

File No. 110027

Committee Item No. 6
Board Item No. 7

COMMITTEE/BOARD OF SUPERVISORS
AGENDA PACKET CONTENTS LIST

Committee: Budget and Finance Committee

Date: January 26, 2011

Board of Supervisors Meeting

Date 2/1/11

Cmte Board

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| <input type="checkbox"/> | <input type="checkbox"/> | Legislative Digest |
| <input checked="" type="checkbox"/> | <input checked="" type="checkbox"/> | Budget Analyst Report |
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| <input type="checkbox"/> | <input type="checkbox"/> | Ethics Form 126 |
| <input type="checkbox"/> | <input type="checkbox"/> | Introduction Form (for hearings) |
| <input checked="" type="checkbox"/> | <input checked="" type="checkbox"/> | Department/Agency Cover Letter and/or Report |
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OTHER

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| <input checked="" type="checkbox"/> | <input type="checkbox"/> | *Settlement Agreement (Confidential) |
| <input checked="" type="checkbox"/> | <input type="checkbox"/> | * <u>Asian Art Museum Foundation Proposal (Confidential)</u> |
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Completed by: Victor Young

Date: January 21, 2011

Completed by: Victor Young

Date: 1-27-11

An asterisked item represents the cover sheet to a document that exceeds 25 pages. The complete document is in the file.

1 [Settlement of Potential Litigation - Asian Art Museum Foundation Bonds - City Assurance to
2 Seek Appropriation for Bonds - \$120,400,000]

3
4 **Resolution approving the settlement of potential litigation involving the restructuring of**
5 **the \$120,400,000 California Infrastructure and Economic Development Bank Variable**
6 **Rate Revenue Bonds, Series 2005 (Asian Art Museum Foundation of San Francisco)**
7 **(2005 Bonds) through the execution of a Settlement Agreement by and among the City**
8 **and County of San Francisco, the Asian Art Museum Foundation of San Francisco,**
9 **JPMorgan Chase Bank, National Association, MBIA Insurance Corporation, National**
10 **Public Finance Guarantee Corporation and The Bank of New York Mellon Trust**
11 **Company N.A., including, among other matters, the form of the Assurance Agreement**
12 **under which the City will support repayment of the 2005 Bonds, and other additional**
13 **material terms of such settlement.**

14
15 WHEREAS, The Asian Art Museum of San Francisco ("Museum") houses one of the
16 most important collections of Asian art not just in the United States but in the western world,
17 and averages over 300,000 visitors a year and in addition to its exceptional public art
18 exhibitions, the Museum plays an instrumental role in Asian art scholarship, conservation, and
19 education directly and through its Research Institute for Asian Art, as well as public education
20 programs for children, adults, and Asian art scholars; and,

21 WHEREAS, The Asian Art Museum is a charitable trust department of the City, and the
22 City, through its Asian Art Commission (the "Commission"), serves as trustee of Museum
23 charitable trust assets and oversees the development and administration of the Museum
24 and controlling and managing the City's Asian art collection (S.F. Charter Sections 5.100 -
25 5.101, 5.104); and,

1 WHEREAS, The City owns the Museum building and the Museum's collection; and,

2 WHEREAS, The Asian Art Museum Foundation of San Francisco ("Borrower") is a
3 private 501(c)(3) charitable organization that exists for the sole purpose of supporting the
4 Museum; and,

5 WHEREAS, On March 20, 2003, the Museum relocated from Golden Gate Park to its
6 present location in Civic Center, after having completed a rehabilitation and adaptive reuse of
7 San Francisco's former main library building; and,

8 WHEREAS, The rehabilitation of the Museum building was financed through a
9 combination of public and private financing, consisting of \$41,730,000 in City General
10 Obligation Bonds, and \$107,445,000 of Revenue Bonds, Series 2000 (Asian Art Museum
11 Foundation of San Francisco) (the "2000 Bonds") that the Borrower caused to be issued; and,

12 WHEREAS, In 2005, the Borrower refinanced the 2000 Bonds by issuing \$120,400,000
13 aggregate principal amount of Variable Rate Revenue Bonds, Series 2005 (Asian Art Museum
14 Foundation of San Francisco) (the "2005 Bonds") through the California Infrastructure and
15 Economic Development Bank (the "Issuer"), which bond obligations were insured by MBIA
16 Insurance Corporation ("MBIA") (as further described below); and,

17 WHEREAS, In 2009, the Borrower further caused a restructuring of the 2005 Bonds
18 under the terms of that certain Amended and Restated Indenture dated as of December 1,
19 2009 (the "Indenture"), between the Issuer and The Bank of New York Mellon Trust Company
20 N.A. ("Trustee") due to, among other factors, the rating downgrade of MBIA (the "Existing
21 Bonds"); and,

22 WHEREAS, In connection with a restructuring of the Existing Bonds, the Borrower and
23 JP Morgan Chase Bank (the "Bank") entered into a Reimbursement Agreement dated as of
24 December 1, 2009 (the "Reimbursement Agreement"), under which the Bank issued its
25

1 irrevocable transferrable direct pay letter of credit (the "Letter of Credit") to support the
2 payment of the Existing Bonds; and,

3 WHEREAS, MBIA issued its Financial Guaranty Insurance Policy No. 45667(1) on
4 February 3, 2005, to guarantee the scheduled payment of principal of and interest on the
5 Bonds as and when due under the terms of the Indenture, as endorsed and supplemented
6 (collectively, the "Policy"), and under the Amended and Restated Quota Share Reinsurance
7 Agreement, effective January 1, 2009 (the "Reinsurance Agreement"), between MBIA and
8 National Public Finance Guarantee Corporation ("National"), National agreed to reinsure the
9 obligations of MBIA under the Policy; and,

10 WHEREAS, The Borrower executed an interest rate swap with the Bank, as Swap
11 Counterparty, as further set forth in that certain International Swaps and Derivatives
12 Association ("ISDA") Master Agreement dated as of January 27, 2005, together with the
13 Schedule of ISDA Master Agreement and Credit Support Annex and Confirmation, each dated
14 as of January 27, 2005, as amended by the Amendment Agreement dated as of December
15 22, 2009 (collectively, the "Swap"); and,

16 WHEREAS, Events of Default have occurred and are continuing on the part of the
17 Borrower under the Reimbursement Agreement, the Amended and Restated Loan Agreement
18 dated as of December 1, 2009, between the Borrower and the Issuer, and the Insurance and
19 Reimbursement Agreement dated as of February 1, 2005, as amended, between the
20 Borrower and the Bond Insurer; and,

21 WHEREAS, The Letter of Credit expired by its terms on December 21, 2010, and as
22 such on December 20, 2010, the Bonds were subject to mandatory tender for purchase under
23 the Indenture, and the Bank became the owner of the Bonds due to a Trustee draw on the
24 Letter of Credit to pay the purchase price of the Existing Bonds; and,

1 WHEREAS, The Borrower, the Bank, the Swap Counterparty, the Trustee and the
2 Bond Insurer entered into a Forbearance Agreement and Reservation of Rights dated as of
3 December 20, 2010 (the "Forbearance Agreement"), under which the Parties agreed to
4 forbear from executing certain rights, including, without limitation, the Bank's agreement to
5 forbear exercising any rights or remedies under the Reimbursement Agreement and the
6 Indenture, during the period ending on January 21, 2011 (the "Forbearance Period), to afford
7 the parties the opportunity to explore possible work out and restructuring of the Existing
8 Bonds; and,

9 WHEREAS, The City has a vital interest in safeguarding for the public's benefit the
10 continued operation of the Museum, including its public display of art and cultural artifacts;
11 and,

12 WHEREAS, Potential litigation exists among the City, the Borrower, the Bank, MBIA,
13 National and The Bank of New York Mellon Trust Company, N.A., as trustee, involving the
14 Existing Bonds, the Swap, the Policy, the Letter of Credit and the rights and obligations of the
15 parties under those agreements and instruments; and,

16 WHEREAS, The parties now wish to fully and finally resolve their current disputes and
17 potential claims, lawsuits, rights and remedies involving the Existing Bonds (collectively, the
18 "Disputes"), by providing for a work-out solution to address the Borrower's current financial
19 situation that in accordance with that certain Term Sheet attached as Exhibit B to the
20 Settlement Agreement (as described below), which requires that: (i) the Bank, the Borrower,
21 the Trustee, MBIA and National execute and deliver a Policy Termination and Release
22 Agreement; (ii) the Bank and the Trustee agree to terminate the Policy (the "Bond Insurer
23 Termination"); (iii) subject to the terms of the Policy Termination and Release Agreement, the
24 principal amount of the Reimbursement Obligations and the 2005 Bonds will be reduced to
25 \$98,400,000; (iv) the Swap between the Swap Counterparty and the Borrower terminate at

1 the time of closing of the Loan Facility (as further described below, and herein the "Closing"),
2 and upon Closing all Swap collateral be returned to the Borrower and the Borrower will not be
3 liable for any costs associated with terminating the Swap; (v) the City commits to consider
4 providing financial support to assure the payment by the Borrower of the principal of and
5 interest under the terms of the Assurance Agreement (attached as Exhibit A to the Settlement
6 Agreement); (vi) the Bank agrees to extend credit to or for the benefit of the Borrower in the
7 form of the Loan Facility (the "Loan Facility") as described in and subject to the terms and
8 conditions of the Term Sheet, including the satisfaction of the Bond Insurer's payment
9 obligations under the Policy Termination and Release Agreement; and (vii) the parties agree
10 to mutual releases of liability, all as more particularly described in the Settlement Agreement,
11 a copy of which is on file with the Clerk of the Board of Supervisors in File No. ¹¹⁰⁰²⁷ (the
12 "Settlement Agreement"); and,

13 WHEREAS, The Settlement Agreement includes a form of Assurance Agreement
14 under which the City agrees that, upon a failure or prospective failure by the Borrower to pay
15 the principal of or interest on the Loan Facility as and when due, the Controller shall have the
16 non-discretionary ministerial obligation to take all necessary and appropriate actions to
17 prepare and, to the fullest extent possible, to request a budgetary appropriation or
18 supplemental appropriation from the Board of Supervisors to satisfy the Borrower's obligation
19 to make payments of the principal of and interest on the Loan Facility as and when due,
20 provided that the Board of Supervisors and Mayor shall have the sole discretion to approve or
21 disapprove any such appropriation or supplemental appropriation. In addition, the Bank shall
22 have certain rights to cause or recommend increases to general admission prices to the
23 Museum if the Board fails to appropriate sums under the Assurance Agreement, all as more
24 particularly set forth in the form of Assurance Agreement on file with the Clerk of the Board;
25 and,

1
2 WHEREAS, The Mayor and the Controller have negotiated and proposed the
3 settlement of the Disputes, and the City Attorney has recommended the proposed settlement,
4 upon the terms and conditions set forth in the Settlement Agreement, which includes, among
5 other matters, City support for the Borrower's payments of the Loan Facility on the terms and
6 conditions set forth in the Assurance Agreement attached to the Settlement Agreement; now,
7 therefore, be it

8 RESOLVED, That under Section 10.22 of the San Francisco Administrative Code, the
9 Board approves the settlement and compromise of the Disputes in accordance with the terms
10 and conditions set forth in the Settlement Agreement; and,

11 RESOLVED, That the Controller is authorized to execute and deliver the Settlement
12 Agreement, including the Assurance Agreement, in substantially the form of those
13 agreements on file with the Clerk of the Board in File No. 110027; and, be it further

14 RESOLVED, That the Controller and the Director of Public Finance and all other
15 appropriate officers and employees and representatives of the City are authorized and
16 directed, upon consultation with the City Attorney, to do everything necessary or appropriate,
17 including the execution of documents and certificates, to effectuate the purposes of this
18 resolution, provided that such officers will not take any actions or agree to any changes in the
19 agreements approved under this resolution that would materially increase the obligations or

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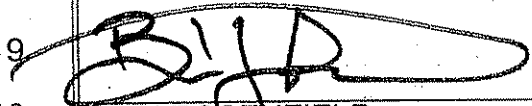
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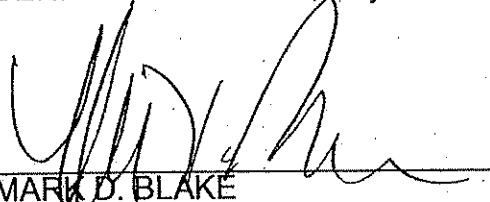
1 liabilities of the City under the terms and conditions of the Settlement Agreement on file with
2 the Clerk of the Board in File No. 110027, and changes to the agreements shall be approved
3 by the City Attorney.

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RECOMMENDED:
OFFICE OF THE CONTROLLER


BEN ROSENFELD
Controller

APPROVED:
DENNIS J. HERRERA, City Attorney


MARK D. BLAKE
Deputy City Attorney

Item 6
File 11-0027

Departments:
Asian Art Museum (AAM), Controller,
Office of Public Finance (OPF)

EXECUTIVE SUMMARY

Legislative Objectives

- The proposed resolution would authorize a settlement of potential litigation involving the restructuring of the \$120.4 million California Infrastructure and Economic Development Bank Variable Rate Revenue Bonds, Series 2005 ("2005 Bonds"), issued by the Asian Art Museum Foundation of San Francisco ("the Foundation"), through the execution of a Settlement Agreement by and among the City and County of San Francisco, the Foundation; JPMorgan Chase Bank, National Association; MBIA Insurance Corporation; National Public Finance Guarantee Corporation; and the Bank of New York Mellon Trust Company, N.A.; including an Assurance Agreement between the City and JP Morgan Chase Bank, National Association, under which the City would be required to consider repayment of the 2005 Bonds if the Foundation is unable to pay off this debt.

Key Points

- The Asian Art Museum Commission ("Commission") also serves as the Board of Directors for the Asian Art Museum Foundation of San Francisco ("the Foundation"), a 501(c)3 nonprofit organization whose responsibilities include raising private funds for the Asian Art Museum (AAM). Funds raised are used to provide support for the Museum's annual operating budget and for long-term capital improvements and acquisitions. The Foundation contributed \$11.1 million, or 61 percent of the Asian Art Museum's annual operating budget of \$18.2 million in FY 2010-2011, with the remaining \$7.1 million, or 39 percent provided by the City.
- In 2000, the Foundation issued \$107.4 million in fixed-rate revenue bonds ("2000 Bonds") to provide funds for moving the Asian Art Museum from Golden Gate Park to the old City Main Library on Larkin Street. In 2005, the Foundation issued \$120.4 million in variable rate bonds ("2005 Bonds") to refinance the outstanding balance on the 2000 Bonds. JPMorgan Chase Bank, National Association ("JPMorgan") was appointed remarketing agent for the 2005 Bonds. The 2005 Bonds were insured as to payment of principal and interest by MBIA Insurance Corporation. The 2005 Bonds were also supported with a standby bond purchase agreement provided by JPMorgan. In order to secure a low fixed percentage rate, the Foundation entered into an interest rate swap agreement with JPMorgan.
- Due to a number of factors (see Background section below), the Foundation is no longer able to meet its debt service obligation on the 2005 Bonds. In December 2010, JP Morgan tendered the outstanding bonds and demanded that the \$119.4 million, still owed, be repaid in full in five years. As of November 2010, the Foundation had \$78.5 million in unrestricted assets and, even with projected private fundraising, did not believe it could pay off the debt in five years and continue to provide the level of support that it has been providing to the AAM's annual operating budget.
- The City, the Foundation, JP Morgan, and the other parties to the 2005 bond debt issuance have negotiated a proposed Settlement Agreement that would reduce the Foundation's obligation to JPMorgan by \$21 million to \$98.4 million from \$119.4 million and reduce the interest rate paid by the Foundation to a fixed rate of 4.6 percent, to be paid off over 30 years instead of the 23 year term that remained on the Foundation's variable rate debt agreement prior to December 2010. A separate signed Assurance Agreement, which is exclusively between the City and JPMorgan, in

which the City guarantees that it will consider repaying JP Morgan in the event the Foundation is unable to repay the debt, is a condition of the Settlement Agreement. Both the Settlement Agreement and Assurance Agreement are conditional on the City's willingness to provide financial support to the Foundation and to consider paying off the outstanding debt in the event the Foundation cannot meet its financial obligation to JPMorgan.

- The City, rather than the Foundation, is the owner of the AAM building and the AAM artwork. Were the Foundation to be required to liquidate its assets, the City is not at risk of losing the AAM building or the artwork. However, the City Charter would continue to require the City to maintain, display, and provide security for its Asian art collection without support for the annual operating budget now provided by the Foundation.
- Under the proposed Assurance Agreement, in the event that the Foundation cannot meet its obligation, the Controller would be required to request a General Fund payment from the Board of Supervisors to JPMorgan for any outstanding payments owed by the Foundation.
- The City's total maximum exposure, according to the City's Office of Public Finance (OPF), is the total debt obligation, less the Foundation's unrestricted assets. Given the best available estimation of the current value of the Foundation's unrestricted assets, which is \$78.5 million, and the \$98.4 million in outstanding debt obligation under the proposed Settlement Agreement, the City's current exposure is \$19.9 million (\$98.4 million minus \$78.5 million). However, the City Attorney's Office notes that if the Foundation's assets should be diminished, such as in the event of a loss in the Foundation's investment portfolio, the City's exposure could exceed \$19.9 million.
- The proposed Settlement Agreement automatically expires on February 11, 2011, unless approved by the Board of Supervisors prior to that.
- If the Board of Supervisors does not approve the proposed Settlement Agreement and Assurance Agreement, the Controller and OPF report that the City's borrowing rate could be negatively impacted. Furthermore, maintaining a constant level of service at the AAM would require additional City support for the AAM through the City's Annual Appropriation Ordinance based on the City's annual budget approved by the Board of Supervisors.
- According to the OPF, the proposed Settlement Agreement is without precedent in San Francisco, and may be without precedent beyond San Francisco.
- While neither the Settlement Agreement nor the Assurance Agreement specifically require that the Foundation reimburse the City in the event the Foundation fails to meet its financial obligations to JPMorgan, the City Attorney has advised that the Foundation's legal repayment obligations under these two proposed agreements will be codified subsequent to approval of the subject proposed resolution by the Board of Supervisors in a forthcoming amendment to the existing Museum Project Facilitation Agreement between the Commission and the Foundation.

Fiscal Impacts

- If the Foundation meets all its obligations to JPMorgan under the proposed Settlement Agreement, there would be no fiscal impact to the City. However, if the Foundation should default on its loan repayments, the Controller would be required, under the proposed Settlement Agreement and Assurance Agreement, to request appropriation authorization from the Board of Supervisors to reimburse JPMorgan from the General Fund in the amount left outstanding. Based on the current estimated value of the Foundation's unrestricted assets, the maximum risk to the General Fund is

approximately \$19.9 million.

Recommendation

- The Budget and Legislative Analyst considers approval of the proposed resolution to be a policy decision for the Board of Supervisors.

MANDATE STATEMENT AND BACKGROUND**Mandate Statement**

In accordance with City Charter Section 10.22, "any unlitigated claim against the City and County in excess of \$25,000 may be allowed or settled and compromised on the written recommendation of the head of the department or of the board or commission in charge of the department against which the claim is made, with the written approval of the City Attorney and the approval of the Board of Supervisors by resolution." Furthermore, City Charter Section 10.22 states "No claim shall be paid until the Controller shall certify that monies are available from the proper funds or appropriations to pay the claim as allowed or as compromised and settled."

Background

The Asian Art Museum (AAM) is a Charitable Trust Department defined by Section 5.101 of the City Charter, granting them exclusive charge of the trusts and other assets under their jurisdiction. Section 5.104 of the City Charter established the Asian Art Commission ("Commission"), consisting of 27 trustees appointed by the Mayor. According to Section 5.104 of the Charter, the Commission is charged with:

1. Developing and administering the AAM;
2. Controlling and managing the City and County's Asian art, consistent with the conditions applicable to the Avery Brundage Collection and other gifts;
3. Maintaining the Asian Art Museum Foundation ("the Foundation"), a private 510(c)(3) nonprofit organization that serves as the main fundraising entity for the AAM; and
4. Other responsibilities regarding acquiring Asian art objects and establishing the AAM as "the outstanding center of Asian art and culture in the western world."

Section 16.106 of the City Charter requires the Board of Supervisors to annually appropriate an operating budget for the AAM, in "an amount sufficient for the purpose of maintaining, displaying, and providing for the security of the City and County's collection of Asian art." The AAM's FY 2010-2011 budget is \$18.2 million, of which approximately \$7.1 million (39 percent) was appropriated by the City and \$11.1 million (61 percent) was contributed by the Foundation.

The 2000 and 2005 Bond Issuances, and the Expiration of the Foundation's Letter of Credit

In 2000, the Foundation issued \$107.4 million in fixed-rate revenue bonds ("2000 Bonds") to provide funds for moving the AAM from Golden Gate Park to the old City Main Library on Larkin Street. The revenue bonds were issued through the California Infrastructure and Economic Development Bank (the "I-Bank").

In 2005, the Foundation, through the I-Bank, issued \$120.4 million variable rate bonds ("2005 Bonds") to refinance the outstanding balance on the 2000 Bonds. JPMorgan Chase Bank,

National Association (“JPMorgan”) was appointed remarketing agent for the 2005 Bonds. The 2005 Bonds were insured as to payment of principal and interest by MBIA Insurance Corporation (MBIA). The 2005 Bonds were also supported with a standby bond purchase agreement provided by JPMorgan.

In order to secure a low fixed percentage rate, the Foundation entered into an interest rate swap agreement with JPMorgan (the “Swap”). Under the terms of the Swap, the Foundation was to pay a fixed rate of 3.364 percent to its swap partner who would pay an amount designed to offset the variable interest rate. Therefore, according to Mr. Mark McLoughlin,¹ Chief Operating Officer and Chief Financial Officer of the Foundation, the Foundation believed that, although it had issued \$120.4 million in variable rate debt, it was reasonably assured of paying a low fixed interest rate and sufficiently insulated from actually paying a varying rate on its debt.

Several factors have upset the Swap and the Foundation’s repayment of the 2005 Bonds, including the following:

- In 2008, MBIA, the Bond Insurer, had its credit rating downgraded during the U.S. financial crisis. Once MBIA was downgraded and the market shifted, MBIA was no longer able to insure the Swap, therefore requiring the Foundation to post \$20.0 million in collateral with JPMorgan.
- With the downgrading of the Bond Insurer’s credit rating, the Foundation no longer paid a predictable fixed low rate of 3.364 percent, and saw the variable rate it was paying on the debt increase to as high as 9 percent according to Mr. McLoughlin.
- In 2009, the Foundation restructured the 2005 Bonds and entered into a direct-pay letter of credit with JPMorgan. According to the Controller and Office of Public Finance (OPF), “the purpose of the letter of credit was to cure an event of default due to the downgrade of the Bond Insurer.” The letter of credit had an expiration date of December 21, 2010.
- In November 2010, Moody’s Investors Services warned of a possible reduction in the Foundation’s credit rating, and on December 17, 2010, Moody’s reduced the Foundation’s credit rating to junk status, dropping it to Ba1 from Baal, due to the Foundation’s letter of credit expiring on December 21, 2010.²
- The Foundation has experienced events of default in its repayment of the 2005 Bonds to JPMorgan.

On December 21, 2010, with \$119.4 million in outstanding 2005 bonds, the Foundation’s letter of credit with JPMorgan expired. With the expiration of the letter of credit, the \$119.4 million in outstanding 2005 Bonds were tendered by JPMorgan. The Foundation would have been required by its agreement with JP Morgan to repay the \$119.4 million over a five-year rapid amortization period, rather than the 23-year remaining period that had existed prior to the expiration of the letter of credit. The Foundation, which, as shown in Table 1 below, has only \$78.5 million in total unrestricted assets, would not have been able to fully repay the \$119.4 million, plus accruing interest, within five years.

¹ Mr. McLoughlin was not Chief Operating Officer and Chief Financial Officer of the Foundation at the time the variable rate debt was issued in 2005.

² Moody’s increased the Foundation’s credit rating to Aa3 on December 22, 2010.

The City and County of San Francisco, the Foundation; JPMorgan; MBIA Insurance Corporation; National Public Finance Guarantee Corporation; and the Bank of New York Mellon Trust Company, N.A. ("the six parties") executed a one-month Forbearance Agreement on December 20, 2010 to arrange for a financial solution between all of the interested parties. As noted on Page 3 of the January 6, 2011 Controller and OPF memorandum to the Board of Supervisors, the six parties entered into a non-binding Term Sheet which formed the basis of the proposed Settlement Agreement and Assurance Agreement.

Current Limits to the City's Exposure

The AAM building, located at 200 Larkin Street, and the AAM art collection are the property of the City, not the Foundation. Therefore, under all existing arrangements, if the Foundation were to default on the 2005 Bonds, or any other legal or financial obligations, the Foundation's creditors could not possess the AAM's art collection or the AAM building as collateral. Creditors could pursue the Foundation's approximately \$78.5 million in unrestricted assets, summarized in Table 1, below.

**Table 1. Estimated Value of Foundation's Unrestricted Assets,
Less Obligations, as of November 30, 2010**

Asset/Obligation	Estimated Value (Millions)
Unrestricted investments	\$69.9
Debt reserve fund	7.7
Property and equipment	2.6
Miscellaneous	0.7
Payables and accruals	(1.2)
Deferred revenue and deposits	(0.8)
Interest payable (current bond)	(0.4)
Total	\$78.5

* Includes \$15 million swap collateral at to be returned to the Foundation upon signing of the Settlement Agreement.

Source: Asian Art Museum

However, as noted on page 4 of the January 6, 2011 Controller and OPF memorandum to the Board of Supervisors, it is the opinion of the Controller and the OPF that "it is likely that the cost to the City of accessing the capital markets would be adversely affected if the Foundation were permitted to proceed with liquidation upon a default under the 2005 bonds." Furthermore, the Controller and OPF note that if the Foundation was unable to provide the AAM with what is approximately 61 percent of its annual operating budget, the City would need to increase its support of the AAM if a constant level of service was to be provided.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would authorize a settlement of potential litigation involving the restructuring of the \$120,400,000 California Infrastructure and Economic Development Bank Variable Rate Revenue Bonds, Series 2005 ("2005 Bonds"), issued by the Foundation, through the execution of a Settlement Agreement by and among the City and County of San Francisco; the Foundation; JPMorgan; MBIA Insurance Corporation; National Public Finance Guarantee Corporation; and the Bank of New York Mellon Trust Company, N.A. ("the six parties"). The proposed resolution would also authorize a separate Assurance Agreement between the City and JP Morgan only, under which the City would be required to consider repayment of the 2005 Bonds in the event that the Foundation is unable to pay off its outstanding debt.

The Proposed Settlement Agreement between the Six Parties

Under the Proposed Settlement Agreement, JPMorgan would forgive \$21 million of the Foundation's \$119.4 million debt and refinance the remaining \$98.4 million through a 30-year, fixed rate loan at an interest rate of 4.6 percent. As a guarantee to the bank, the City would agree that it would provide financial support to assure the repayment by the Foundation to JPMorgan of both the principal and the interest, as set forth in the Assurance Agreement.

The Foundation would be required to meet numerous conditions listed in the Settlement Agreement. Under Article 5 of the proposed Settlement Agreement, the Foundation would be required to:

1. "Use its reasonable best efforts" to execute a three-year capital campaign in order to generate \$20 million in new, unrestricted assets;
2. Hire , at its own expense and not in an amount greater than \$250,000, a management consultant with expertise in museum operations, subject to the approval of both the City and the Bank, to conduct a management consulting review of the Foundation's operations, charitable gift development, and governance, to be completed by June 30, 2011;
3. Appoint City officials with financial expertise to serve as non-voting members of the Foundation's investment and capital committees; and
4. Receive the approval of the City's Controller for any significant changes to the AAM's annual budget or any significant sale of the Foundation's assets.

If the Foundation fails to make its annual loan payment to JPMorgan, in full, according to the Amortization Schedule contained in the Term Sheet to the proposed Settlement Agreement, the City would be required to make up the difference, per the Assurance Agreement described below. If neither the Foundation nor the City makes the required payment to JPMorgan (even though the City is obligated to consider repayment to JP Morgan of all outstanding Foundation debt under the terms of the Assurance Agreement, described further below), then:

- 1.J PMorgan, at its discretion, may: (isn't the City liable??)
- a. Appoint a Chief Restructuring Officer to the Foundation to assist the Foundation on matters including finances, operations, and other AAM operations;
 - b. Appoint a person with financial expertise to serve as a non-voting member of the Foundation's Investment and Capital Campaign Committees; and
 - c. Audit, inspect, and review any or all of the books, records, and documents relating to the AAM and the Foundation, its finances and operations.
- 2.The Foundation would be required to obtain JPMorgan's written approval for the Foundation's annual budget; any significant changes to the budget; and any significant asset sales.
- 3.J PMorgan would have the right to cause the Foundation to raise ticket prices, fees, or donations for general admission in line with the average of the top three more expensive non-profit museums in California accredited by the American Association of Museums.

The Assurance Agreement between the City and JPMorgan

In addition to the Settlement Agreement, the proposed resolution would authorize the City to enter into an Assurance Agreement directly with JPMorgan,³ committing the City to consider providing financial support for the Foundation's obligations to make scheduled payments to JPMorgan. Any financial support required under the Assurance Agreement would be subject to appropriation approval of the Board of Supervisors. The City entering into the Assurance Agreement is a condition of the proposed Settlement Agreement.

Under Section 1.3 of the Assurance Agreement, JPMorgan would pursue payment from the City on behalf of the Foundation in the event of any of the following conditions:

- 1.The Foundation fails to make any scheduled payment of interest and/or principal, as specified under the Amortization Schedule; or
- 2.J PMorgan notifies the City that it has drawn on the Foundation's Debt Service Reserve Fund, established in accordance with the proposed Settlement Agreement, and the Debt Service Reserve Fund has not been replenished by the Foundation as required by the terms of the Settlement Agreement, or there were insufficient funds in the Debt Service Reserve Fund; or
- 3.The Controller determines that the Foundation has insufficient funds to repay JPMorgan according to the Amortization Schedule, upon the Controller's review of the Foundation's annual budget, which is required under the Settlement Agreement.

³ As prepared, the Foundation would not be party to the Assurance Agreement. However, Ms. Sesay notes that the City and JPMorgan are considering requesting the Foundation to sign on as an acknowledgment of the Agreement.

Within 30 days of any of the three conditions being met, the Controller would have a “non-discretionary ministerial obligation” to prepare and request a budgetary appropriation or supplemental appropriation from the Board of Supervisors, in order to repay any outstanding amount due by the Foundation to JPMorgan. The Assurance Agreement states that “the Board of Supervisors shall have the sole discretion to approve or disapprove any such appropriation or supplemental appropriation.”

If the Board of Supervisors does not approve the Controller’s budgetary request, the following would occur under the Assurance Agreement:

1. The Controller would be required to make additional requests to the Board of Supervisors for a budgetary appropriation or supplemental appropriation for all outstanding amounts owed from the Foundation to JPMorgan, not more frequently than every six months;
2. J PMorgan “in its sole discretion shall have the right and power to pursue all rights, claims, causes of action available under law or in equity, including, without limitation, a writ of mandamus;”⁴
3. J PMorgan would retain the right to require the Foundation to raise the ticket fees, prices, or donations for admission under the criteria described in the Settlement Agreement; and
4. The Foundation and the City would be required to receive JPMorgan’s permission to execute any wholesale relocation of the AAM’s artwork, and JPMorgan would retain the right to refuse such a relocation of artwork if it determined that the relocation of artwork would have a negative material impact on JPMorgan’s financial interests.

Additionally, if any of the three Assurance Agreement conditions, detailed above on page 8 of this report, are met, at the City’s request, JPMorgan agrees to work with the City to refinance any remaining outstanding debt, provided the refinancing is “at no loss, cost or expense to the Bank.”

The proposed Assurance Agreement would expire upon payment, in full, of all obligations from either the Foundation or the City to JPMorgan.

February 11, 2011 Outside Approval Date

As specified in Section 2.3 of the proposed Settlement Agreement, if the Board of Supervisors does not approve the proposed resolution approving the proposed Settlement Agreement and Assurance Agreement on February 11, 2011 (the “Outside Approval Date”), the proposed Settlement Agreement would automatically terminate, and the six parties would revert to whatever rights, remedies and obligations they have at law or in equity. If they agreed to do so, the six parties could agree to extend the Outside Approval Date, provided that the agreement was made in writing.

⁴ A court order compelling the City to take certain actions.

Effective Date of the Settlement Agreement

If the Board of Supervisors approves the proposed resolution, the effective date of the Settlement Agreement would be the same date that the resolution becomes effective.

FISCAL IMPACTS

The fiscal impact on the City of the proposed Settlement Agreement and the Assurance Agreement are conditional on the Foundation's ability to repay its loan to JPMorgan under the terms of the Settlement Agreement. According to the Term Sheet to the Agreement, between the Foundation and JPMorgan, the Foundation's annual debt service would commence in 2012 and last for 30 years, with the Foundation making its final payment in 2041. According to the Amortization Schedule, the Foundation would pay a reduced amount in the first two years of debt service of \$4.6 million in the first year and \$5.6 million in the second year. Beginning in the third year the Foundation would make annual payments to JPMorgan between \$6.24 and \$6.26 million, in accordance with Amortization Schedule.

If the Foundation is able to make its payments and meet all additional requirements of the Foundation as specified in the proposed Settlement Agreement and Term Sheet, there would be no direct cost to the City.

However, if any of the three Assurance Agreement conditions, listed above on page 8 above, are met, where the Foundation is not able to meet its financial obligations to JPMorgan, the City would be required to consider repaying JP Morgan the entire outstanding balance, per the terms of the proposed Settlement Agreement and Assurance Agreement, as described above.

According to Ms. Nadia Sesay, the City's Director of Public Finance, the City's maximum exposure, if the proposed resolution is approved, is the amount of debt less the Foundation's unrestricted assets. According to Mr. McLoughlin, as of November 30, 2010, the Foundation's unrestricted assets totaled \$78.5 million, as summarized in Table 1 above. As the debt amount owed by the Foundation to JP Morgan would be \$98.4 million under the proposed settlement, the City's estimated maximum exposure, under the proposed Settlement Agreement and corresponding Assurance Agreement would be \$19.9 million.

However, the City Attorney's Office notes that if the Foundation's assets should be diminished, such as in the event of a loss in the Foundation's investment portfolio, the City's exposure could exceed \$19.9 million to an amount between \$19.9 million and \$98.4 million.

In the event that the Foundation is able to successfully complete the Settlement Agreement-required three-year capital campaign, with its goal of raising \$20.0 million in new, unrestricted funds, and provided that the rate of return on the Foundation's investments exceeds 6.0 percent, the City's absolute financial risk would be at or approximately \$0, per the requirements of the Settlement Agreement and Assurance Agreement. However, although the Foundation would be legally obliged to liquidate its assets in the event of default, neither the proposed Settlement Agreement nor the proposed Assurance Agreement preclude the City from intervening in order

to repay the Foundation's debt, at any point in the debt repayment (see Policy Considerations below).

Repayment from the Foundation to the City

According to the Section 1.7 of the Assurance Agreement, the City would be entitled to seek full and complete repayment from the Foundation for any amount that the City pays to JPMorgan; however, any such payment would be conditional on (a) the Foundation having first reimbursed JPMorgan, in full, for its new \$98.4 million loan, and (b) the Foundation's ability to reimburse the City following full repayment of the new loan. Furthermore, despite this clause in the Assurance Agreement, the Foundation does not, as of January 20, 2011, have a legal obligation to reimburse the City (see Policy Considerations section below). The Foundation is not a party to the Assurance Agreement.

POLICY CONSIDERATIONS

The Proposed Settlement Agreement Automatically Expires on February 11, 2011, unless Approved by the Board of Supervisors

As noted above, if the Board of Supervisors does not approve the proposed resolution that would approve the proposed Settlement Agreement by the Outside Approval Date of February 11, 2011, the proposed Settlement Agreement would automatically terminate, and the six parties would revert to whatever rights, remedies, and obligations they have at law or in equity. However, the six parties could agree to extend the Outside Approval Date, if the agreement is made in writing.

Failure to Enter Into the Proposed Settlement Agreement and Assurance Agreement Could Have Negative Fiscal Consequences for the City

As highlighted in the January 6, 2011 memorandum from the Controller and OPF to the Board of Supervisors, it is the opinion of the Controller and the OPF that "it is likely that the cost to the City of accessing the capital markets would be adversely affected if the Foundation were permitted to proceed with liquidation upon a default under the 2005 bonds." Furthermore, the Controller and OPF note that if the Foundation was unable to provide the AAM with what is approximately 61 percent of its annual operating budget, and if the City desired to maintain a constant level of service at the AAM, the City would need to increase its support of the AAM through the City's Annual Appropriation Ordinance based on the City's annual budget as approved by the Board of Supervisors.

The Proposed Settlement Agreement Is Without Precedent in the City, and May Be Without Precedent Beyond San Francisco

According to Ms. Sesay, the proposed Settlement Agreement and Assurance Agreement, in which the City is guaranteeing the financial obligations of the nonprofit Foundation in the amount of an estimated \$19.9 million, is without precedent in the City, and may be without precedent altogether. Ms. Sesay stated that the City has never provided an assurance for financial or debt obligations for a private nonprofit or other entity at this level of debt. Furthermore, as the

OPF, Controller, and City Attorney's Office worked to help craft the proposed Settlement Agreement, none of these departments were aware of a precedent for the proposed Settlement Agreement occurring in other jurisdictions.

The Budget and Legislative Analyst therefore notes that approving the proposed Settlement Agreement and Assurance Agreement, from which the City would rely on General Fund monies to guarantee loan repayments to a bank on behalf of the private Asian Arts Museum Foundation, could establish a precedent for guaranteeing future similar loans or debt repayments owed by other private nonprofit or other entities, whether or not they are connected to one of the City's Charitable Trust Departments.⁵ If the Board of Supervisors approves the proposed resolution, it is possible that other private nonprofit and other organizations may request similar financial backing in the form of General Fund guarantees from the City. However, the Board of Supervisors would not be under any obligation to provide financial guarantees to other organizations if it approves the proposed Settlement Agreement and Assurance Agreement.

Given that the global recession has impacted the financial security of numerous museums, nationwide, and given that the City has formal relationships with other museums, in addition to the Charitable Trust Departments, and, because the requested loan assurance would be the first time that the City has used General Fund dollars to guarantee a private loan of this magnitude, which could potentially create a precedent for such future requests, the Budget and Legislative Analyst considers approval of the proposed resolution to be a policy matter for the Board of Supervisors.

**Neither the Proposed Settlement Agreement or the Assurance Agreement
Preclude the City from Using General Fund Monies to Prevent the Liquidation of
the Foundation's Unrestricted Assets**

The proposed Settlement Agreement would legally oblige the Foundation to repay its debt to JPMorgan, including repayment through the liquidation of the Foundation's unrestricted assets in the event that the Foundation is not able to make a scheduled payment to JPMorgan. However, as noted above, neither the proposed Settlement Agreement nor the proposed Assurance Agreement preclude the City from using General Fund monies to prevent the liquidation of the Foundation's unrestricted assets, or at any point prior to or following default.

The Budget and Legislative Analyst observes that, in the event that the Foundation cannot make a payment to JPMorgan and either enters into or is likely to enter into default, requiring the liquidation of the Foundation's unrestricted assets, including those assets listed in Table 1 above, the City could use General Fund monies to repay JPMorgan, prior to the liquidation of the Foundation's assets.

As is noted above, the six parties' estimation of the Foundation's ability to repay the \$98.4 million refinanced loan to JPMorgan includes the Foundation's ability, with the City's help, to raise \$20 million in new, unrestricted donations, in three years.

⁵ Other Charitable Trust Departments include the Fine Arts Museums of San Francisco and the War Memorial and Performing Arts Center.

As of January 20, 2011, the Foundation Is Not Under a Legal Obligation to Reimburse the City in the Event the Foundation Does Not Meet its Obligations and the City pays off some or all of the Foundation's Debt to JP Morgan

As noted in the Fiscal Impact section above, according to the Section 1.7 of the Assurance Agreement, the City would be entitled to seek full and complete repayment from the Foundation for any amount that the City pays to JPMorgan; however, any such payment would be conditional on (a) the Foundation having first reimbursed JPMorgan, in full, for the 2011 Loan, and (b) the Foundation's ability to reimburse the City following full repayment of the 2011 loan. However, the proposed Settlement Agreement does not obligate the Foundation to repay the City in the event that the City provides fiscal assistance to the Foundation for the repayment of its obligations to JPMorgan.

As noted in the Fiscal Impact section above, the estimated exposure to the City is \$19.9 million, assuming that the Foundation's present assets are as described in Table 1.

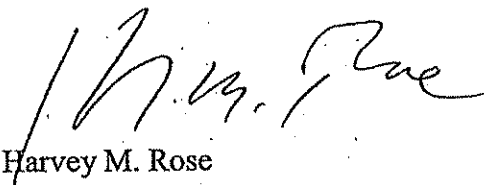
According to Ms. Sesay, prior to the execution of the proposed Settlement Agreement and Assurance Agreement, the City and the Foundation would agree on amendments to the Museum Project Facilitation Agreement⁶ that would specify the terms under which the Foundation would be required to reimburse the City for any payment that the City makes to JPMorgan on the Foundation's behalf, whether under obligation of the proposed Settlement Agreement and Assurance Agreement or otherwise. However, as of the preparation of this report on January 20, 2011, the specific language addressing the requirement that the AAM repay the City has not been drafted.

According to Mr. Blake, if the Board of Supervisors approves the proposed resolution, the Commission and Foundation will proceed with the drafting of modified terms for its existing Museum Project Facilitation Agreement. Mr. Blake further states that the terms of the modified language would follow the terms set forth in the Settlement Agreement. Therefore, in addition to addressing the issue of the Foundation repaying the City in the event the City pays off some of the Foundation's debt to JP Morgan, the modified Museum Project Facilitation Agreement will set the terms for the enhanced oversight of the Foundation by the City set forth in the Settlement Agreement. Once language is finalized, the Commission and Foundation will need to each approve the amended Museum Project Facilitation Agreement. However, as of January 20, 2011, the Budget and Legislative Analyst was not provided with any proposed language to modify the Museum Project Facilitation Agreement.

⁶ The Museum Project Facilitation Agreement between the City, through the Asian Art Museum Commission and the Foundation, specified the terms of the 2000 bonds. The agreement has not been updated since September 8, 2000.

RECOMMENDATION

The Budget and Legislative Analyst considers approval of the proposed resolution to be a policy decision for the Board of Supervisors.



Harvey M. Rose

cc: Supervisor Chu
Supervisor Mirkarimi
Supervisor Kim
President Chiu
Supervisor Avalos
Supervisor Campos
Supervisor Cohen
Supervisor Elsbernd
Supervisor Farrell
Supervisor Mar
Supervisor Wiener
Clerk of the Board
Cheryl Adams
Controller
Greg Wagner



CITY AND COUNTY OF SAN FRANCISCO
OFFICE OF THE CONTROLLER

Ben Rosenfield
Controller

Monique Zmuda
Deputy Controller

Nadia Sesay
Director
Office of Public Finance

MEMORANDUM

TO: Board of Supervisors

FROM: Ben Rosenfield, City Controller *BR*
Nadia Sesay, Director of Public Finance *NS*

SUBJECT: Resolution Approving the Settlement of Potential Litigation Involving the Restructuring of Asian Art Museum Foundation Bonds, including City Assurance to Seek Appropriation, if needed, for such Bonds

DATE: January 6, 2011

Recommended Action:

The Controller's Office respectfully requests consideration of the attached resolution and supporting documents by the Budget and Finance Committee of the Board of Supervisors on or before January 26, 2011 and approval of the Resolution at the Board of Supervisors on or before February 8, 2011. As mentioned below, JPMorgan Chase Bank's (the "Bank") offer reflected in the Term Sheet expires on February 11, 2011.

Background:

The Asian Art Museum of San Francisco (the "Museum") with more than 17,000 objects houses one of the most important collections of Asian art in the western world, including the more than 7,700 of Asian art objects donated by Avery Brundage. The Museum is a charitable trust department of the City and County of San Francisco (the "City"), and the City, through its Asian Art Commission (the "Commission"), serves as trustee of Museum charitable trust assets; oversees the development and administration of the Museum, and controls and manages the City's Asian art collection. (Charter section 5.104). The City owns the Museum building and the Museum's collection. Under the City Charter, the Board of Supervisors is responsible for appropriating each year sufficient funds for "maintaining, displaying, and providing for the security of the City's collection of Asian art." (Charter section 16.106).

The Asian Art Museum Foundation of San Francisco (the "Foundation") is a non-profit public benefit corporation that serves as the fundraising arm of for the benefit of the Museum. The City's Charter requires that the Commission "maintain a charitable foundation or other legal entity for the purpose of developing the Asian Art Museum." (Charter section 5.104(3).)

The current annual budget of the Museum is \$18.2 million. The Foundation contributes \$11.1 million toward that budget. The City pays the remainder through General Fund appropriations.

In 2003, the Museum relocated from Golden Gate Park to its present location in the Civic Center Complex, at 200 Larkin Street, after having completed the rehabilitation of the San Francisco's former

main library building. The rehabilitation of the Museum was financed with a combination of funds from the Foundation and the City.

In 1994, voters approved Proposition B, which authorized the issuance of \$41.7 million in general obligation bonds for the Asian Art Museum. The City issued \$25.0 million of bonds in 1996 and the remaining \$16.7 million in 1999. The Museum also received funds from Proposition A (Public Buildings Safety Improvement Bonds, 1989).

In 2000, the Foundation, through the California Infrastructure and Economic Development Bank (the "I-Bank"), issued \$107.4 million in fixed-rate bonds to finance the design and construction of the project to renovate the Old Main Library for the Museum (the "2000 Bonds").

Also in 2000, the Commission and the Foundation entered into a Museum Facilitation Agreement, which describes how the Commission and Foundation will coordinate their activities in the new building for the Museum. Under that agreement the Foundation has certain rights to sponsor special exhibitions, operate a museum store, and rent the Museum building for special events, and retain the revenues from those activities.

In 2005, the Foundation, through the I-Bank, issued \$120.4 million in variable rate bonds to refinance the 2000 Bonds (the "2005 Bonds"). The Bank was appointed remarketing agent for the 2005 Bonds. The 2005 Bonds were insured as to payment of principal and interest by MBIA Insurance Corporation (the "Bond Insurer"), an further supported with a standby bond purchase agreement (liquidity facility) provided by the Bank. The Foundation also entered into an interest rate swap (the "Swap") with the Bank. Under the terms of the Swap, the Foundation pays a fixed rate of 3.364% and receives 62.5% of the LIBOR Index plus 16 basis points.

In 2009, due to, among other factors, illiquidity in the municipal bond market (as further described below under "Recent Events") the Foundation restructured the 2005 Bonds and entered into a direct-pay letter of credit agreement with the Bank. The purpose of the letter of credit was to cure an event of default due to the credit downgrade of the Bond Insurer (now reinsured by National Public Finance Guarantee). As a result, the Foundation was required to post collateral against the termination value of the Swap, and has had to post as much as \$20 million to satisfy the collateral posting requirements of the Swap. The combined effects of the market illiquidity, losses on its investments and collateral posting required under the Swap created significant and ongoing financial challenges for the Foundation, including its ability to pay debt service on the 2005 Bonds.

On December 21, 2010 the letter of credit expired, and no alternative sources of credit support for the bonds were available. On December 20, 2010 the 2005 Bonds were subject to mandatory tender due to the expiration of the letter of credit. As such, \$119.4 million of the 2005 Bonds remain outstanding, and as a result of a mandatory tender are all owned by the Bank. As of December 2010, the Foundation had posted approximately \$13 million in collateral against the termination value of the Swap. The 2005 Bonds are solely obligations of the Foundation, and no credit or revenues of the City are pledged for their repayment.

Recent Developments:

As a result of events related to the 2008 credit market and economic crisis, the Foundation experienced losses in its investment portfolio making it impossible to fully pay down its \$119.4 million in outstanding 2005 Bonds.

In addition, in December 2010, Moody's downgraded the Foundation's underlying credit to "Ba1" (below investment grade) from "Baa1". The rating is on watch list for further downgrade and Moody's expects to

review the rating again within 90 days. Standard and Poor's gives the Foundation an underlying credit rating of "A-".

The Bank declined an extension of the letter of credit in late 2010. In response, on November 30, 2010, the City Attorney wrote a letter to the Bank urging the Bank to reconsider its decision, extend the letter of credit and otherwise refrain from taking any steps that could have adverse financial impact on the Foundation, to allow sufficient time for the parties to arrive at a sensible restructuring of the financing. The City Attorney sent a similar letter to the Bond Insurer. The parties entered into discussions coordinated by this office in an effort to restructure the 2005 Bonds.

The outstanding 2005 Bonds have been tendered to the Bank. If the settlement is not approved, the Foundation will be obligated to repay the 2005 Bonds to the Bank over a five-year rapid amortization period, rather than the remaining 23 year amortization period, at significantly higher interest rates.

When the letter of credit expired, the City, the Foundation, the Bank, MBIA, National Public Finance Guarantee ("National"), and the Bank of New York Mellon (Trustee for the 2005 bonds) executed a Forbearance Agreement for a one-month period. The Forbearance Agreement allows time for a financial solution to be arranged between all of the interested parties. It is expected that the Forbearance Agreement will be extended to allow a work-out solution to be implemented for the 2005 Bonds.

On January 6, 2011, the parties entered into a non-binding Term Sheet, which forms the basis for the proposed settlement. A copy of that Term Sheet is attached. By its terms, the offer the Bank makes to restructure the 2005 Bonds expires on February 11, 2011.

Current Plan of Finance:

The Resolution authorizes the execution of a Settlement Agreement among all the parties, and includes a restructuring of the 2005 Bonds in accordance with the signed Term Sheet, a Settlement Agreement that includes mutual releases by all the parties, a form of Assurance Agreement between the City and the Bank, and undertakings for amendments to the Museum Project Facilitation Agreement between the Commission and the Foundation.

If the Resolution is adopted by the Board and approved by the Mayor, and if the settlement is approved by the Commission and the board of the Foundation, the Foundation's 2005 Bonds (which, as noted are currently owned by the Bank) will be refinanced and converted into a 30-year fixed-rate tax-exempt loan (the "Loan") from the Bank, at an interest rate of 4.60%. The Loan is structured to give the Foundation breathing room and defers the full amortization of principal for 2 years from the closing date. Revenues and unrestricted assets of the Foundation, along with a debt service reserve fund will be pledged as security for 2005 Bonds, the principal amount of loan will be reduced to \$98.4 million from \$119.4 million. As of November 30, 2010, the Foundation has approximately \$70.0 million in assets. As part of the Settlement Agreement, the Swap will be terminated without cost to the Foundation and the associated posted collateral will be returned to the Foundation. In effect, these changes to the current debt contemplated by the settlement are worth at least approximately \$34.0 million to the Foundation (i.e., reduction in principal on the 2005 Bonds of \$21.0 million, and a return of the Swap collateral (assumed at \$13 million).

In addition, the Foundation has agreed to embark on a capital fundraising campaign with the objective of raising at least \$20 million over three years. The capital fundraising target, when combined with revenues, unrestricted assets, and interest earnings of the Foundation, is estimated to provide sufficient funds to make scheduled principal and interest payments on the Loan. Should available funds become insufficient to make a scheduled payment, the Bank will draw on the debt service reserve for such purpose, and the Foundation will have an obligation to replenish the reserve.

The Settlement Agreement provides for the termination of the existing insurance policy by the Bond Insurer, through a Policy Termination and Release Agreement.

The Settlement Agreement also includes the form of Assurance Agreement between the City and the Bank, under which the City agrees that, upon a failure by the Foundation to pay the principal of or interest on the new credit facility as and when due, failure of the Foundation to replenish the debt service reserve if the Bank needs to draw on it, or the Controller's determination that the Foundation's annual budget is not sufficient to pay the debt service on the new credit facility, the Controller has the ministerial obligation to request a budgetary appropriation or supplemental appropriation from the Board of Supervisors to satisfy the Foundation's obligation to make payments of the principal of and interest on the loan facility as and when due. The Board of Supervisors and Mayor retain the sole discretion to approve or disapprove any such appropriation or supplemental appropriation.

But under the Assurance Agreement, if the Foundation defaults on its Loan, and the Board of Supervisors does not appropriate funds in accordance with the Assurance Agreement, then the Bank will have the right to cause the Borrower to raise ticket prices, fees or donations for general admission for the public to view the display of the art at the Museum to amounts not exceeding the average of the fee, price or donation with respect to the general admission of the top three more expensive non-profit museums in California accredited by the American Association of Museums. Also, under such circumstances, the Foundation and the City would be required to obtain JPMorgan's consent to any wholesale relocation of the art work from the Museum. Finally, under the Assurance Agreement, the City agrees that for the entire period that the new credit facility is outstanding, the City will not support or encourage any foundation or other entity that would compete with the Foundation as the functions it performs for the Museum.

Additional Information Regarding the Settlement:

In addition to the Foundation's pledge to embark on a capital fundraising campaign, the Foundation will, as part of the proposed amendments to the Museum Facilitation Agreement outlined in the Settlement Agreement, be required to engage at its cost a management consultant with expertise in museum operations to review the finances and operations of the Foundation, allow for the appointment of City officials with financial expertise to serve as non-voting members on the investment committee and the capital committee of the Foundation, and obtain approval of the Controller of the Foundation's annual budget or any significant changes to the budget.

The Settlement Agreement includes mutual releases by all the parties, and usual language in a settlement agreement of this type regarding no admission of liability by any party.

Conclusion:

The City has a vital stake in protecting its interest in the Asian Art Museum. The City has contributed \$57.4 million toward the construction of the Museum, and each year contributes towards the museum's operations. While not readily calculable, it is likely that the cost to the City of accessing the capital markets would be adversely affected if the Foundation were permitted to proceed with liquidation upon a default under the 2005 Bonds. Also, the City would likely face significant increases in its required contribution of General Fund monies to operate the Museum, and private fundraising efforts would likely be seriously hampered. Finally, the proposed settlement avoids the significant legal costs and turmoil that would result if the matter were allowed to proceed to liquidation and public access to and enjoyment of the Museum could be interfered with for an interim period until financial matters and legal positions were clarified.

The Office of Public Finance believes that the rate on the loan is very competitive for the Museum given its current rating. Moreover, the fixed rate (which incidentally reflects still prevailing historic lows) removes the interest rate risk and renewal of credit facility risk associated with the current variable rate structure. Finally, the cancellation of the Swap at no cost, with a return of any collateral posted, is a very significant concession by the Bank.

We have worked closely with the City Attorney's Office in negotiating this proposed settlement, and the City Attorney recommends approval as well.

Your consideration of this request is greatly appreciated. Please contact Ben Rosenfield at (415) 554-7500 or Nadia Sesay at (415) 554-5956 if you have any questions.

cc: Angela Calvillo, Clerk of the Board of Supervisors
Ben Rosenfield, Controller
Starr Terrell, Mayor's Office
Harvey Rose, Budget Analyst
Greg Wagner, Mayor's Budget Office
Jesse Smith, Chief Assistant City Attorney
Mark Blake, Deputy City Attorney
Jay Xu, Director of the Asian Art Museum
Mark McLoughlin, Chief Operating Officer & CFO of the Museum

CONFIDENTIAL: FOR SETTLEMENT PURPOSES ONLY
SUBJECT TO CALIFORNIA EVIDENCE CODE SECTION 1152

SETTLEMENT AGREEMENT

AMONG

CITY AND COUNTY OF SAN FRANCISCO,

ASIAN ART MUSEUM FOUNDATION OF SAN FRANCISCO,

JPMORGAN CHASE BANK, NATIONAL ASSOCIATION,

MBIA INSURANCE CORPORATION,

NATIONAL PUBLIC FINANCE GUARANTEE CORPORATION

AND

THE BANK OF NEW YORK MELLON TRUST COMPANY, N.A.

DATED AS OF JANUARY 5, 2011

Complete copy of the document
located in File No. 110027

JANUARY 5, 2011



ASIAN ART MUSEUM FOUNDATION OF SAN FRANCISCO AND CITY AND COUNTY OF SAN FRANCISCO

Proposal for Asian Art Museum Foundation of San Francisco/the City and County of San Francisco

California Infrastructure and Economic Development Bank Variable Rate Revenue Bonds Series 2005 Bank Bonds

STRICTLY PRIVATE AND CONFIDENTIAL

J.P.Morgan

Complete copy of document
located in File No. 110027