



COUNCIL AGENDA ITEM

FRESNO CITY COUNCIL FINANCE AND AUDIT COMMITTEE

October 23, 2013

TO: Fresno City Council Members,
FROM: Lee Brand, Chair
Clint Olivier, Vice Chair
Blong Xiong, Council President and Committee Member

Agenda Item

Recommend that the Fresno City Council approve the findings and recommendations of the Finance and Audit Committee regarding the future management of the Convention Center.

Background

On June 5, 2013 Chair Brand presented his preliminary findings to the Council on the Convention Center operations and finances. The Council voted to hold Convention Center budgeted operating funds in contingency pending the outcome of a further investigation, with the provision that ongoing expenses would be paid. The Finance and Audit Committee met three times to conduct a thorough review and evaluation of the Convention Center operations and finances. At their final meeting on October 8th they voted unanimously to approve the findings and recommendations contained herein. Please see attached **Exhibits A-L2** attached for information related to the findings and recommendations.

Findings:

1. There are no opportunities at this point in time to refinance any of the existing Convention Center debt issuances that would result in any significant debt service costs.
2. City decisions to continue funding major capital improvements at the Convention Center Complex after the final decision to build Savemart Arena are questionable. Although there was certainly the need to upgrade complexes, some consideration should have been made to consider possible sale of one or more of the venues. At this point in time, bond encumbrances far exceed market value of venues making it economically unfeasible to sell any of the venues for any time in the foreseeable future.

3. The Net General Fund subsidy for the Convention Center has averaged approximately \$8.0 million per year for the past 6 years and would be even higher if the City was still funding the Convention Visitors Bureau (CVB).
4. For the past three years, SMG has carried forward Accounts Payable in the \$1.5 to \$2.0 million range including \$600,000 to \$750,000 owed to the City of Fresno. As of 6-30-13, SMG owed the City approximately \$730,000. This amount included over \$200,000 owed for water and sewer and over \$450,000 owed for APES fees (\$1.00 ticket add on for capital improvements).
5. In City staff reports in 2004 and 2008 regarding support for SMG management of the Convention Center, representations were made that the Net General Fund Subsidy would be reduced \$6 million. In fact, the Net General Fund Subsidy actually increased at least \$2 million under SMG's management.
6. From 2004 through 2008 SMG accrued approximately \$2 million in employee benefit costs and failed to follow contractual procedures/remedies to request mid term budget amendments from the City. The contract extension approved in 2009 was settled for \$1 million. The City agreed to repay at \$100,000 per year. The City currently owes SMG \$500,000.
7. Of the four venues at the Convention Center, Selland Arena and the Saroyan Theatre generate the biggest losses. In 2012, Selland Arena lost about \$700,000 and Saroyan Theatre lost about \$300,000.
8. The total approximate amount of deferred capital improvements at the Convention Center complex is \$7.9 million. There is currently no capital reserve plan to address this issue. Failure to address needed capital improvements will exacerbate the financial losses for the Convention Center.
9. There is not a reliable methodology to accurately track Room Tax (T.O.T.) and measure the economic impact in the community resulting from Convention Center events.
10. SMG does provide detailed monthly reports including financial reports to the City Manager every month. These reports, however, have not been released to Council members.
11. In 6 of the past 9 years, SMG has failed to meet their budget benchmarks including the past 2 years. SMG's failure to meet their budget benchmark enables the City the opportunity to cancel the management contract pursuant to Section 10.2 of the 2009 contract between SMG and the City.

During the October 8th hearing, testimony was provided by City Manager Bruce Rudd and SMG General Manager Bill Overfelt helped explain why SMG failed to meet their budget benchmark including capital improvement projects that put certain venues (i.e. Selland Arena) off line for 90 days plus and impacted potential revenue. Mr. Overfelt also testified that he had communicated directly to the City Manager during those periods where their budget operating costs were going to exceed their budget benchmark but also acknowledged that he did not attempt to bring the issue to the Council.

12. The management fee provision in the current contract with SMG increases every year via a CPI index increase irrespective of the actual performance of SMG. In recent years, with a lower number of events, the management fees are higher than in previous years when there were more event days.
13. There is a need to improve the relationship between SMG and the Convention Visitors Bureau (CVB). The City discontinued funding CVB 4 years ago. CVB funding is assessed directly from member hotel/motel owners and does not have the same focus as it did when the City provided \$600,000 plus per year in funding.
14. The City is not realizing the full potential of outdoor advertising on Convention Center buildings and other City owned properties. There are revenue opportunities for selling outdoor advertising space to Convention Center vendors and sponsors at strategic locations at Convention Center buildings.
15. The question of a potential conflict of interest with SMG managing both the Save Mart Center and the Convention Center has not been satisfactorily answered. SMG manages Convention Centers and other similar venues worldwide and Fresno is the only City in their management portfolio where they manage for both two competing, separate entities in the same city.

Council Options for Management of Convention Center:

1. The Council has three options:

One: Do nothing and continue on with SMG managing the Convention Center with no contractual changes;

Two: Re-negotiate the contract with SMG including subcontracts to make substantive changes in the contract that will provide the City more control of Convention Center operations and a significant reduction in the annual Net General Fund subsidy. Under this option, SMG and subcontractors would have to voluntarily agree to any negotiated contract changes; or

Three: Cancel the contract with SMG and request the City Manager/City Attorney prepare a Request for Proposal (RFP) for management of the Convention Center complex. The City would have the option to negotiate directly with subcontractors.

2. To implement option 3 will require the City Attorney send a letter of intent to cancel the management contract between SMG and the City.

Financial consequences of each option:

One: If nothing is done with the existing contract with SMG, the City General Fund will continue to subsidize operations in the \$7.0 to \$8.0 million per year range. There is no plan to address the estimated \$7.9 million in capital improvements needed for all of the Convention Center venues. There is also

no plan to remedy the \$1.5 to \$2.0 accrued accounts payable carried by SMG. Even with improved market conditions, deteriorating venues at the Convention Center will be unable to compete in the market place;

Two: The financial benefits of selecting option two are subject to the City and SMG agreeing upon a contract amendment. SMG officials have met with the City Manager and have discussed financial concessions and significant contract changes suggested by Chair Brand at the September 9th Finance and Audit Committee meeting. These changes will focus on profitability, transparency, and increased involvement and oversight by the City. The attached spreadsheet details financial concessions discussed at Finance and Audit Committee meetings (**Exhibit K**). There are ongoing negotiations between SMG and the City to develop an agreed upon Term Sheet of financial concessions and substantive contract changes.

Three: The exact financial benefit of cancelling the SMG contract and initiating an RFP will not be known until the City can develop the RFP format and examine the proposals submitted. It is estimated that a new RFP implementing recommendations outlined in the September 9th meeting and additional items discussed informally (i.e. outdoor advertising ordinance amendment) could yield Net General Fund Subsidy savings between \$500,000 to \$1,000,000 per year.

Final Recommendations:

Based on a thorough evaluation of Convention Center operations and finances the Committee recommended that the Council accept the findings offered in this document and approve the recommendations below:

1. Request the City Attorney/City Manager send a notice of cancellation to SMG advising them of our intent to cancel their management contract for the Convention Center and prepare an RFP for management of the Convention Center Complex. SMG will be encouraged to submit a proposal in a new RFP;

Or

Request City Manager/City Attorney to complete a formal contract amendment with SMG and affected Subcontractors consistent with the attached Term Sheet and present contract amendment for Council approval on the October 31st meeting.

2. Recommend that City hire an industry consultant with experience in evaluating Convention Center management operations to conduct an independent review of the Convention Center operations and finances and assist in the development of the RFP (only if RFP option is selected);
3. Draft an amendment to City sign ordinance to allow for outdoor banners and electronic billboard signs on City owned properties;

4. Working with industry consultant, examine potential uses and revenue opportunities of Chukchansi ball park during the off season when the City has the right to use the facility;
5. Request City Manager/City Attorney develop Convention Center commission agreement to incentivize CVB or any outside agency with an interest in promoting events at the Convention Center to expand existing marketing efforts of SMG;
6. All realized savings emanating from the implementation of either a substantive contract amendment with SMG or through an RFP shall be directed to a Capital Improvement Reserve Fund for Convention Center improvements until such time that substantial progress has been made on Convention Center capital improvements. All funding shall be subject to a majority vote of the Council;
7. The City and SMG or a future Convention Center operator (via an RFP) reconcile all current accounts payable through negotiated re-payment or write off to zero balance prior to the start of operations on or before July 1, 2014. All future budgets shall reflect true costs and accurately state the Net General Fund Subsidy; and
8. City to develop a more accurate tracking methodology for room tax revenues and measuring economic impact on the community through a joint effort with the CVB and Convention Center operator.
9. SMG or a future management company for the Convention Center should provide financial reports consistent with City financial formats and in full compliance with Government Accounting Standards Board (GASB) accounting standards;
10. SMG or a future management company for the Convention Center should provide complete financial reports within 30 days following the end of the previous month. (i.e. June 30th financial statements must be provided no later than July 30th of the following month);
11. Mandatory annual report to Council during budget hearings of Fiscal year approved budget vs. actual budget data. **See Exhibits L-1 & L-2.**

c: Mayor
City Manager
City Attorney
City Clerk

EXHIBIT 'A'

Recommendations for Contract Amendment between City and SMG

1. Mandatory annual independent audit of all operations completed by a reputable CPA firm.
2. The City of Fresno to have right to direct SMG to remove the facility's General Manager with 90 days written notice and an explanation for the reason for removal. The City will continue to have the right to approve of any replacement.
3. City Manager to have approval rights for all existing and future SMG subcontracts with a total value between \$10,000 to \$50,000. The Council shall have approval rights for all SMG subcontracts with a total value exceeding \$50,000.
4. Contractor shall not exceed the approved annual budget net operating deficit (excluding debt service and capital expenditures) without the approval of the City and under circumstances within Contractor's control;
5. SMG to reconcile all current accounts payable and receivable through payment, re-negotiation, or write off to zero balance. SMG to make reasonable efforts to keep accounts payable at 90 days or less. SMG to immediately notify City if any accounts payable exceeds 90 days and will provide a plan to resolve issue;
6. Convention Center Manager to provide detailed monthly reports to Council, Mayor, City Manager and City Attorney;
7. Mandatory annual report to Council during budget hearing of Fiscal year approved budget vs. actual budget data (See Exhibit L);
8. Implementation of new risk sharing business plan for Convention Center operations;
9. Establish 7-person advisory oversight board consisting of one CVB board member or director; SMG General Manager; one Fresno

Chamber of Commerce member, one Hotel/Motel industry member, PBIB director or board member; one Council member and the city Manager of Fresno. City Manager to chair board;

10.SMG should provide financial reports consistent with City financial formats and in compliance with Government Accounting Standards Board (GASB); and

11.SMG should provide complete financial reports within 30 days following the end of the previous month.