Case Studies on Property Development:*

OAKLAND MUSEUM SALE AND LEASEBACK

David E. Dowall
David Shiver

Working Paper No. 392

November 1982

Institute of Urban and Regional Development

University of California, Berkeley

---

*Financial support for the research on and writing up of this case study was provided by the Education Committee of the Urban Land Institute, Washington, D.C.

OAKLAND SALE-LEASEBACK OF MUNICIPAL FACILITIES

David E. Dowall and David Shiver

INTRODUCTION

Henry L. Gardner, city manager for the City of Oakland, California, was reviewing documents for an important city council meeting the next day. At the meeting, he would present details with respect to a proposal he and his staff had negotiated with a tax shelter syndicate to sell and leaseback the city's museum. When consummated, the deal would provide the city with new funds to refurbish its civic auditorium. The proposal had been in the planning stages for several months and had generated considerable publicity. Many cities across the nation were watching to see whether a municipality could successfully employ this financing technique, which was commonly used by private firms and corporations to raise cash (Exhibit 1).

THE CIVIC CENTER AUDITORIUM

The Oakland Civic Center Auditorium, built in 1927, was located across from a small lake and park near the city's central business district. The facility was heavily used by the city's ballet company and symphony, other civic groups, and by local concert promoters. It attracted approximately half a million patrons per year.

Eight months before, the state had inspected the auditorium, and found several serious code violations. It threatened to condemn the facility unless the city undertook major repairs to eliminate the violations. While the city had been providing annual operating subsidies of approximately $250,000 and was willing to continue its subsidy program, it could not provide additional money from its general or capital funds to cover rehabilitation costs. The magnitude of the costs, estimated to range from $10 to $14 million, far exceeded the city's revenue raising capacity. Furthermore, Proposition 13, a property tax limitation law approved by California voters several years earlier, essentially had abrogated the authority of municipalities to issue new general obligation bonds. Mr. Gardner knew that floating revenue bonds secured only by revenues from the auditorium would be impossible since he projected indefinite annual operating losses from the facility--even upon rehabilitation.

He had, however, read of a Fortune 500 Corporation which had sold and leased-back its New York headquarters in order to raise funds. He wondered whether Oakland could structure a similar deal, and instructed his staff to contact Goldman, Sachs, and Co., the city's underwriter, to study financing strategies. After several months of intensive discussion in Oakland and New York, his staff and underwriter representative reported that it appeared that a sale-leaseback of municipal facilities would be the best way to finance rehabilitation of auditorium improvements. But its feasibility would be contingent on several actions by the city and the terms of the sale and lease to be negotiated.

Early on, his staff determined that the sale-leaseback of the civic auditorium alone was insufficient to finance both its reconstruction and repurchase, and suggested that the city also sell and leaseback its museum. The problem with selling the museum would be potential misunderstanding of the arrangement by groups such as "The Oakland Museum Association" --a volunteer support organization-- and the general public. Mr. Gardner could see a lot of bad publicity generated which could kill his project. He figured the best way to handle this potential problem would be to invite separately representatives of the museum group, auditorium users, and individual council members into his office to explain personally what he and his staff were preparing. He would assure them that the city would not be selling or pledging its museum collection, and would retain control over the use of the facilities. Even though lease terms at the time of these discussions had not been set, he knew that whoever bought the museum would be interested only in tax benefits and not museum operations.

Additionally, his staff had been working with the city attorney's office and the city's bond counsel, Orrick, Herrington & Sutcliffe, to find out what legal hurdles faced the city. First, while the city had a procedural ordinance for disposition of surplus properties, it had none for disposition of non-surplus property. The museum could not be considered surplus; therefore, any attempt to sell it could be challenged in court. The bond counsel drafted a procedural ordinance which would allow the city to sell non-surplus property. Similarly, a procedural ordinance was needed in order to float municipal improvement revenue bonds. Oakland's city charter provided that the council may issue revenue bonds "for any lawful purpose and upon any such terms and conditions as it establishes by the procedural ordinance." After adoption of such an ordinance, the city would be free to make a bond resolution to issue a set amount of bonds for a qualifying purpose. Third, Mr. Gardner's staff recommended that the city council extend the boundaries of its Central District Urban Renewal Area to include the museum and auditorium sites, and to rename the civic auditorium as the "Oakland Convention Center Extension". This action would allow the city some flexibility in issuing industrial revenue bonds.

Finally, Mr. Gardner had been advised that Integrated Resources, a New York based real estate syndication firm, was interested in participating in a sale-leaseback agreement. Mr. Gardner, wanting to move as quickly as possible on the project, submitted to the Council and received its approval of ordinances establishing procedures for Municipal Improvement Bond, sale or lease of non-surplus property, and extension of the Central District Urban Renewal Boundaries (Exhibit 2). At the same time, he began negotiations over the sale and lease terms with Integrated Resources. His efforts had resulted in the following proposal.

MUSEUM TRANSACTION

He proposed that the city sell its facilities in two phases. First the city would sell the museum to Oakart Associates, a limited partnership created by Integrated Resources and targeted to professionals and wealthy individuals in high marginal tax brackets who seek tax shelters and capital appreciation in real estate. As part of the sales package, the city would create a ground lease under which Oakart would lease the land on which the museum was situated for an initial term of 30 years, with seven five-year renewal options.

An appraiser retained by the city estimated the value of the museum to be $22,000,000. Mr. Gardner used this figure as the selling price. Oakart had agreed to make an initial 5 percent downpayment of $1,100,000 and a five and a half year series of semi-annual equity contributions of $300,000. At the end of five and a half years, Oakart would have a 20 percent equity position, the required percentage necessary for the transaction to qualify as sale under Internal Revenue Service regulations. The remainder of the purchase price would be covered by a 30 year term, non-recourse purchase money note, secured by a deed of trust. Debt service payments would be made semi-annually in arrears. The payments would be interest only during the first 10 years and would liquidate the entire note with level amortization payments over the remaining 20 years.

At the closing, Oakart would simultaneously enter into a leaseback of the museum and a sublease of the land to the city, for an initial term of 30 years and with four five-year renewal options. In its deed of trust, the Oakart partnership would grant to a trustee its interest in the museum property as well as its interest in the museum leasehold, and lease and sublease under the leasehold estate created by the ground lease.

The terms for museum lease payments were crucial to the project's feasibility because they would determine the cost of financing auditorium improvements and repurchase price to the city. Mr. Gardner thus had spent much time bargaining over the rental terms. He and Oakart finally agreed to set rent payments at a fixed percentage of land and improvement value. The original offer worked out between the city and

Oakart was as follows:

LEASE RENTAL OFFER TO THE CITY

	Estimated Annual Rental Constants		
Estimated Mortgage Rate	13.0%	13.5%	14.0%
Lease Period			
Initial Term	12.37%	12.84%	13.32%
Primary Term			
1st 5 Years	7.80	8.35	8.89
Next 5 Years	12.37	12.84	13.32
Next 5 Years	13.45	13.85	14.27
Last 15 Years	21.18	21.76	22.37
Renewals	9.65	9.85	10.05
Cost of Leasing	11.47	11.90	12.34
Spread	153 B.P.	160 B.P.	166 B.P.
Level Equivalent	11.89	12.29	12.69

Assuming a mortgage rate between 13 to 14 percent, the city could save from 153 to 166 basis points when it financed its auditorium improvements.

Since the initial offer, however, the mortgage rate had declined to the range 12 to 13 percent, and new rental constants were negotiated. Mr Garner's latest estimate of net lease payments by the city to Oakart would be $1,830,000 per annum in the first five years, and would increase to $3,542,000 in the final fifteen years of the primary term. The city would be responsible for all costs and expenses related the operation of the museum and grounds. Costs include insurance, taxes, repairs, and other contingencies. Oakart would relinquish all rights to operate the property, determine its use, or to sublease any portion of the facility.

The city would finance the auditorium improvements by floating Municipal Improvement Revenue bonds, at 12.5 percent interest, compounded semi-annually, with a 15 year call provision. The bonds would be secured by a security interest in the purchase money note and a deed of trust granted by the city to a trustee. As additional security, the city would pledge and assign its interest in the museum lease and land sublease, and obtain municipal bond insurance (which guarantees payment of principal and interest) from the American Municipal Bond Insurance Company. Oakland in prior bond issuings had received Aaa ratings from Standard and Poor's.

The trust indenture created by the city, would establish two special funds: a construction fund and a capital fund. Both funds would be administered by a trustee. The city would receive $21,273,000, net issuance costs of $627,000. Of the net proceeds, Mr. Gardner figured that $8,273,000 would be placed in the capital fund and $13,000,000 in the construction fund. The city could freely requisition money from the construction fund to pay for improvements, with any remaining funds transferable to the capital fund. The capital fund would be used to make lease payments, and to redeem or retire the outstanding bonds.

AUDITORIUM SALE-LEASEBACK

Mr. Gardner had reached an understanding with Oakart that the city could close the sale of its auditorium six months after the museum transaction. The city's appraiser estimated the value of the auditorium to be about $35.8 million, breaking down as follows: $20 million for the existing buildings, $3 million for improvements made, and $3.8 million for interest accrued during the construction period.

While he expected that the ownership structure of the auditorium deal would be similar in most respects to the museum sale-leaseback, the financing arrangements had not been set. Goldman Sachs had advised that industrial development bonds might be feasible since proceeds to the city would be considered as sales proceeds and not as bond proceeds -- thus, freeing the city from arbitrage bond restrictions. The only problem with the IDB as a financing vehicle was that State of California regulations put an interest cap of 12 percent on bonds. At the time of Mr. Gardner's negotiations, tax exempt interest rates exceeded the 12 cap, so alternative financing instruments --such as a lease-purchase arrangement-- were being explored by his staff and financial consultant. But he was confident the auditorium deal would be executed. For the purposes of his cash flow analysis, he figured that cash proceeds would total about $34.7 million, after deducting bond issuance costs and a reserve fund requirement. (he figured that bond underwriters would require that a reserve fund be established, equal to 12.5 percent of the total bond issue). Exhibit 3 was prepared by his staff to indicate the disposition of proceeds.

REPURCHASE OF THE FACILITIES

He expected the mayor and council members to be concerned about whether the city would be able to repurchase the museum and auditorium. Unlike the case of equipment sale-leaseback transactions, the Internal Revenue Service did not permit fixed repurchase prices for real property. A fixed price would not, according to IRS regulations, qualify the agreement as a sale. Mr. Gardner planned to minimize uncertainty by having Oakart agree to the income approach to establish a repurchase price. He calculated the present value of the museum in the 30th year, using three separate cost of capital assumptions (Exhibit 4). He assumed that museum lease payments would be \$2,695,000 per annum for the 20 year lease option period from year 31 to year 50, and that the value of the structure for the fifteen years following the lease option period would be \$100,000,000. The cost of capital figures were estimates of rates at the end of the initial 30 year lease term. Based on these assumptions, he figured that the museum repurchase price could range from \$30,497,000, to \$37,808,000, or \$47,915,000 at 12 percent, 10 percent, and 8 percent discount rates, respectively.

In his cash flow analysis, he assumed that the auditorium would be sold for \$35,800,000, including \$12,000,000 in improvements, and construction interest of \$3,800,000. By the end of the initial lease period, he estimated that the city would have \$43,317,000 to repurchase the facilities. He concluded that, given what he thought were conservative assumptions, the city would have enough cash to repurchase the museum (Exhibit 5a). He made a second cash flow analysis showing that even if the auditorium were not sold, the city would have sufficient cash at the end of the primary term to buy back the museum (Exhibit 5b).

Oakart had agreed to two additional repurchase procedures. First, during the primary lease term, the city could repurchase the museum at any mutually acceptable price. Second, the city may outbid by one dollar, any bid on the property accepted by Oakart from a third party investor. Also, any third party purchaser would be bound to the terms of the lease agreements, and would be obligated to give the city at the end of its primary lease term exclusive right to repurchase the facility, using the agreed upon income approach to valuation.

These were the most important elements of the sale-leaseback package he had developed with his staff and consultants. All that remained was to persuade the mayor and council members to accept the proposal and pass a bond resolution ordinance to authorize issuance of bonds. He was excited by the prospects.

EXHIBIT 1

TAX-EXEMPT LEVERAGED LEASING

PURPOSE: Leveraged lease financing provides municipalities with a creative vehicle for sharing in the tax benefits derived from the sale and leaseback of public facilities. Leveraged leases can produce net borrowing costs significantly lower than traditional bond financings. These cost savings can easily exceed 150 basis points, depending on the type and age of the facility involved, and the nature of the leverage leasing arrangements. In addition, leveraged lease financings can be structured so that there are no restrictions placed on the interest earnings and/or the use of the facility sale proceeds.

ELIGIBLE MUNICIPALITIES: Any political subdivision (e. g., City, County, Redevelopment Agency, etc.) which is able to issue special purpose revenue bonds and/or industrial development bonds may take advantage of leverage lease financing. Also, any other political subdivision which owns public facilities may participate if it has access to a financing authority (i. e., a charter city could act as the financing authority for its school district).

ELIGIBLE FACILITIES: Most new or existing municipal facilities can be considered for leverage lease financing. These include but are not limited to schools, administrative office buildings, museums, convention centers, etc. There are, however, certain limitations which must be considered; for example, the building must be earthquake safe, convertible to a private use (i. e., a school might be converted to a shopping center), and not be subject to any sale restrictions (e. g., Federal/-State grant covenants restricting ownership of property, outstanding bonds, etc.).

BASIC STRUCTURE: Leveraged lease financing involves the sale of a public facility by a municipality to a private investor, and the simultaneous leasing back of the facility by the municipality. To accomplish this, the private investor is required to make a cash equity contribution for a portion of the purchase cost. The municipality, in turn, provides tax-exempt revenue bond financing to the investor for the remainder of the cost. Bonds are issued either as Municipal Improvement Revenue Bonds secured by a purchase money note from the investor or as Industrial Development Bonds issued directly on behalf of the investor.

MUNICIPAL IMPROVEMENT BOND APPROACH (MAJOR STEPS):

1. The municipality sells a public facility (or facilities) to a private investor. This sale entitles the investors to the substantial tax benefits associated with property ownership.
2. The municipality issues Municipal Improvement Revenue Bonds which are secured by a purchase money note received from the purchaser of the facility (the private investor).
3. The municipality leases the facility's land to the private investor. The investor, in turn, leases the facility and sub-leases the land back to the municipality.
4. The municipality makes lease payments (net of ground lease payments) to the investor during the primary lease period. At the end of the primary lease period, the municipality will have the option of repurchasing the facility or exercising its first lease renewal option.
5. The municipality uses all of the bond proceeds within a three (3) year period for eligible capital improvements.

The advantage of this approach is that Municipal Improvement Revenue Bonds are not considered to be Industrial Development Bonds (IDB's) and the bond sale is therefore not restricted by the small issue IDB size and capital expenditure limitations (for example, the City of Oakland's Museum was sold for $22 million. If IDB's had been used, the City would have been limited to a $10 million sale price because museums are not exempted from the small issue IDB limitations.). The disadvantage of this approach is that all proceeds must be used for eligible municipal improvements within three (3) years or become subject to federal arbitrage restrictions.

INDUSTRIAL DEVELOPMENT BOND APPROACH (MAJOR STEPS):

1. The municipality sells a municipal facility to a private investor and leases it back under the same terms and conditions as the Municipal Improvement Revenue Bond Approach.

2. The investor purchases the facility from the municipality with the proceeds derived from tax-exempt IDB's issued by the municipality on behalf of the investor.

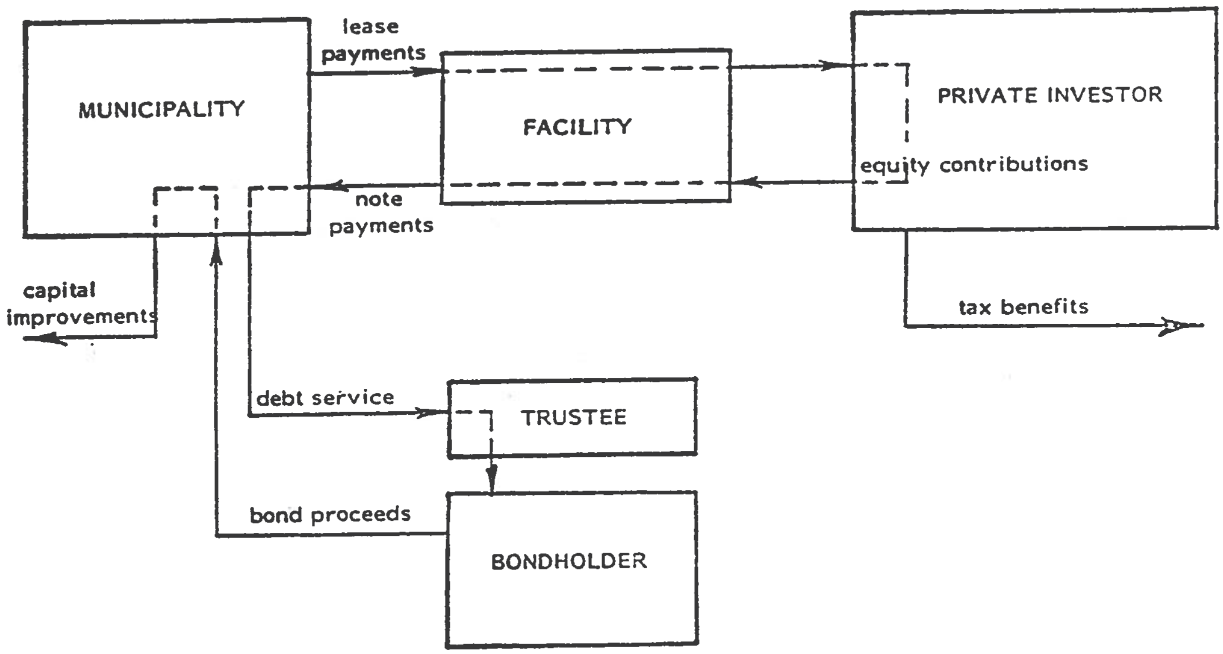
3. The municipality uses the sale proceeds for any municipal purpose, including investing all or a portion of the proceeds in order to pay lease payments to the investor and possibly to repurchase the facility at the end of the primary lease period.

The advantage of this approach is that the funds received by the municipality are unrestricted as to use and/or investment earnings because the proceeds are derived from the sale of a municipal facility and are not considered bond proceeds.

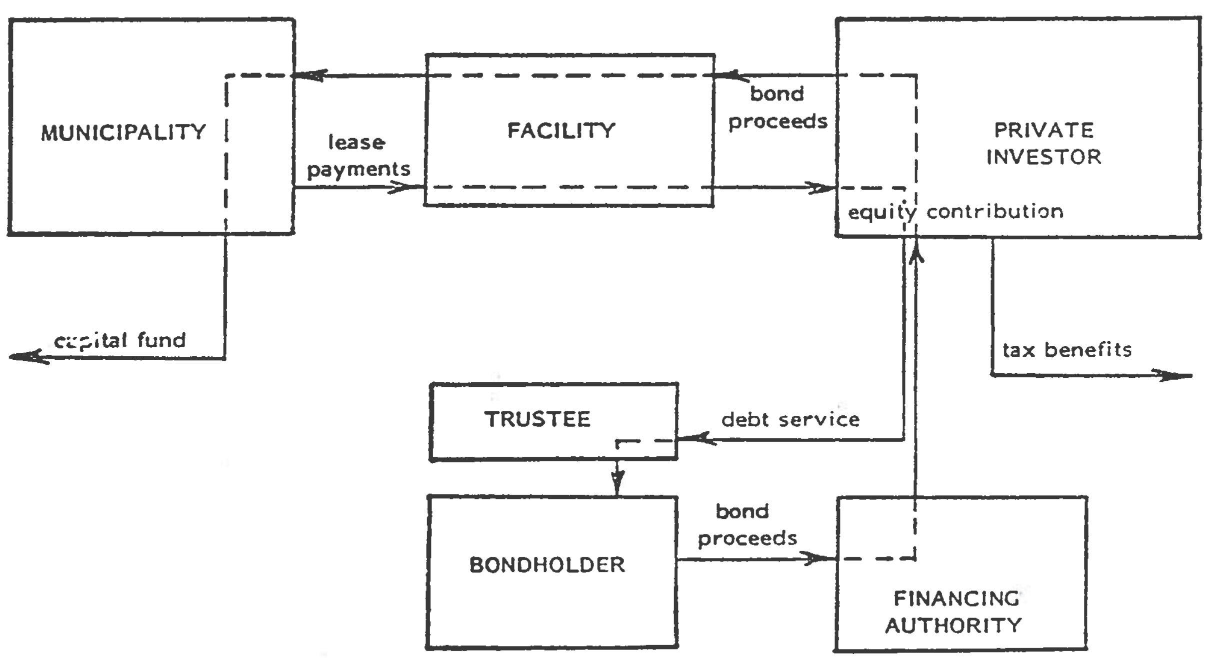
The disadvantage of this approach is that the bonds are IDB's and are subject to small issue IDB size and capital expenditure limitations (except in the case of specifically exempted facilities such as convention centers, sports arenas, etc.).

MUNICIPAL OBLIGATIONS: By entering into a leveraged lease financing, a municipality gives up all rights of ownership of the subject facility and, unlike equipment sale/leasebacks, may not enter into any pre-close agreement which would establish a future repurchase price. The municipality must also agree to make all lease payments during the primary lease period net of the investor's ground lease obligations, and to ensure the investors that the facility will remain in at least its current condition during the lease period. The municipality is required to maintain insurance policies on the facility, including but not limited to, fire, flood, earthquake (in California), general public liability, and other risk policies which are normally included under "extended coverage" endorsements. In addition, the municipality will be required to pay all property taxes for the investor. However, a municipality may avoid the issue of property taxes altogether by: reaching an agreement to waive the collection of taxes on the subject facility (all of the political subdivisions which share the property tax revenues would have to agree to this); establishing redevelopment project areas in order to create a tax increment generating facility; only selling facilities which are exempted by law from taxation even if they are privately owned (i. e., facilities which are free to the public such as schools, museums, etc.).

BENEFITS: Leveraged lease transactions are structured so that the private investors are able to take advantage of both the tax shelter benefits associated with property ownership as well as low interest rate financing. However, in order to do so, the private investors are required to make a cash equity contribution of at least 20% of the facility purchase price. The municipality ultimately shares in the tax benefits and equity contribution through substantially reduced lease payments in the first five to ten years of the lease period. Also, leveraged lease transactions can be structured to provide unrestricted sale proceeds to the municipality. This allows a portion of the proceeds to be invested in long-term securities without the typical arbitrage limitations. Through prudent investment of a portion of the sales proceeds, it is possible for a municipality to build up a capital fund sufficient to pay all of its facility leaseback payments with funds remaining to repurchase the facility at the end of the primary lease period. This, of course, depends upon the percentage of proceeds which are initially invested rather than spent, and the spread between the interest earned on the investments and the cost of bond financing.



MUNICIPAL IMPROVEMENT REVENUE BOND APPROACH



INDUSTRIAL DEVELOPMENT BOND APPROACH

STONE & YOUNGBERG
MUNICIPAL FINANCING CONSULTANTS, INC.

EXHIBIT 2

CITY OF OAKLAND
Interoffice Letter

To: Redevelopment Agency, Administrator Attention: Henry Gardner Date: December 22, 1981

From: George H. Williams, AIA

Subject: RESOLUTION RECOMMENDING PROPOSED BOUNDARY CHANGES TO THE CENTRAL DISTRICT URBAN RENEWAL PLAN, AUTHORIZING SUBMITTAL TO CITY COUNCIL OF THE PROPOSED AMENDMENT TO SAID PLAN AND ALL NECESSARY DOCUMENTS RELATED THERETO, AND AUTHORIZING SUBMISSION OF SUCH CHANGES TO THE PLANNING COMMISSION FOR THEIR REPORT AND RECOMMENDATIONS

A resolution has been prepared recommending that the Central District Urban Renewal Plan area be amended to expand the Project Area to include areas set forth on the attached Exhibit A. The primary purpose of this amendment is to permit redevelopment-type activity to take place in the area of the Oakland Auditorium and Oakland Museum.

The proposed expanded area has been the subject of study by Agency staff and Agency counsel, and it is their opinion that the area qualifies for redevelopment activity as defined by California Community Redevelopment Law and is necessary for the effective redevelopment of the existing Central District Urban Renewal Project Area.

RECOMMENDATION:

It is recommended that: (1) the Agency recommends that the Central District Urban Renewal Plan be amended as described in Exhibit A and (2) the Agency and City Council take all necessary steps to adopt the proposed amended plan, to authorize the Administrator of the Redevelopment Agency to prepare the necessary documentation and to submit the recommended plan changes to the Planning Commission for their report and recommendation and (3) authorize the Administrator of the Redevelopment Agency to transmit these recommendations to the City Council pursuant to Health & Safety Code Section 33450 et seq.

George H. Williams

GEORGE H. WILLIAMS, AIA
Director, Office of Economic
Development and Employment

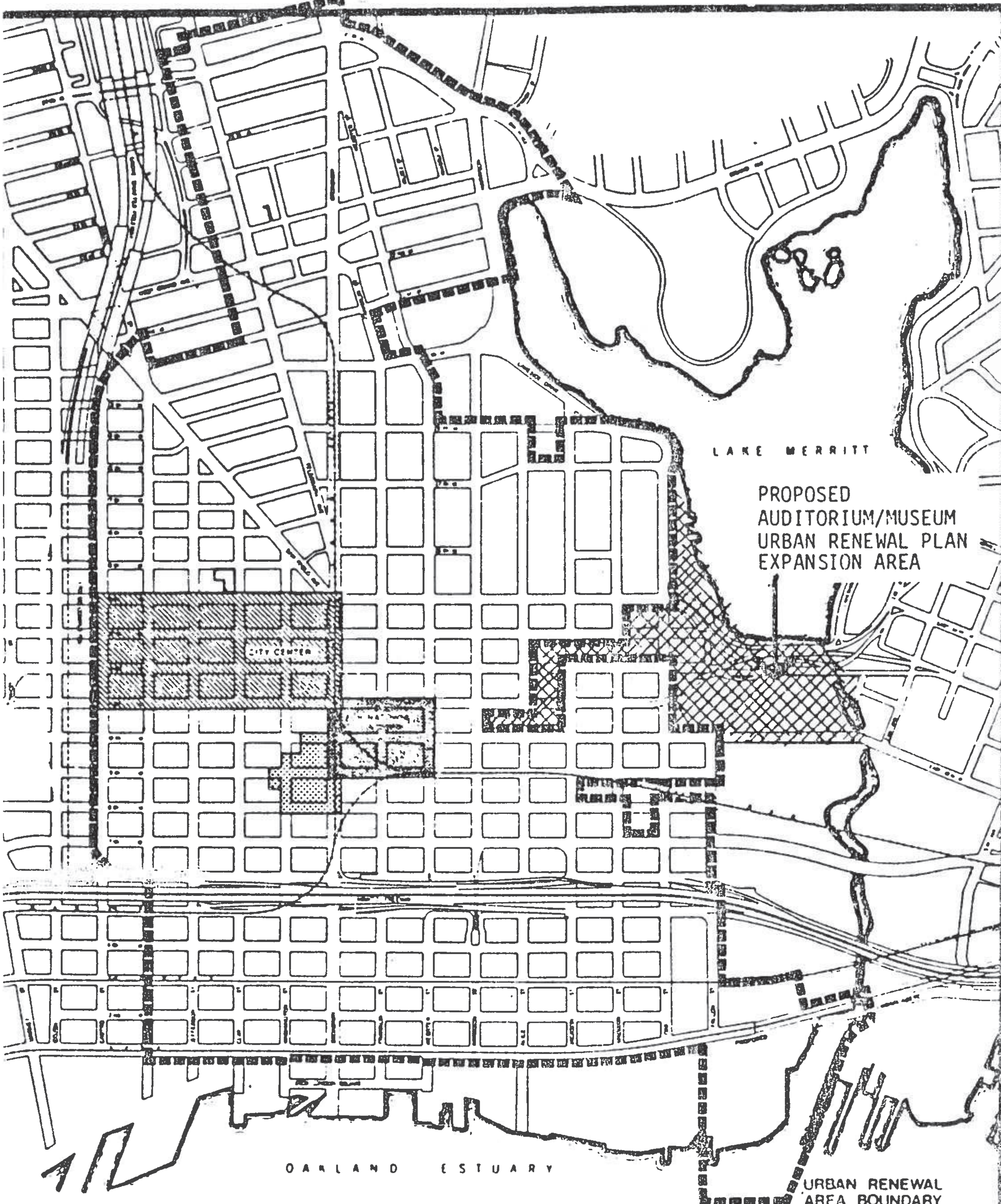
APPROVED FOR FORWARDING TO
REDEVELOPMENT AGENCY

Henry L. Gardner

Administrator

Attachment

EXHIBIT 2 con't



CENTRAL DIST. URBAN RENEWAL PLAN

LAND ACTIVITY MAP: EXHIBIT A

REDEVELOPMENT AGENCY OF THE CITY OF OAKLAND

AMENDED: 1979

CITY CENTER PROJECT ACQUISITION AREA

CHINATOWN PROJECT ACTION AREA

VICTORIAN ROW OLD OAKLAND PROJECT AREA

AUDITORIUM/MUSEUM EXPANSION AREA

B

EXHIBIT 3

Proceeds from Auditorium Sale

($000)

Auditorium sales price:	
Building	$20,000
Improvements	12,000
Construction interest	3,800
	$35,800
Net cash available:	
Face value of bonds	$38,869
Reserve fund	(4,859)
Net bond proceeds	34,010
Partnership cash down payment	1,790
Cash available	35,800
Issuance costs	(1,068)
	$34,732
Disposition of net cash available:	
Cash proceeds invested in capital fund	$30,932
Cash proceeds to fund interest costs during construction	3,800
	$34,732

EXHIBIT 4

Projected Repurchase Price of Museum

($000)

	Cost of Capital		
	8%	10%	12%
Present value of annual payments of $2,695 received over 20 years	$26,460	$22,944	$20,130
Present value of $100,000 received in 20 years	21,455	14,864	10,367
Estimated repurchase price	$47,915	$37,808	$30,497

EXHIBIT 5a

CITY OF OAKLAND

MUSEUM TRANSACTION FOLLOWED BY AUDITORIUM TRANSACTION WITH $12 MILLION OF IMPROVEMENTS

SUMMARY OF PROJECTED CASH FLOW RESULTS

($000)

		Capital Fund							Construction Fund					
		14.5% Investments		14.25% Investments		8% Investments								
End of Year	Six Month Period Ending	Balance	Interest Income	Balance	Interest Income	Balance	Interest Income	Reserve Fund Income at 2%	Fund Balance Available	Interest Income at 11%	Total Interest Income	Total Amount Available	Lease Payments	Total Remaining
	01/01/82	$ 8,373							$13,000			$21,373		$21,373
	06/30/82	8,373	$ 606						12,000	$715	$1,321	21,694	$ 915	20,779
1	12/31/82	39,305	2,849	$ 406	$ 29			$49	9,000	660	3,587	52,298	1,754	50,544
2	12/31/83	39,305	2,849	4,038	288			49		330	3,516	46,859	1,754	45,105
3	12/31/84	39,305	2,849	7,356	524			49			3,422	50,083	2,338	47,745
4	12/31/85	39,305	2,849	9,602	684			49			3,582	52,489	2,338	50,151
5	12/31/86	39,305	2,849	12,179	868			49			3,766	55,250	2,338	52,912
6	12/31/87	39,305	2,849	12,179	868	$ 2,519	$101	49			3,867	57,870	3,081	54,789
10	12/31/91	39,305	2,849	12,179	868	8,200	328	49			4,094	63,778	3,448	60,330
15	12/31/96	39,305	2,849	12,179	868	12,700	508	49			4,274	68,458	3,783	64,675
20	12/31/01	39,305	2,849	12,179	868	9,752	390	49			4,156	65,392	4,693	60,699
25	12/31/06	39,305	2,849	12,179	868	3,305	132	49			3,898	58,687	4,693	53,994
30	12/31/11	39,305	2,849	5,421	386			49			3,284	48,010	4,693	43,317

Interest spread, between initial investments and debt: 2%

Assumptions:

1. Proceeds of the museum sale are invested such that $8,373,000 yields 14.5% per annum for a fixed term of 30 years, and the balance of $13,000,000 yields 11% on a short-term basis.

2. The auditorium sale is closed on July 1, 1982, and the proceeds of $30,932,000 are invested to yield 14.5% per annum for a fixed term of 29.5 years.

3. During 1982 and 1983, the short-term investments are disbursed for museum improvements of $1,000,000 and $12,000,000 of improvements to rehabilitate the auditorium.

4. Interest on the reserve fund of $4,859,000 required by the Convention Center Extension Bonds will accrue to the City at the rate of the assumed interest spread.

5. Reinvested net interest is assumed to yield 8% after the 5th year, and 14.25% prior to that.

6. Lease payments, which are net of ground lease receipts, represent the combination of (a) museum lease payments which are based on a sales price of $22,000,000 multiplied by an annual rental factor specified by the museum purchaser, and (b) auditorium lease payments which are amounts that have been specified by the auditorium purchaser.

[illegible] of significant assumptions

CITY OF OAKLAND

MUSEUM TRANSACTION ONLY

SUMMARY OF PROJECTED CASH FLOW RESULTS

($000)

EXHIBIT 5b

		Capital Fund							Construction Fund					
		14% Investments		13.75% Investments		7% Investments								
End of Year	Six Month Period Ending	Balance	Interest Income	Balance	Interest Income	Balance	Interest Income	Reserve Fund Income at 1.5%	Fund Balance Available	Interest Income at 11%	Total Interest Income	Total Amount Available	Lease Payments	Total Remaining
	01/01/82	$10,373							$11,000			$21,373		$21,373
	06/30/82	10,373	$726						10,000	$605	$1,331	21,704	$ 915	20,789
1	12/31/82	10,373	726	$ 416	$ 29				9,500	550	1,305	21,594	915	20,679
2	12/31/83	10,373	726	10,825	744						1,470	22,668	915	21,753
3	12/31/84	10,373	726	11,973	823						1,549	23,895	915	22,980
4	12/31/85	10,373	726	13,285	913						1,639	25,297	915	24,382
5	12/31/86	10,373	726	14,783	1,016						1,742	26,898	915	25,983
6	12/31/87	10,373	726	14,783	1,016	$ 1,290	$ 45				1,787	28,233	1,309	26,924
10	12/31/91	10,373	726	14,783	1,016	5,622	197				1,939	32,717	1,309	31,408
15	12/31/96	10,373	726	14,783	1,016	11,704	410				2,152	39,012	1,436	37,576
20	12/31/01	10,373	726	14,783	1,016	16,631	582				2,324	44,111	1,771	42,340
25	12/31/06	10,373	726	14,783	1,016	23,125	809				2,551	50,832	1,771	49,061
30	12/31/11	10,373	726	14,783	1,016	32,286	1,130				2,872	60,314	1,771	58,543

Interest spread, between initial investments and debt: 1.5%

Assumptions:

1. Proceeds of the museum sale are invested such that $10,373,000 yields 14% per annum for a fixed term of 30 years and, the balance of $11,000,000 yields 11% per annum on a short-term basis.

2. During 1982, disbursements of $1,500,000 are made from the short-term investments for museum improvements and auditorium engineering studies. The decision is then made not to sell the auditorium, and the balance of short-term investments, $9,500,000, is invested to yield 13.75% per annum, for a fixed term of 29 years.

3. Reinvested net interest is assumed to yield 7% after the 5th year, and 13.75% prior to that.

4. Lease payments, which are net of ground lease receipts, are based on the museum sales price of $22,000,000, multiplied by an annual rental factor specified by the museum purchaser.

The accompanying summary of significant assumptions is an integral part of this projection.

EXHIBIT 6

§ 103. Interest on certain governmental obligations

(a) General rule.—Gross income does not include interest on—

(1) the obligations of a State, a Territory, or a possession of the United States, or any political subdivision of any of the foregoing, or of the District of Columbia; and

(2) qualified scholarship funding bonds.

(b) Industrial development bonds.—

(1) Subsection (a)(1) or (2) not to apply.—Except as otherwise provided in this subsection, any industrial development bond shall be treated as an obligation not described in subsection (a)(1) or (2).

(2) Industrial development bond.—For purposes of this subsection, the term "industrial development bond" means any obligation—

(A) which is issued as part of an issue all or a major portion of the proceeds of which are to be used directly or indirectly in any trade or business carried on by any person who is not an exempt person (within the meaning of paragraph (3)), and

(B) the payment of the principal or interest on which (under the terms of such obligation or any underlying arrangement) is, in whole or in major part—

(i) secured by any interest in property used or to be used in a trade or business or in payments in respect of such property, or

(ii) to be derived from payments in respect of property, or borrowed money, used or to be used in a trade or business.

(3) Exempt person.—For purposes of paragraph (2)(A), the term "exempt person" means—

(A) a governmental unit, or

(B) an organization described in section 501(c)(3) and exempt from tax under section 501(a) (but only with respect to a trade or business carried on by such organization which is not an unrelated trade or business, determined by applying section 513(a) to such organization).

(4) Certain exempt activities.—Paragraph (1) shall not apply to any obligation which is issued as part of an issue substantially all of the proceeds of which are to be used to provide—

(A) projects for residential rental property if each obligation issued pursuant to the issue is in registered form and if—

(i) 15 percent or more in the case of targeted area projects, or

(ii) 20 percent or more in the case of any other project, of the units in each project are to be occupied by individuals of low or moderate income (within the meaning of section 167(k)(3)(B)),

(B) sports facilities,

(C) convention or trade show facilities,

(D) airports, docks, wharves, mass commuting facilities, parking facilities, or storage or training facilities directly related to any of the foregoing,

(E) sewage or solid waste disposal facilities or facilities for the local furnishing of electric energy or gas,

(F) air or water pollution control facilities,

(G) facilities for the furnishing of water for any purpose if—

(i) the water is or will be made available to members of the general public (including electric utility, industrial, agricultural, or commercial users), and

(ii) either the facilities are operated by a governmental unit or the rates for the furnishing or sale of the water have been established or approved by a State or political subdivision thereof, by an agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof,

(H) qualified hydroelectric generating facilities, or

(I) qualified mass commuting vehicles.

For purposes of subparagraph (A), the term "targeted area project" means a project located in a qualified census tract (within the meaning of section 103A(k)(2)) or an area of chronic economic distress (within the meaning of section 103A(k)(3)). For purposes of subparagraph (E), the local furnishing of electric energy from a facility shall include furnishing solely within the area consisting of a city and 1 contiguous county.

(5) **Industrial parks.**—Paragraph (1) shall not apply to any obligation issued as part of an issue substantially all of the proceeds of which are to be used for the acquisition or development of land as the site for an industrial park. For purposes of the preceding sentence, the term "development of land" includes the provision of water, sewage, drainage, or similar facilities, or of transportation, power, or communication facilities, which are incidental to use of the site as an industrial park, but, except with respect to such facilities, does not include the provision of structures or buildings.

(6) Exemption for certain small issues.—

(A) **In general.**—Paragraph (1) shall not apply to any obligation issued as part of an issue the aggregate authorized face amount of which is $1,000,000 or less and substantially all of the proceeds of which are to be used (i) for the acquisition, construction, reconstruction, or improvement of land or property of a character subject to the allowance for depreciation, or (ii) to redeem part or all of a prior issue which was issued for purposes described in clause (i) or this clause.

(B) Certain prior issues taken into account.—If—

(i) the proceeds of two or more issues of obligations (whether or not the issuer of each such issue is the same) are or will be used primarily with respect to facilities located in the same incorporated municipality or located in the same county (but not in any incorporated municipality),

(ii) the principal user of such facilities is or will be the same person or two or more related persons, and

(iii) but for this subparagraph, subparagraph (A) would apply to each such issue,

then, for purposes of subparagraph (A), in determining the aggregate face amount of any later issue there shall be taken into account the face amount of obligations issued under all prior such issues and outstanding at the time of such later issue (not including as outstanding any obligation which is to be redeemed from the proceeds of the later issue).

(C) **Related persons.**—For purposes of this paragraph and paragraph (7), a person is a related person to another person if—

(i) the relationship between such persons would result in a disallowance of losses under section 267 or 707(b), or

(ii) such persons are members of the same controlled group of corporations (as defined in section 1563(a), except that "more than 50 percent" shall be substituted for "at least 80 percent" each place it appears therein).

(D) $10,000,000 limit in certain cases.—At the election of the issuer, made at such time and in such manner as the Secretary shall by regulations prescribe, with respect to any issue this paragraph shall be applied—

(i) by substituting "$10,000,000" for "$1,000,000" in subparagraph (A), and

(ii) in determining the aggregate face amount of such issue, by taking into account not only the amount described in subparagraph (B), but also the aggregate amount of capital expenditures with respect to facilities described in subparagraph (E) paid or incurred during the 6-year period beginning 3 years before the date of such issue and ending 3 years after such date (and financed otherwise than out of the proceeds of outstanding issues to which subparagraph (A) applied), as if the aggregate amount of such capital expenditures constituted the face amount of a prior outstanding issue described in subparagraph (B).

(I) Aggregate amount of capital expenditures where there is urban development action grant.—In the case of any issue substantially all of the proceeds of which are to be used to provide facilities with respect to which an urban development action grant has been made under section 119 of the Housing and Community Development Act of 1974, capital expenditures of not to exceed $10,000,000 shall not be taken into account for purposes of applying subparagraph (D)(ii).

(J) Issues for residential purposes.—This paragraph shall not apply to any obligation which is issued as a part of an issue a significant portion of the proceeds of which are to be used directly or indirectly to provide residential real property for family units.

(c) Arbitrage bonds.—

(1) Subsection (a)(1) or (2) not to apply.—Except as provided in this subsection, any arbitrage bond shall be treated as an obligation not described in subsection (a)(1) or (2).

(2) Arbitrage bond.—For purposes of this subsection, the term "arbitrage bond" means any obligation which is issued as part of an issue all or a major portion of the proceeds of which are reasonably expected to be used directly or indirectly—

(A) to acquire securities (within the meaning of section 165(g)(2)(A) or (B)) or obligations (other than obligations described in subsection (a)(1) or (2)) which may be reasonably expected at the time of issuance of such issue, to produce a yield over the term of the issue which is materially higher (taking into account any discount or premium) than the yield on obligations of such issue, or

(B) to replace funds which were used directly or indirectly to acquire securities or obligations described in subparagraph (A).

(3) Exception.—Paragraph (1) shall not apply to any obligation—

(A) which is issued as part of an issue substantially all of the proceeds of which are reasonably expected to be used to provide permanent financing for real property used or to be used for residential purposes for the personnel of an educational organization described in section 170(b)(1)(A)(ii) which grants baccalaureate or higher degrees, or to replace funds which were so used, and

(B) the yield on which over the term of the issue is not reasonably expected, at the time of issuance of such issue, to be substantially lower than the yield on obligations acquired or to be acquired in providing such financing.

This paragraph shall not apply with respect to any obligation for any period during which it is held by a person who is a substantial user of property financed by the proceeds of the issue of which such obligation is a part, or by a member of the family (within the meaning of section 318(a)(1)) of any such person.

(4) Special rules.—For purposes of paragraph (1), an obligation shall not be treated as an arbitrage bond solely by reason of the fact that—

(A) the proceeds of the issue of which such obligation is a part may be invested for a temporary period in securities or other obligations until such proceeds are needed for the purpose for which such issue was issued, or

(B) an amount of the proceeds of the issue of which such obligation is a part may be invested in securities or other obligations which are part of a reasonably required reserve or replacement fund.

The amount referred to in subparagraph (B) shall not exceed 15 percent of the proceeds of the issue of which such obligation is a part unless the issuer establishes that a higher amount is necessary.

(5) Student loan incentive payments.—Payments made by the Commissioner of Education pursuant to section 438 of the Higher Education Act of 1965 are not to be taken into account, for purposes of paragraph (2)(A), in determining yields on student loan notes.

(6) Regulations.—The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this subsection.