



Memorandum

**TO: Rules and Open Government
Committee**

FROM: Kay Winer

**SUBJECT: History San José Request
For Additional Funding**

DATE: August 20, 2007

Approved

Date

8/20/07

RECOMMENDATION

Accept this report on History San José's requests for additional funding, including:

- Status of the audit conducted by Macias Consulting to address the organization's request for an increase in permanent funding per Manager's Budget Addendum #4;
- Council's response to past request for additional funding; and
- Response to current request for emergency funding by advancing quarterly payments for the next two quarters.

BACKGROUND

A twenty-year operating and maintenance agreement was executed with History San José (HSJ) in 1998. The annual subsidy payment schedule was designed in accordance with HSJ's preference that its 20 year subsidy totaling over \$8 million, be "front loaded" with a diminishing subsidy each year. During the negotiations, HSJ stated that providing more money "up front" would provide the organization with the resources to quickly establish itself as a non-profit and to provide the financial leverage that would generate outside contributed and earned income. Its official proposal was to "front" all of the money in the first ten years of the Agreement. HSJ envisioned that over time, it would no longer require financial support from the City. The City would, however, continue to provide landscaping and grounds maintenance during the term of the Agreement.

In addition to the annual operating subsidy, the City provided more than \$500,000 to HSJ during the early years of the Agreement for capital projects, replacement of the phone system, a new HVAC system at the Pacific Hotel, and refurbishment of the light tower. Much of the collections have been moved to the Central Service Yard and the City funded costs for shelving and continues to provide security and utility cost support. The annual value of these services to HSJ is over \$108,000. The remaining collections housed at the Stockton Warehouse are scheduled to be moved to the Central Service Yard, which will place all of the collections in a proper environment. RDA has also provided substantial support for capital improvements at the Fallon-Peralta complex.

The funding arrangement with HSJ is uniquely different from any of the other City-owned museums. In all cases, the annual operating subsidy has been established at a fixed amount for the duration of the agreement. This includes the Art Museum, Children's Discovery Museum, and the Mexican Heritage Plaza. With the exception of the Art Museum, which receives custodial support from the City, all of the others are responsible for providing routine maintenance and the City, through General Services, maintains responsibility for major capital needs.

ANALYSIS

Status of the Audit by Macias Consulting (MBA#4)

On May 1, 2007, HSJ submitted a letter to Les White, Interim City Manager, requesting that the operating subsidy be maintained at the FY 06-07 rate of \$687,323 instead of being reduced to \$574,823 per the Agreement and that the City work with HSJ to increase the level of annual funding to meet the basic annual operating cost of \$1,865,000. HSJ stated further that it understood that consideration of this request would entail an audit and submission of a business plan that would require City review and approval.

Manager's Budget Addendum #4 (MBA#4) was submitted to the Council on May 8, (copy attached). The MBA recommended that the operating subsidy be granted in accordance with the Agreement in the amount of \$574,823 pending completion of a full financial analysis. It recommended that the City Auditor complete the full financial analysis and submit findings and recommendations to the Council. This effort had typically required a period of three months to complete. The practice of completing an audit prior to considering any request for funding over and above the operating subsidy had been established with the San Jose Repertory Theatre, American Musical Theatre and Mexican Heritage Corporation.

Council authorized proceeding with the audit and approved funding in the amount of \$574,823 pending any changes that might occur as a result of the audit findings. The Auditor's office indicated that due to its workload, the report could not be completed within a three month timeframe and might take up to six months to complete. Consequently, the City entered into an agreement with Macias Consulting to complete the audit. The scope of work includes:

- Assessment of HSJ's overall financial viability;
- HSJ's compliance with the 1998 operations and maintenance agreement;
- Determination of the cost to operate an organization of similar nature and size, including determining at what funding level that City should support; and
- Determine appropriate performance/outcome expectations.

Staff has just recently received a preliminary draft from Macias Consulting and is in the process of reviewing it and will provide comments to the consulting firm by the end of this week. The comments will fall in the areas where clarification or corrections are needed. When a revised draft is sent, City staff will meet with HSJ to provide an opportunity for further clarification and/or corrections. Staff's goal is to submit recommendations to the Council by the end of September.

Past Request from HSJ for Additional Funding

The Mayor's June budget message for FY 2005-06 directed that HSJ's operating subsidy be reduced by \$50,000 rather than the \$75,000 in the funding schedule of the Agreement. This would be one-time only. An amendment to HSJ's Agreement was required to effect the change. In the process of meeting with HSJ on the amendment, the organization identified other items for discussion, including operation of the two parking lots during specific special events to provide greater flexibility, as well as additional revenues. HSJ also requested reopening the Agreement to increase the annual operating subsidy. There was no specific amount requested by HSJ at the time. Staff did not agree to re-open the Agreement, as there was no specific justification provided and this would be precedent setting action, potentially leading to requests for additional funding from many or all of the groups that have long-term operating agreements with the City.

The Council approved the Amendment to the Agreement reducing the subsidy by \$50,000 rather than \$75,000 for one-time only and approved the changes to operating the parking lots. The staff report approved by Council also confirmed that the Agreement would not be re-opened to negotiate the operating subsidy.

Emergency Funding Request

The City Manager was made aware by Councilmember Madison Nguyen of an emergency funding request from HSJ on August 10, which was followed up by a message from Margie Matthews, Chair of the HSJ Board. The request is that the second quarter payment in October 2007 be advanced to August 29 and that the 3rd quarter payment in December be advanced to October 2007. HSJ stated that it cannot meet its expenses and without an advance, will be unable to meet its next payroll on August 29. (Each quarterly payment is \$143,705.75.)

In its correspondence to the City, HSJ has stated that it has used up its reserve and spent the endowment. Without immediate City funding, HSJ stated that school programs and other functions will be curtailed and/or eliminated.

Alternatives

In order to assure continued provision of services pending Council's decision on the recommendations from the Macias audit, two alternatives to HSJ's request should be considered:

1. Consider an advance payment for one quarter only at the September 11, 2007 Council meeting:

The soonest that the Council can take action on a funding request is September 11 due to "sunshine" requirements. HSJ is required to submit a detailed spending plan to staff by Friday, August 24 so that it can be included in a report to the City Council for distribution by August 31. If the spending plan is not submitted on time or does not provide sufficient detail or information, consideration by the City Council of this request will be deferred to a later date. Approval of an advance payment will also require an amendment of the existing Agreement.

Staff is not recommending consideration of a second advance at this time. We expect to bring forward the audit recommendations to Council by the end of September, which should bring closure to the question of the funding level to HSJ by the City.

2. City assumes responsibility for managing special events and core programs beginning September 1, 2007.

Under this alternative, HSJ will provide the City with its events and programming schedule, effective September 1, 2007. PRNS staff will assume responsibility to assure that events that have already been booked will be held; the City would offer temporary positions to HSJ employees who conduct tours or school programs to assure continuation of these services. This alternative requires the cooperation of HSJ and an amendment to their current Agreement. Funding to support this alternative would be the current year's operating subsidy to HSJ.

CONCLUSION

Completion of the audit by Macias Consulting is on schedule and staff will bring forward its recommendations to the Council by the end of September. The audit report will be shared with HSJ prior to finalization and staff's recommendations will also be discussed with HSJ before the item is placed on the Council agenda.

Two alternatives have been presented to assure continued services at History Park prior to Council consideration of staff's recommendations on the audit in late September.


Kay Winer
Chief Deputy City Manager

Attachment: MBA#4



Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Kay Winer

SUBJECT: Request from History San José
for Additional Funding

DATE: May 8, 2007

Approved

/s/

Date 05/09/07

RECOMMENDATION

1. Provide an annual operating subsidy of \$574,823 for FY 2007-08 to History San José (HSJ), consistent with the subsidy schedule contained in the Agreement with the City while the City Auditor completes a full financial analysis of additional funding requests. (This is consistent with the process that has been used for requests from San José Repertory Theatre, American Musical Theatre and Mexican Heritage Corporation.)
2. Request the City Auditor to complete the financial analysis in order to respond to the following requests from HSJ:
 - Stabilize the operating subsidy for FY 2007-08 at the FY2006-07 level of \$687,323.
 - Increase annual funding to cover a larger percentage of the \$1,865,000 determined by HSJ as the amount required to maintain basic operations of HSJ.
3. Direct Parks, Recreation and Neighborhood Services to continue working with HSJ to maximize meeting HSJ's highest priorities in landscaping maintenance with existing resources, rather than restore a specific full-time gardener who had worked at History Park for a number of years.

(The May 1, 2007 letter that makes the requests for additional funding and restoration of a gardener is attached.)

BACKGROUND

In April 1998, an Agreement was approved for a twenty-year operating agreement between the City and History San José. This was the culmination of months of negotiations to turn over responsibility for the facilities and collections from the City to the non-profit organization. Negotiations culminated with an Agreement in which a key provision was a mutually-agreed upon schedule of declining operations and maintenance subsidy by the City to HSJ. (See attached schedule.) This approach to providing the operating subsidy was in response to HSJ's request that more support be provided "up front", as the organization was confident that its fund raising capacity would be strengthened over time, thus lessening the amount of City general fund support.

The Mayor's June budget message for FY 2005-06 provided direction that HSJ's operating subsidy be reduced by \$50,000 rather than the \$75,000 called for in the contract. There was also direction to allow HSJ to operate the two parking lots serving the museum during special events. This would provide HSJ with flexibility that it desired, as well as a small amount of additional revenues. During a series of meetings that beginning in September 2005, HSJ also requested to re-open discussions with regard to the subsidy. Staff did not recommend reopening the Agreement to renegotiate new terms for the operating subsidy. It was staff's opinion that by so doing, many, if not all of the other non-profits with an operating subsidy would submit a similar request. On June 13, 2006, the Council approved staff's recommendations to only amend the Operation Agreement to modify the payment for one year and to provide HSJ the opportunity to manage the two parking lots under certain special event conditions.

ANALYSIS

Request to Increase Operating Subsidy

HSJ has stated that it will conclude this fiscal year with an approximate \$250,000 deficit. Further, its letter of May 1, 2007 states that by not reducing the subsidy for next year and maintaining it at the current fiscal year level of \$687,323 will sustain the organization temporarily, but will not be sufficient to carry HSJ to June 30, 2008. According to HSJ, the organization's budget for next year will be \$2.3 million. Of that amount, \$1,865,000 is required to maintain basic operations of HSJ on an annual basis. At this time, HSJ has not determined how much of that amount will be requested of the City on a yearly basis, although HSJ has stated that it is confident that it will be able to raise funds for programming, which is approximately \$435,000 (difference between \$2.3 million and \$1,865,000).

Each of the major arts and culture organizations that have submitted requests to the City for funding above the subsidy contained in their contract have undergone a complete review by the City Auditor and submission of a business or reorganization plan prior to Council action on their respective requests. The organizations include San José Repertory Theatre, the American Musical Theatre and Mexican Heritage Corporation. For consistency, it is recommended that the City Auditor be directed to complete a full financial analysis of the organization and to submit findings and recommendations to the Council. This effort has typically taken approximately three months to complete. HSJ expects that an audit is part of the process of reviewing their request. It is recommended that, pending completion of the Auditor's analysis, the established annual subsidy schedule of \$574,823 be retained for FY 2007-08.

Request to Reinstate Gardener to History Park

History Park, along with all of the other parks facilities in the City, was subject to reductions over the past five years. One of the reductions was the loss of a full-time, dedicated gardener who had been assigned to History Park for a number of years. No further reductions in parks maintenance are proposed for FY 2007-08. Parks and Recreation prepared a History Park Maintenance Plan that describes the services and frequency of services to the facility. These include general routine maintenance and repair items; landscaping such as irrigation, weed abatement, edging, pruning, etc.

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Although Parks and Recreation staff has met previously with HSJ and shared the maintenance schedule, it is recommended that additional discussions take place to determine if there are additional ways in which the budgeted resources can be distributed differently to address HSJ's highest priorities.

CONCLUSION

Pending completion of a financial analysis by the City Auditor, it is recommended that the annual operating subsidy for HSJ be consistent with the adopted payment schedule of \$574,823. It is further recommended that Parks, Recreation and Neighborhood Services staff meet further with HSJ to determine how the budgeted resources for History Park can be distributed differently in order to meet the museum's highest priorities.

COORDINATION

The information in the MBA was shared with History San José and the City Auditor.

/s/
Kay Winer
Chief Deputy City Manager

Attachment

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May 1, 2007

Les White, City Manager
San José City Hall
200 East Santa Clara Street
San José, CA 95113

Dear Les,

Thank you for taking the time last week to meet with History San José (HSJ) to discuss the financial difficulties the Museum is experiencing as a direct result of declining City funding, and to hear about the negative effects occurring at History Park since full time City gardener, Carla Morrison, was reassigned last summer.

This letter is to confirm our conversation that History San José respectfully requests:

- 1) That the City stabilize the current City Operations Payment at the FY07 rate of \$687,323 for the coming fiscal year. Our payment is currently scheduled to drop to ~~\$598,873~~ — a difference of ~~\$148,450~~. ^{574,823}
_{112,450}
- 2) That the City restore Carla Morrison as the full time City gardener assigned to the 14-acre History Park beginning FY08.

Concerning the City Operations Payment— stabilizing at the FY07 Operations Payment rate will help sustain HSJ temporarily, however, it will not be a sufficient amount to carry HSJ to the end of FY08. The estimated budget for that year, according to the HSJ/City Contract, is 2.3 million. Of that amount, approximately \$1,865,000 (based on FY06 Audit) is needed to maintain basic operations of the Museum. HSJ is anxious to begin work with the

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City to determine a level of funding that is fair and reasonable to both the City and HSJ. It is understood that part of that process will include a City Audit and the development of a City approved business plan, which we welcome.

Concerning Carla Morrison—as you know, History Park serves as a primary meeting place for more than 105,000 visitors each year who attend diverse community events. Included in that number are 26,000 school children and teachers and a cadre of neighborhood joggers, power walkers, and strollers. We want to keep History Park looking its best for the community and for the rental events that gross over \$100,000 annually. We depend on this income to fund our annual operating budget. HSJ is specifically requesting Carla Morrison because of her immense and intimate knowledge of History Park as a result of caring for the Park for over 10 years.

Again, thank you for your time and consideration of this request. If you need any additional information, please do not hesitate to call Alida at 408.918.1041.

Sincerely,

Alida J. Bray
President & CEO

Margie Matthews
Board of Directors, Chair

*cc: Mayor and City Council Members,
Kay Winer, Chief Deputy City Manager
Mignon Gibson, Administrative Officer*

ATTACHMENT: HISTORY SAN JOSÉ SUBSIDY SCHEDULE

Year	FY	History San José Annual Subsidy	Supplemental Staff Payment*	History San José Total Annual Subsidy
1	1998-99	964,000	199,823	1,163,823
2	1999-00	750,000	199,823	949,823
3	2000-01	750,000	199,823	949,823
4	2001-02	750,000	199,823	949,823
5	2002-03	750,000	199,823	949,823
6	2003-04	712,500	199,823	912,323
7	2004-05	660,000	199,823	859,823
8	2005-06**	610,000	199,823	809,823
9	2006-07	487,500	199,823	687,323
10	2007-08	375,000	199,823	574,823
11	2008-09	135,262	199,823	335,085
12	2009-10	135,262	199,823	335,085
13	2010-11	135,262	199,823	335,085
14	2011-12	135,262	199,823	335,085
15	2012-13	135,262	199,823	335,085
16	2013-14	135,262	199,823	335,085
17	2014-15	135,262	199,823	335,085
18	2015-16	135,262	199,823	335,085
19	2016-17	135,262	199,823	335,085
20	2017-18	61,710	199,823	261,533
Total	98/99-17/18	\$ 8,088,068	\$ 3,996,460	\$ 12,084,528

* Details the supplemental payment that was to remain constant during the entire term of the agreement for four City staff persons that ceased working at the Museum.

**Amount adjusted to detail Subsidy reduction of \$50,000 rather than \$75,000 per direction of "Mayor's June Budget Message for Fiscal Year 2005-2006", dated June 8, 2005.