$2.5 million.

The City would be responsible for remaining debt service up to \$2.5 million per year until the end of the sixth year.

- If Mr. Frautschi's pledge is exhausted early, the City may be called upon to cover more than one year of the six-year period.

Scenario 1 – Endowment’s Actual Returns Applying Firewalls and City’s Financial Risk

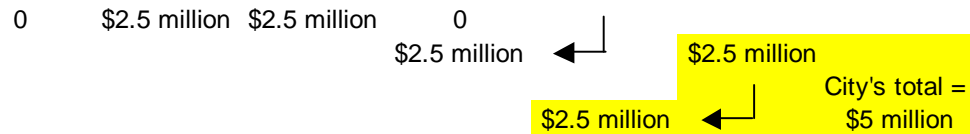
Less than \$100 million

In \$1,000s

	2005	2006	2007	2008	2009	2010	2011	Notes
Opening balance	107,140	105,473	93,876	69,006	80,073	80,507	79,770	
Debt service subsidy -- 2001 series loan	100	3,300	5,100	5,100	5,100	5,100	5,100	
Debt service subsidy -- Series B loan	602	1,824	0	0	0	0	0	1
Operating subsidy	1,400	1,400	0	0	0	0	0	
Annual rate of return	6.07%	-4.16%	-20.41%	24.08%	7.56%	6.07%	3.17%	2

FIREWALLS:

Mr. Frautschi's pledge	MCAD	City
up to \$5 million for first four years	up to \$2.5m	up to \$2.5m



- "Series B" debt service subsidy is not awarded if fund balance less than \$100 million. Firewalls and City would be called on if subsidy not awarded.
- Actual annual returns of MCAST's investments of the endowment fund. Five-year weighted average used for 2011.

If the endowment fund investments experience a loss early on, MCAD may be called on prior to the end of Mr. Frautschi's four-year period. This could expose the City to annual payments in both 2010 and 2011 totaling up to \$5.0 million.

Scenario 2 – Repeat of American Balanced Fund’s Recent Rates of Returns

In \$1,000s

	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>Notes</u>
Opening balance	107,140	105,473	96,998	109,134	88,627	98,212	103,277	
Debt service subsidy -- 2001 series loan	100	3,300	5,100	5,100	5,100	5,100	5,100	
Debt service subsidy -- Series B loan	602	1,824	0	2,101	0	0	2,113	1
Operating subsidy	1,400	1,400	0	1,400	0	0	1,147	
Annual rate of return	6.07%	-1.20%	18.42%	-10.26%	17.22%	11.00%	10.38%	2

1. "Series B" debt service subsidy is not awarded if fund balance less than \$100 million. Firewalls and City would be called on if subsidy not awarded.
2. Actual annual returns of MCAST's investments of the endowment fund. Five-year weighted average used for 2011.

Scenario 2 – American Balanced Fund’s Actual Returns Applying Firewalls and City’s Financial Risk

In \$1,000s

	2005	2006	2007	2008	2009	2010	2011	Notes
Opening balance	107,140	105,473	96,998	109,134	88,627	86,496	84,293	
Debt service subsidy -- 2001 series loan	100	3,300	5,100	5,100	5,100	5,100	5,100	
Debt service subsidy -- Series B loan	602	1,824	0	2,101	0	0	0	1
Operating subsidy	1,400	1,400	0	1,400	0	0	0	
Annual rate of return	6.07%	-1.20%	18.42%	-10.26%	4.00%	4.00%	4.00%	2

Less than \$97 million
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FIREWALLS:	Mr. Frautschi's pledge		MCAD	City
	up to \$5 million for first four years		up to \$2.5m	up to \$2.5m
	0	\$2.5 million	0	\$2.5 million
	0	\$2.5 million	\$2.5 million	\$2.5 million

1. "Series B" debt service subsidy is not awarded if fund balance less than \$100 million. Firewalls and City would be called on if subsidy not awarded.

2. MCAST returns trough August 2005 used for 2005. American Balanced Fund annual rates of return repeated for 2006, 2007 and 2008. Redeployment of endowment fund reflected as 4% return for 2009, 2010 and 2011.

A balance below \$97 million requires redeploying the fund to more liquid and less risky investments. As a result, the rate of return would range from 3% to 4%. This adjustment is made in the model during 2009. Applying the same adjustment to Scenario 1 does not change its outcome.