



Office of the City Auditor

**Report to the City Council
City of San José**

**TEAM SAN JOSE
PERFORMANCE 2017-18**

**Report 18-08
November 2018**

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Office of the City Auditor
Sharon W. Erickson, City Auditor

November 16, 2018

Honorable Mayor and Members
Of the City Council
200 East Santa Clara Street
San José, CA 95113

Team San Jose Performance FY 2017-18

Since 2004, the San José McEnery Convention Center and several other City-owned facilities have been operated on the City's behalf by Team San Jose, Inc. The Management Agreement between the City and Team San Jose requires an annual audit by the City Auditor to determine whether, and how well, Team San Jose achieved the agreed-upon performance targets that are the basis for the City's incentive payment.

In October 2017, the City Council authorized the City Manager to negotiate and execute an amendment to the agreement, including modifications to the incentive fee measures that would be applied retroactively for FY 2017-18. That agreement was finalized on November 2, 2018 but a target for theater occupancy has not yet been established.

Team San Jose Exceeded Its Weighted Incentive Score Target for FY 2017-18. In FY 2017-18, Team San Jose booked over 170,000 future hotel room nights and generated \$115 million in estimated economic impact from events held at the Convention and Cultural Facilities. Overall, even without theater occupancy, Team San Jose exceeded its weighted incentive fee score. Team San Jose thus qualifies for the incentive fee of \$200,000.

We will present this report at the November 26, 2018 meeting of the City Council's Community and Economic Development Committee. We would like to thank Team San Jose and the City Manager's Office for their time and cooperation during the audit process. We recommend that the Administration work with Team San Jose to establish and formalize the target for theater occupancy for FY 2018-19. A response from the Administration is attached on the yellow pages at the end of this report.

Respectfully submitted,

Sharon W. Erickson
City Auditor

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Introduction

The mission of the City Auditor's Office is to independently assess and report on City operations and services. The audit function is an essential element of San José's public accountability and our audit reports provide the City Council, City management, and the general public with independent and objective information regarding the economy, efficiency, and effectiveness of City operations and services.

In accordance with the City Auditor's fiscal year (FY) 2018-19 Audit Work Plan, we have completed an audit of Team San Jose, Inc.'s (TSJ) management of the City's Convention and Cultural Facilities. Our audit purpose was to determine whether Team San Jose met the incentive fee measures specified in the *First Amendment to the Agreement for the Management of the San José Convention Center and Cultural Facilities between the City of San José and Team San Jose* (Management Agreement) for FY 2017-18.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. We limited our work to those areas specified in the "Audit Objective, Scope, and Methodology" section of this audit report.

We thank Team San Jose and the City Manager's Office for their time, information, insight, and cooperation during the audit process.

Background

The San José Convention and Cultural Facilities (the Facilities) are City-owned and consist of:

- The San José McEnery Convention Center
- South Hall
- Parkside Hall
- The City National Civic (formerly known as Civic Auditorium)
- The Center for the Performing Arts
- The California Theatre
- The Montgomery Theater

The Convention Center, South Hall, and Parkside Hall generally host trade shows, conventions, corporate meetings, social events, and consumer shows.

The Cultural Facilities host performing arts, concerts, and events. These include, but are not limited to, performances by the Symphony Silicon Valley and Opera San José (at the California Theatre), the Children's Musical Theater of San José (at the Montgomery Theater), and Broadway San José (at the Center for the Performing Arts/California Theatre).

Exhibit I: Team San Jose Managed Facilities
San José McEnery Convention Center



California Theatre

City National Civic



Center for Performing Arts

Montgomery Theater



Source: Team San Jose, Inc.

Team San Jose Has Managed the Facilities Since 2004

Team San Jose, Inc., a 501(c)(6) non-profit corporation, was formed in 2003 in response to the City's request for proposal (RFP) for the management and operations of the Convention Center, which had previously been managed by City staff in the former Department of Convention, Arts, and Entertainment. Team San Jose has a 17-member board of directors that includes representatives from local hotels, arts, business, and labor. It also includes a City Council liaison and an ex-officio member from the City Manager's Office. The City's Management Agreement with Team San Jose requires the City Auditor's Office to conduct an annual audit of the performance measures in the agreement.

In June 2004, the City Council approved the first five-year Management agreement with TSJ. The Management Agreement directed this Office to conduct a performance audit of TSJ against established performance measures on an annual basis. The Management Agreement also created an annual management fee of \$150,000, with provisions that enabled the City to delete the management fee in the final two years of the agreement if TSJ did not meet its performance measure targets.

In January 2009, the City Council approved a new five-year Management Agreement with TSJ beginning July 1, 2009 and ending June 30, 2014. The new agreement added additional performance measures and incentive measures for use in determining whether TSJ would receive an incentive fee, and increased the maximum incentive fee to \$500,000. This agreement was subsequently amended in FY 2010-11 to change the maximum incentive fee to \$350,000.¹

In June 2014, the City and Team San Jose entered into a new Management Agreement for the period of July 1, 2014 through June 30, 2019, with two additional five-year options. With this Agreement Team San Jose gained the ability to modify its adopted budget, the theater performance measures changed, the management fee and incentive fee amounts changed, and Team San Jose took charge of standard capital improvements and repairs.

In 2016, the City contracted with Conventions, Sports, and Leisure International (CSL), an independent consulting firm, to examine the current performance and incentive fee measures, and develop enhanced metrics. Based on those recommendations, in October 2017, the City Council authorized the City Manager to negotiate and execute an amendment to the Management Agreement with Team San Jose to revise the performance measures and enhance reporting

¹ Under this agreement, the incentive fee that TSJ received was scaled based on its performance relative to the performance measure targets. Depending on whether TSJ exceeded the overall weighted incentive target and by how much, TSJ was eligible for increasing incentive fees that maxed out at \$500,000, or \$350,000 when the agreement was amended in FY 2010-11.

requirements. The amendment was finalized November 2, 2018, with changes retroactively effective for FY 2017-18.

In addition, the City and Team San Jose have separate agreements under which Team San Jose provides convention and visitors bureau (CVB) services on behalf of the City, staffs the Visitors Information Booth at the San José Airport (Airport) and provides destination marketing services for the Airport under a separate agreement.

The Performance-Based Agreement between the City and Team San Jose Establishes Performance/Incentive Measures

The 2014 Management Agreement provides that the City pays Team San Jose a fixed Management Fee of \$1 million per year “to provide, without limitation, for payment of a portion of the expenses incurred by TSJ for the management of the operations and maintenance of the City's Facilities, as determined by the TSJ Board of Directors.” If certain performance targets are met, the City also pays Team San Jose a \$200,000 incentive fee.²

Incentive fees, such as the incentive fee from City's Management Agreement with Team San Jose, have been common in government for several decades. The purpose is to ensure that contractors have the freedom to determine how to meet agreed-upon performance objectives, and are incentivized to exceed those targets. Under the Management Agreement, Team San Jose proposes targets, and then the City reviews and approves them. The Agreement requires the City to approve targets prior to the beginning of each fiscal year. The City also uses a consultant with expertise in the convention, entertainment, and visitor industries to evaluate Team San Jose's proposed targets.

The Amendment to the Management Agreement outlines five measures that track TSJ's financials, economic impact, theater occupancy, and customer survey results.³ For each measure, the weighted percent is calculated by taking the percent of the target achieved multiplied by the assigned percent. The sum of these measures the weighted incentive fee score. The incentive fee is granted for scores reaching 100 percent or more. Exhibit 2 compares the previous incentive fee measures to the revised measures.

² Under the current Amendment to the Management Agreement, the incentive fee is set at \$200,000 for the first five years of the agreement, and will increase \$50,000 after each of the five year extensions.

³ Because construction of the facilities managed by TSJ was financed through tax-exempt debt, the management agreement cannot include an incentive pay provision that is based on return on investment or net profit. Hence, the incentive fee measures used to determine TSJ's incentive pay differ slightly from the general performance measures.

Exhibit 2: Incentive Fee Measures and Their Weighting

| Previous Incentive Fee Measures | | Revised Incentive Fee Measures | |
|---------------------------------|-------------|---------------------------------|-------------|
| Gross Operating Revenue | 40% | Gross Operating Results | 40% |
| Economic Impact | 40% | Economic Impact | 40% |
| Hotel Room Nights (15%) | | Hotel Room Nights (20%) | |
| Estimated Economic Impact (15%) | | Estimated Economic Impact (20%) | |
| Attendance (10%) | | | |
| Theater | 10% | Theater | 10% |
| Performances (5%) | | Theater Occupancy (10%) | |
| Special Events (5%) | | | |
| Customer Satisfaction | 10% | Customer Satisfaction | 10% |
| Total | 100% | Total | 100% |

Source: Management Agreement and the Amendment to the Management Agreement between the City and Team San Jose

History of Team San Jose Performance Audits

As required by the City’s Management Agreement, the Office of the City Auditor has audited Team San Jose’s performance to the Management Agreement performance targets since 2005.⁴ The list below summarizes the results of those audits:

- The audit of Team San Jose’s performance targets for [FY 2004-05](#) found that TSJ met the target for one of four performance measures, did not meet the target for two performance measures, and had insufficient data to assess whether or not TSJ met the fourth performance measure. The report had 17 recommendations, which included recommendations that TSJ staff sign a form attesting awareness of the conflict of interest policy and report on its performance relative to performance targets as well as adherence to a schedule of planned maintenance. In that year TSJ received a \$150,000 management fee.
- The subsequent audits—from [FY 2005-06](#) to [FY 2008-09](#) confirmed that TSJ did not meet all of the performance measure requirements but received the \$150,000 management fee as outlined in the Management Agreement in each of those years. The FY 2005-06/2006-07⁵ report included a recommendation that TSJ perform a nation-wide search to find a chief executive officer with the experience to manage the Convention and Cultural Facilities in accordance with the Management Agreement, and the [FY 2007-08](#) report recommended that the City Council waive its right

⁴ Each of these audit reports can be viewed at: www.sanjoseca.gov/audits.

⁵ This office published one report that analyzed Team San Jose’s performance in both FY 2005-06 and FY 2006-07.

to delete the fixed payment of \$150,000 from the final two years of the Management Agreement.⁶

- In [FY 2009-10](#) and [FY 2010-11](#) we found that TSJ qualified for the incentive fee under the new management agreement. As a result, the City paid TSJ \$400,000 of a possible \$500,000 incentive fee for FY 2009-10, and the maximum \$350,000 in the remaining year. The FY 2009-10 audit included 13 recommendations, many of which were aimed at improving the fiscal health of the City's Convention and Cultural Facilities, and creating a reserve fund for future economic uncertainty. The FY 2010-11 audit included four recommendations, including recommendations to consolidate the City's operating agreements with TSJ to manage the Convention and Cultural Facilities as well as the CVB into one agreement.⁷
- In [FY 2011-12](#) we found that TSJ met six of eight performance measure targets and five of seven incentive fee targets. Because TSJ did not meet at least 90 percent for each individual incentive fee measure as required by the agreement, it did not qualify for the incentive fee. We should note that the City instead authorized an increase in the Convention Facilities appropriation as a reimbursement of expenses not to exceed \$350,000.
- Our [FY 2012-13](#), and [FY 2013-14](#) audits found that TSJ qualified for the incentive fee under the Management Agreement. As a result, the City paid TSJ the maximum incentive of fee of \$350,000 in both years.
- TSJ qualified for the incentive fee of \$200,000 in FY [2014-15](#), FY [2015-16](#), and FY [2016-17](#). The FY 2014-15 report included a recommendation that the City Manager's Office, Team San Jose, and San Jose Theater Preservation Inc. evaluate and clarify their roles in collecting, managing, and expending theater preservation fees.

All 37 of the recommendations that resulted from those audits have been implemented or closed.

Audit Objective, Scope, and Methodology

The objective of our audit was to determine whether Team San Jose met its performance and incentive fee measures for FY 2017-18. To do so we:

- Reviewed relevant documents including: the 2014 Management Agreement, the 2018 First Amendment to the Management Agreement,

⁶ This Office made this recommendation because the City Manager's Office determined that the performance measures established at the beginning of the agreement were not realistic given variability in the economy. Subsequent agreements set performance measures annually.

⁷ During FY 2009-10, TSJ overspent its budget, and the City Council issued a notice of default to TSJ. However, TSJ enacted significant cost cutting measures and earned more revenue in FY 2010-11, resulting in decreased net operating losses. The City also hired an industry advisor to compare the operations of San José's convention facilities to peers and craft observations and recommendations.

Council-adopted performance targets, TSJ's performance reports, the FY 2017-18 audited financial statement for the Facilities,⁸ the Convention Center debt service schedule, parking garage revenue and expense reports, Budget Office Source and Use reports for the Convention and Cultural Affairs Fund (Fund 536), the Transient Occupancy Tax (TOT) Fund (Fund 461), the Convention Center Facilities District Revenue Fund (Fund 791), TSJ's estimated economic impact based on event attendance, theater occupancy records, the agreed-upon procedures for hotel-room night bookings performed by *Petrinovich Pugh & Company, LLP* on TSJ's behalf, and TSJ's customer service surveys for the fiscal year.

- Interviewed management and staff from TSJ, as well as from the City Manager's Office of Economic Development and Budget Office about the performance measures and TSJ's accomplishments for the fiscal year.
- Tested the accuracy and completeness of TSJ's recording of the number of Theater Occupancy Days for theaters, estimated economic impact based on event attendance, customer service survey results, and hotel room nights booked during the year.
- Tested the accuracy of TSJ's computation of gross operating results using the audited financial statements for FY 2017-18 and the Amendment to the Management Agreement's methodologies.

⁸ The financial audit of the City's Convention and Cultural Facilities, by the independent accounting firm of Macias Gini, and O'Connell was completed in October 2018.

Finding I Team San Jose Exceeded Its Weighted Incentive Score Target for FY 2017-18

Summary

In FY 2017-18, TSJ booked over 170,000 hotel room nights, had an estimated economic impact of \$115 million, exceeded its target in gross operating results, reached 518 days of events at its cultural facilities, and received 100 percent satisfaction ratings on its customer service surveys. Overall, even without theater occupancy, Team San Jose exceeded its weighted incentive fee score of more than 100 percent. Team San Jose thus qualifies for the incentive fee of \$200,000.

Exhibit 3: Weighted Incentive Score

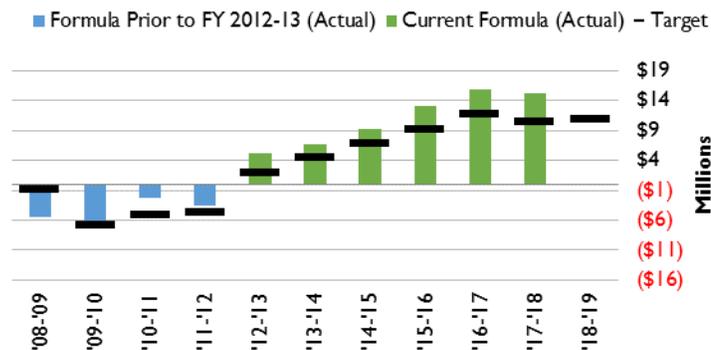
| Incentive Fee Measures | % of Target | Weighted Incentive Fee Percentage |
|--|--------------------|-----------------------------------|
| Gross Operating Results (40%) | 145% | 58.0% |
| Hotel Room Nights (20%) | 110% | 22.1% |
| Estimated Economic Impact (20%) | 103% | 20.6% |
| Theater Occupancy (10%) | No Approved Target | N/A* |
| Customer Satisfaction (10%) | 105% | 10.5% |
| Weighted Incentive Fee Score | | >111.2% |

*Because no target for theater occupancy was established, the weighted incentive fee percentage for theater occupancy was not calculated.

Gross Operating Results – 145% of Target

The Amendment to the Management Agreement defines gross operating results⁹ as gross revenues from operating the Facilities, plus hotel tax revenue,¹⁰ plus revenue from the parking garage at the Convention Center, less certain direct and indirect expenses for operating the Facilities. The calculation does not include City-directed expenses, including, City oversight, fire insurance premiums, repairs and maintenance, depreciation, the management fee paid by City to TSJ, the \$15.2 million payment in FY 2017-18 for debt service for the Convention Center’s original construction, nor does it include the \$8.2 million payment for debt service for the 2011-2013 renovation and expansion.¹¹ For FY 2017-18, TSJ achieved a gross operating results of \$15.2 million compared to a target of \$10.5 million. This was 145 percent of target.

Exhibit 4: Gross Operating Results



Source: Auditor analysis of the Management Agreement, audited financial statements for the Convention and Cultural Affairs Fund, parking garage revenue and expense reports, Budget Office reports for the Convention and Cultural Affairs Fund, and prior TSJ audits.

Note: In 2012-13, the calculation method changed. The blue bars show the old formula, the green bars the new formula. The old formula was: Operating revenues – Operating expenses (excluding: depreciation, oversight, fire insurance, fixed executive management fee, repairs, and maintenance).

⁹ The amendment changed the name of “Gross Operating Profit” to Gross Operating Results. However, the calculation of this measure remained the same in the 2014 Management Agreement.

¹⁰ Hotel taxes are formally known as Transient Occupancy Taxes (TOT). Only the portion that the City transfers to the Convention and Cultural Affairs Fund (Fund 536) counts towards Gross Operating Results. The City collects a tax of 10 percent of the rent that a hotel operator charges to a hotel guest (\$48.95 million in FY 2017-18). Four percent goes into the General Fund (\$19.5 million). Six percent goes into the Transient Occupancy Tax Fund (Fund 461, \$29.4 million). About half of the TOT Fund’s portion subsidizes the Convention and Cultural Facilities (\$14.7 million). Slightly more than a quarter of the TOT Fund’s portion funds the Convention and Visitors Bureau (\$7.5 million) and about another quarter funds cultural grants (\$7 million).

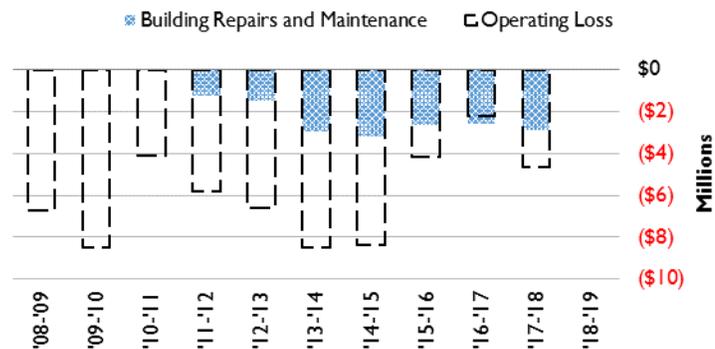
¹¹ The City and Team San Jose agreed that the expansion debt would not count towards gross operating results because it is paid back from a special tax on hotels that are within the Convention Center Facilities District.

The Financial Statements Show an Operating Loss Which Is Funded by Hotel Taxes

While TSJ exceed its gross operating results measure, the audited financial statements for the Convention and Cultural Facilities show an operating loss of about \$4.7 million in FY 2017-18, calculated in accordance with Generally Accepted Accounting Principles (GAAP). The Facilities generally operate at a loss, thus requiring an operating subsidy funded by hotel taxes.¹²

Exhibit 5 shows a 10-year history of operating losses in accordance with GAAP. In FY 2017-18, the nearly \$4.7 million loss recognized on the financial statements included \$2.9 million in repairs and maintenance for upkeep the City-owned facilities.

Exhibit 5: Operating Loss in Accordance with Generally Accepted Accounting Principles¹³



Source: Audited financial statements for the Convention and Cultural Facilities. Beginning with FY 2011-12, we show building repairs and maintenance as separate expenses.

Exhibit 6 reconciles the audited **financial** statements to the **Management Agreement's** definition of gross operating revenue.

¹² The City has not made a significant transfer from the General Fund to the Convention and Cultural Affairs Fund since FY 2009-10.

¹³ In FY 2017-18, the City of San José paid for some repairs, maintenance, and capital improvements to the Convention and Cultural Facilities in the amount of \$7.3 million, including \$6.7 million from the Convention and Cultural Affairs Fund.

Exhibit 6: Reconciliation of Management Agreement Performance Measure of Gross Operating Results to Audited Financial Statements

| | Audited FY 2017-18 Financial Statements | Adjustments for Gross Operating Results per Management Agreement | |
|--|--|--|------|
| Operating Revenues: | | | |
| Building rental | \$ 6,933,518 | | |
| Food and beverage services | \$ 27,604,147 | | |
| Commission revenue | \$ 1,365,929 | | |
| Event electrical/utility services | \$ 313,301 | | |
| Networking Services | \$ 2,078,847 | | |
| Audio/visual services | \$ 305,571 | | |
| Ticketing services | \$ 620,366 | | |
| Telecommunications services | \$ 110,788 | | |
| Equipment rentals | \$ 42,968 | | |
| Event production labor revenues | \$ 14,934,621 | | |
| Other revenues | \$ 486,372 | | |
| Bad Debt Expense | | \$ (46,301) | A |
| Total Operating Revenues | \$ 54,796,428 | | |
| <i>Transient Occupancy Tax revenue to Convention and Cultural Affairs Fund</i> | | \$ 15,176,240 | A, B |
| <i>Parking garage revenue</i> | | \$ 3,536,524 | A |
| Revenues for gross operating results calculation | | \$ 73,462,891 | |
| Operating Expenses: | | | |
| Administrative and general salaries – TSJ | \$ 23,027,772 | | |
| Cost of event production labor | \$ 13,131,930 | | |
| Utilities | \$ 3,160,286 | | |
| Food and beverage costs | \$ 4,002,174 | | |
| Bad debt expense | \$ 46,301 | \$ (46,301) | A |
| Contracted outside services | \$ 5,138,901 | | |
| Professional services | \$ 526,135 | | |
| Operating supplies | \$ 664,010 | | |
| Depreciation | \$ 761,743 | \$ (761,743) | A |
| Repairs and maintenance | \$ 2,890,128 | | |
| Insurance | \$ 294,316 | | |
| City of San José oversight | \$ 742,840 | \$ (742,840) | A |
| Ticketing costs | \$ 82,438 | | |
| Workers' compensation insurance premiums | \$ 1,050,281 | | |
| Fire insurance | \$ 229,217 | \$ (229,217) | A |
| Management and incentive fee – Team San Jose | \$ 1,200,000 | \$ (1,200,000) | C, D |
| Equipment rentals | \$ 214,500 | | |
| City Free Use | \$ 67,350 | \$ (67,350) | A |
| Other expenses | \$ 2,229,707 | | |
| Total Operating Expenses | \$ 59,460,029 | | |
| <i>HVAC Temporary Funding</i> | | \$ 68,537 | |
| <i>CVB expenses paid by Convention and Cultural Affairs Fund</i> | | \$ 500,000 | B |
| <i>Less: City Worker's Compensation</i> | | \$ (60,030) | B |
| <i>Parking garage expenses</i> | | \$ 1,359,545 | B |
| Expenses for gross operating results calculation | | \$ 58,280,630 | |
| Gross Operating Profit or (Loss) | \$ (4,663,601) | \$ 15,182,261 | |

Source: Auditor analysis of audited financial statements for the San José Convention and Cultural Facilities, the Management Agreement, parking garage revenue and expense reports, and Budget Office reports for the Convention and Cultural Affairs Fund.

Notes to Exhibit 6:

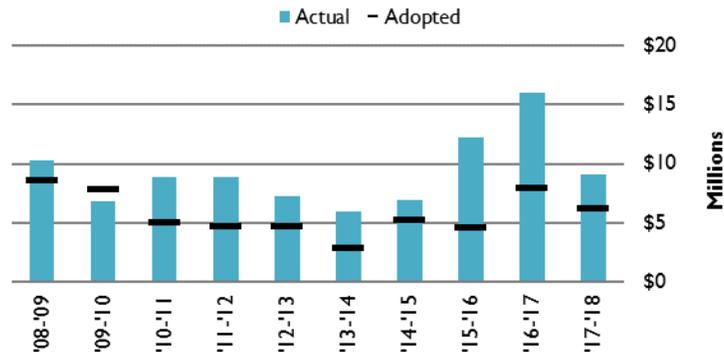
- A. The Amendment to the Management Agreement defines gross operating results to include or exclude these items.

- B. Consistent with prior year’s practice and for purposes of Team San Jose performance, measurement hotel tax was calculated as follows: FY 2017-18 allocation of \$14,764,973 to the Convention and Cultural Affairs Fund, plus \$652,375 attributable to FY 2017-18 hotel activity but allocated to the Fund in FY 2018-19, minus \$241,108 attributable to hotel activity in FY 2016-17 but allocated to the Fund in FY 2017-18. Any hotel tax received in a given year above (or below) the budgeted amount is reconciled and distributed to the Convention and Cultural Affairs Fund in accordance with the San José Municipal Code.
- C. The management fee shown here includes the \$1 million management fee for FY 2016-17 and the \$200,000 incentive fee paid for FY 2017-18 under the Amendment to the Management Agreement.
- D. The City’s approved target included these items.

The Ending Balance in the Convention and Cultural Affairs Fund Has Decreased in the Last Year

The ending balance of the Convention and Cultural Affairs Fund on June 30, 2018 was \$9.1 million – a decrease of \$6.8 million from the prior year. This decrease is primarily attributed to capital improvements at the convention center and cultural facilities. The City spent \$6.7 million on projects including window replacement at the National Civic and restroom remodel at the convention center. The Fund included a capital reserve of \$1.95 million. Exhibit 7 shows a ten-year history of the Fund’s ending balance of the Convention and Cultural Affairs Fund at the end of the fiscal year.

Exhibit 7: Ending Balance of the Convention and Cultural Affairs Fund (Fund 536)

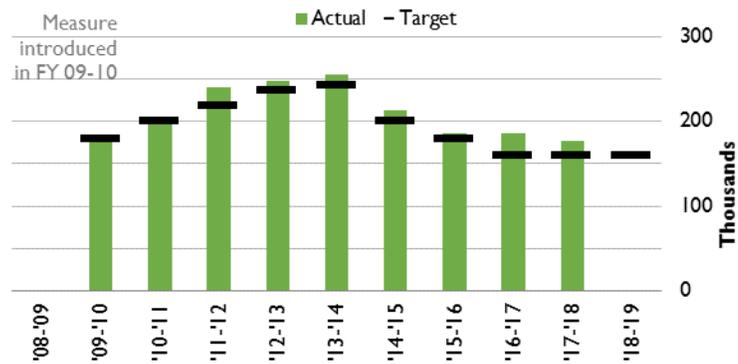


Source: Source and Use Statements in Adopted Budgets and actual fund balance for FY 2017-18

Hotel Room Nights – 110 % of Target

Hotel room nights, as shown in Exhibit 8, is measured as the number of future hotel room nights booked by Team San Jose over the course of the fiscal year. The Amendment to the Management Agreement specifies that the total number of hotel room nights will be measured as 1) the total number of hotel room nights committed by the CVB over the course of the Fiscal Year and 2) the total number of hotel room nights that can be directly or indirectly attributed to activities at the Facilities.

Exhibit 8: Future Hotel Room Nights Booked



Source: Auditor analysis of the Management Agreement, TSJ's hotel room night's production report, third-party reviews of TSJ's hotel room night bookings, and our prior TSJ audits.

TSJ met its hotel night target in each of the nine years it has reported on the measure. In FY 2017-18, the hotel room nights booked were above the target—176,522 hotel room nights¹⁴ were booked compared to a target of 160,000 nights. This was 110 percent of target.

¹⁴ Although 176,522 hotel room nights were booked during the fiscal year, months later in August 2018, 2,573 hotel room nights were canceled. Based on the terms of the agreement, this was not removed from the total booked in the fiscal year.

Estimated Economic Impact – 103 % of Target

Estimated economic impact is an estimation of average daily spending rate multiplied by event attendance and duration. Average daily spending rates vary depending on event type (i.e., conventions and meetings, spectator sports and demonstrations, and participant sports and competitions) and attendee type (i.e., local/social visitors, out-of-town visitors, and exhibitors). Event attendance and the assumed spending rates drive this measure. Exhibit 9 shows the results for estimated economic impact.

Exhibit 9: Estimated Economic Impact



Source: Auditor analysis of the Management Agreement and TSJ event attendance reports, TSJ’s estimated economic impact calculations, and our prior TSJ audits.

In FY 2017-18, the estimated economic impact was above the target—\$115 million in estimated economic impact compared to a target of \$112 million. This was 103 percent of target.

The five events with the highest estimated economic impact contributed 33 percent towards TSJ’s estimated economic impact (\$37.6 million). These events, in alphabetical order included:

- 2018 Apple Worldwide Developers Conference
- FanimeCon 2018
- NVIDIA GPU Technology Conference 2018
- Rock 'n' Roll Half Marathon and Expo
- 2018 Silicon Valley International Auto Show

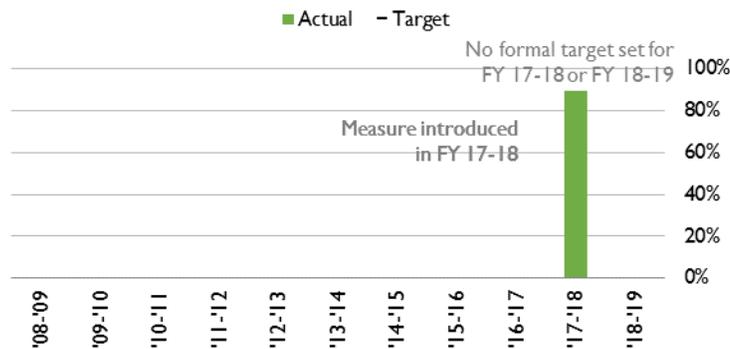
TSJ has met its estimated economic impact targets each of the nine years it has reported on the measure.

Theater Occupancy – No Formal Target for FY 2017-18 or FY 2018-19

Theater occupancy is a new measure in the Amendment to the Management Agreement. It is measured by the number of occupancy days, divided by available days¹⁵ at the four Cultural Facilities (the City National Civic, the Center for the Performing Arts, the California Theatre, and the Montgomery Theater). This includes dances, theater shows, sports events, musicals, and comedy shows, speakers, and cultural performances generally available for the public.

In previous years, the performance measures for TSJ have been brought forward through the Manager's Budget Addendum (MBA) process and ultimately approved as part of the Mayor's June Budget Message. At the time of our audit, there was no set target for FY 2017-18, or FY 2018-19.¹⁶

Exhibit 10: Theater Occupancy



Source: Auditor analysis of the Amendment to the Management Agreement and TSJ's theater occupancy records.

The City's Cultural Facilities were occupied on 518 of 581 available use days (89%). The California Theatre held the most of performances (163) followed by the City National Civic (128), the Center for Performing Arts (120), and the Montgomery Theater (107).

Recommendation #1: The Administration should work with Team San Jose to establish and formalize the target for theater occupancy for FY 2018-19.

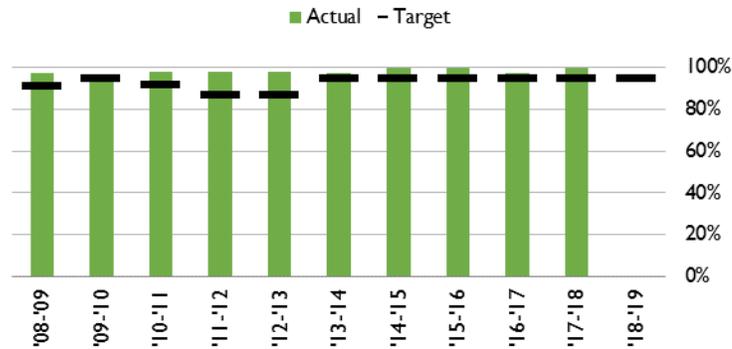
¹⁵ The Amendment to the Management Agreement defines available days as: (a) the number of Thursdays, Fridays, and Saturdays within a fiscal year, minus (b) any such days that fall within a United States holiday period, and minus any such days that are blocked-out for facility repairs. In prior years, available use days include calendar days that are both available and suitable for booking performances and special events excluding move-in and move-out days, typically unsellable weekdays, unsellable holiday periods, and dates held by resident art partners.

¹⁶ Once we brought this to TSJ's attention, TSJ recreated a forecasted target for FY 2017-18 based on the information available to TSJ on May 1, 2017. This target was 432 occupied days out of 581 theater days, 74 percent. The forecasted target for FY 2018-19 was 479 out of 556 available use days, 86%.

Customer Satisfaction – 105% of Target

Customer satisfaction, as shown in Exhibit II, is the percentage of event coordinators who responded to a customer survey with an overall satisfactory rating of the product and services provided. Responses of “excellent,” “very good,” or “good” are considered satisfactory.

Exhibit II: Customer Satisfaction



Source: Auditor analysis of the Management Agreement and its amendment, TSJ’s customer service survey results, prior TSJ audits.

In FY 2017-18, customer satisfaction was above the target—100 percent customer satisfaction compared to a target of 95 percent.¹⁷ This was 105 percent of target.

The response rate was 25 percent. For customer satisfaction, Team San Jose has met or exceeded its targets for all past ten years. According to TSJ and the City, the industry standard is 90 percent.¹⁸

¹⁷ We reviewed the accuracy of the survey results by sampling actual customer survey responses for December 2017.

¹⁸ The Management Agreement and Amendment requires that the City be sent a copy of each survey response. We should note that the City had not been receiving these surveys for multiple years. After notifying the contract manager about this and the requirement, they worked with Team San Jose to update notifications for the contract manager and a City staff person in the Budget office to be notified of survey results.

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Conclusion

Team San Jose (TSJ) exceeded its weighted incentive score target for FY 2017-18, however the amendment to the agreement for management of San José's Convention Center and Cultural Facilities had not been finalized.

In FY 2017-18, TSJ booked over 170,000 hotel room nights, had an estimated economic impact of \$115 million, exceeded its target in gross operating results, reached held 518 days of events at its cultural facilities, and received 100% satisfaction rate of customer service surveys.

RECOMMENDATIONS

Recommendation #1: The Administration should work with Team San Jose to establish and formalize the target for theater occupancy for FY 2018-19.

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TO: Sharon Erickson, City Auditor

FROM: Kim Welsh

SUBJECT: SEE BELOW

DATE: November 16, 2018

**SUBJECT: RESPONSE TO AUDIT OF TEAM SAN JOSE PERFORMANCE
FY 2017-2018**

The Administration has reviewed the City Auditor's report entitled "Team San Jose Performance FY 2017-18." The Administration thanks the City Auditor's Office for its annual efforts to verify Team San Jose's performance. The Administration's response to the audit's one recommendation is presented below.

BACKGROUND

Annually, the City Auditor's Office reviews Team San Jose's documentation of its reported performance on its annual goals for which it receives an incentive fee, should it meet or exceed the goals. The goals are annually submitted to the City Council for approval as part of the Proposed Operating Budget via a Manager's Budget Addendum. Performance goals are recommended to the Council after a review of factors such as past performance, known business, industry trends, and the economy. The targets are negotiated and agreed to by Team San Jose and the City Administration prior to being submitted for Council approval.

RECOMMENDATIONS AND RESPONSE

Recommendation #1: The Administration should work with Team San Jose to establish and formalize the target for theater occupancy for FY 2018-19.

The Administration agrees with the Auditor's recommendation.

As stated in the audit, in October 2017, the City Council authorized the City Manager to negotiate and execute revisions to the Team San Jose master agreement to amend performance measures based on industry best practices and enhance reporting to the Council on Team San Jose's activities. When the FY 18-19 performance measures were developed, the revised agreement with Team Jose had not been executed. Therefore, a new theater performance metric was not submitted as part of the FY 18-19 Operating Budget for Council approval.

HONORABLE MAYOR AND CITY COUNCIL

November 16, 2018

Subject: RESPONSE TO AUDIT OF TEAM SAN JOSE PERFORMANCE FY 2017-18

Page 2

With the revised master agreement finalized, the Administration seeks Council approval of a goal for FY 18-19, which will be evaluated as part of the City Auditor's report at this time next year.

The Theatre Occupancy target is measured by the number of occupancy days, divided by available days at the four cultural facilities managed by Team San Jose: The City National Civic, the Center for the Performing Arts, the California Theatre, and the Montgomery Theatre.

The FY 18-19 Theatre Occupancy target is 86%. This target represents a percentage of occupied days versus available days for the City National Civic, Center for the Performing Arts, California Theatre, and Montgomery Theatre. For FY 18-19, the theater activation target is 479 occupied days of 556 available days for these cultural venues. These estimates are based on leads, historic trends, anticipated bookings by resident art partners such as Broadway San Jose as well as outside rentals, as well as opportunities to flow convention center events into the theaters.

With the acceptance of the Auditor's report, it is recommended that the Council approve the Theatre Occupancy target of 86% for FY 18-19.

/s/

KIM WALES
Deputy City Manager
Director of Economic Development