

Section 3.1: Financial and Operational Status; Compliance Issues

- ◆ **The Zoological Society raised \$11,494,465 against the \$10 million minimum Founders' Fund commitment and expended in excess of \$7 million for operations in each of the first five years of the Management Agreement.**
- ◆ **The Zoological Society developed a planning document in July of 1993 entitled "5-Year Plan: 1993-1998." The 5-Year Plan was approved in concept on July 19, 1993, and, according to Zoo management, was used to guide the Zoo's development. The 5-Year Plan shows that the Zoological Society intended to significantly upgrade and improve Zoo facilities and the overall Zoo experience within the first five years of the Zoological Society's operation, by expending \$30 million in funds raised by the Zoological Society on capital improvements and by instituting managerial and other improvements. A motion to approve a Capital Budget in the amount of \$30 million was passed unanimously by the Board of Directors of the Zoological Society on February 28, 1994. However, only \$10,377,210 of the planned \$30 million was expended on capital improvements (\$6,803,246 in Founders' Fund monies and \$3,573,964 in Capital Campaign monies). The Zoological Society shifted its capital campaign strategy to correspond with the City's Zoo Bond program after recognizing that obtaining significant capital contributions from its donor base was not feasible without the City's capital funding commitment, given the condition of the Zoo. In the professional judgment of the Budget Analyst, the Zoological Society's inability to raise and expend the additional funds on capital projects to upgrade the Zoo and the two-year delay in Zoo Bond sales are the primary reasons the Zoological Society was unable to achieve its major operating and financial objectives during the first five years of the Management Agreement.**
- ◆ **Over the first five years of the Management Agreement, actual operating revenues, including bequests, were \$63,885,195 or \$15,633,805 less than the projected sum of \$79,519,000, which was the five-year operating revenue estimate presented by the Zoological Society when the Zoo Management Agreement was submitted to the Board of Supervisors for approval. Thus, the average annual operating revenue shortfall for the five-year period was \$3,126,761. Actual operating expenditures over the five-year period were \$65,755,637, or \$15,004,259 less than the projected operating expenditure estimate of \$80,759,896. Thus, the average annual operating expenditure shortfall for the five-year period was \$3,000,852.**
- ◆ **Zoological Society staff did not obtain required building and other permits for numerous capital projects and alterations at the Zoo. Thus, required plan checks and inspections were not accomplished and the Zoological Society did not pay required fees to the City. Accordingly, the City Attorney advises that if something happens to one of the structures because of the lack of plan checks and inspections, the City could be held liable.**

As part of our performance audit of the San Francisco Zoological Gardens, we examined the extent to which the Zoological Society is accomplishing the financial and operational objectives that were defined at the time the operation of the San Francisco Zoo was transferred from the Recreation and Park Department to the Zoological Society. Also in this section of the audit we examine whether the Zoological Society is operating in compliance with the provisions of the San Francisco Zoo Lease and Management Agreement and other relevant regulations.

To accomplish these objectives, we:

- Reviewed key documents such as the Management Agreement; the Concepts of Expanded Partnership (the “Concepts”); the 1998 and the 1993 Accreditation Reports of the American Zoological Association (AZA); the Zoological Society’s Draft 5-Year Plan: 1993-1998; USDA Veterinary Inspection Reports; the San Francisco Zoological Gardens Master Plan; the San Francisco Zoo Strategic Plan: 1997-2004; and the March of 1998 Update of Strategic Plan: Financial Plan;
- Interviewed USDA staff and City and County of San Francisco staff responsible for oversight of various functions performed by the Zoo;
- Reviewed performance measures in various reports;
- Conducted visual inspections of facilities;
- Examined in detail the audited financial report for FY 1997-98;
- Examined the pre-closing trial balance report for FY 1997-98;
- Developed a detailed analysis of revenues and expenses for FY 1997-98 based on the Zoo’s pre-closing trial balance report for that year;
- Thereafter, we examined in detail the audited financial statements for FY 1989-90 through FY 1996-97 and developed detailed analyses of revenues and expenses for that period.

Background

“Concepts” for the Expanded Partnership

In early 1992, the Mayor's Office, through the Recreation and Park Department, requested that the San Francisco Zoological Society submit a proposal to expand its role to include management of the entire Zoo, including increased private funding for Zoo operations and maintenance.

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On September 1, 1992, the Recreation and Park Commission adopted Resolution No. 16420 expressing support for an expansion of the City's partnership with the San Francisco Zoological Society on the basis of a six-page document entitled "Concepts for an Expanded Partnership Lease Agreement" (the "Concepts"), which with supporting documents outlined a proposal to transfer decision-making authority and operating responsibility for the Zoo from the City to the Zoological Society (the "Proposal"). The Zoological Society's Board of Directors had previously approved the "Concepts" in April of 1992.

Funding and Accreditation Status in FY 1992-93

At the time the Zoological Society assumed operational control of the Zoo, the following conditions existed:

1. The Capital Asset Management Report of November 29, 1990, included approximately \$10.1 million in recommended capital improvements, solely for basic safety and structural improvements.
- 2 The American Zoological Association had tabled the Zoo's request for re-accreditation in September of 1992 due to concerns about the poor physical plant, the lack of funding to make major capital improvements, and inadequate funding for operations.
3. The Zoo's General Fund subsidy from the City was reduced by \$644,254, or by 13.5 percent, from FY 1991-92 to FY 1992-93. Eight positions were eliminated from the Zoo's FY 1992-93 General Fund budget

Projections of Operating Revenues and Expenses Contained in the Rec/Park-Zoological Society Proposal

The "Proposal" included revenue and expense projections prepared by the Recreation and Park Department and the Zoological Society for the first five years of the proposed expanded partnership. These projections are shown in Exhibit 3.1.1 in the Appendix to this report. The budget summary shows that annual *operating expenditures* for the Zoo were expected to increase from an estimated \$11,850,254 in FY 1991-92 to \$18,821,000 in FY 1997-98, an average annual increase of approximately eight percent. Exhibit 3.1.2 in the Appendix to this report, an extract of a Zoological Society planning document, shows additional revenue and operating assumptions and projections.

Operating revenues were projected to increase by approximately 12.8 percent per year over the five-year period, including an estimated 15.7 percent average annual

increase in memberships in the Zoological Society, a 15.5 percent average annual increase in contributions and events, and an 18.8 percent average annual increase in net profits from retail sales at the Zoo.

Financial Performance

Table 3.1.1 below shows actual operating revenues compared to the projected operating revenues for FY 1993-94 through FY 1997-98 contained in Exhibit 3.1.1.

Table 3.1.1
Actual Revenues Compared to
Projected Operating Revenues

<u>Year</u>	<u>Projected Revenues</u>	<u>Actual Revenues</u>	<u>Difference</u>
1993-94	\$12,974,000	\$10,794,196*	\$2,179,804
1994-95	14,465,000	11,237,324	3,227,676
1995-96	15,922,000	12,251,313	3,670,687
1996-97	17,437,000	13,660,485	3,776,515
1997-98	<u>18,721,000</u>	<u>13,805,634</u>	<u>4,915,366</u>
Total Revenues	\$79,519,000	\$61,748,952	\$17,770,048
Bequests		<u>2,136,243</u>	
Total	\$79,519,000	\$63,885,195	\$15,633,805

Over the first five-year period of the Management Agreement, actual operating revenues, including bequests, were \$15,633,805 or approximately 19.6 percent less than projected operating revenues, which computes to an average shortfall of \$3,126,761 per year.

Table 3.1.2 below shows actual operating expenditures compared to the projected operating expenses for FY 1993-94 through FY 1997-98.

Table 3.1.2
Actual Expenses Compared to
Projected Operating Expenses

<u>Year</u>	<u>Projected Expenses</u>	<u>Actual Expenses</u>	<u>Difference</u>
1993-94	\$13,691,746	\$11,322,273*	\$2,369,473
1994-95	14,702,780	12,387,744	2,315,036
1995-96	16,107,370	13,341,740	2,765,630
1996-97	17,437,000	14,615,865	2,821,135
1997-98	<u>18,821,000</u>	<u>14,088,015</u>	<u>4,732,985</u>
Total	\$80,759,896	\$65,755,637	\$15,004,259

*Derived by allocating \$1,086,023 of City funds to revenues and expenses recorded by the Zoological Society for FY 1993-94. The Zoological Society did not assume control of the Zoo until October of 1993.

Over the first five-year period of the Management Agreement, total actual operating expenditures were \$15,004,259 or approximately 18.6 percent less than projected operating expenditures, which computes to an average of \$3,000,851 per year.

Analysis of Projected versus Actual Revenues

Table 3.1.3 below is a comparison of projected and actual operating revenue sources for the five-year period of FY 1993-94 through FY 1997-98. The major shortfalls were in Admission Fees (\$7,624,667), which are a function of the attendance shortfall; Retail Services (\$7,567,200), which were and continue to be a major problem area at the Zoo; and Membership Dues (\$2,946,213), which are due to a very large shortfall in projected Zoological Society memberships. Current Zoological Society membership is approximately 29,000. Exhibit 3.1.2 shows that the proposal projected a membership total of 47,000.

Table 3.1.3
Projected Revenue Source Amounts
Compared to Actual Revenue Source Amounts
FY 1993 94 through FY 1997-98

	Projected	Actual	Difference
Revenues			
Admission Fees	\$16,458,000	\$8,833,333	\$7,624,667
Retail Services	23,040,000	15,472,800	7,567,200
Membership Dues	9,367,000	6,420,787	2,946,213
Contributions/Events	7,310,000	7,452,038	(142,038)
Children's Zoo	1,349,000	1,009,914	339,086
Other	<u>1,995,000</u>	<u>2,560,080</u>	<u>(565,080)</u>
Total Non-Gen. Fund	\$59,519,000	\$41,748,952	\$17,770,048
Management Fee	20,000,000	20,000,000	-
Bequests		<u>2,136,243</u>	<u>(2,136,243)</u>
Total	\$79,519,000	\$63,885,195	\$15,633,805

Capital Project Funding

Section 15 of the Management Agreement, "Fiscal Matters," includes the following provisions concerning funding:

- **Founders' Fund:** The Zoological Society agreed to provide from private sources a minimum of \$10 million within the first five years of the Management Agreement. All amounts deposited in the Founders' Fund are to be expended approximately as follows: \$5 million shall be used to fund Zoo capital improvements; \$2 million shall be used to fund Zoo operating

expenses; and \$3 million shall be used to increase the Zoological Society's Endowment Fund.

- Capital Campaign: The Zoological Society agreed to use its reasonable efforts to initiate and complete a fund-raising campaign in a minimum amount of \$25 million to finance the construction of capital improvements at the Zoo. [The Management Agreement does not specify a time limit for completing the Capital Campaign].
- Bond Issues: The City agreed to use its reasonable efforts to place before the voters during the initial term of the Management Agreement [the first five years] a measure calling for the issuance of general obligation bonds or other acceptable method of public financing in an aggregate amount of at least \$25 million to finance capital improvements at the Zoo, including a new front Zoo entrance, new animal exhibits, and such other facilities as the City and the Zoological Society may reasonably agree [A Zoo bond measure in the amount of \$48 million was approved by the electorate in the June 1997 election. The first appropriation of that \$48 million bond measure in the amount of \$16,898,894 was approved by the Board of Supervisors in November of 1999].

The Zoological Society raised a total of \$11,494,465 for the Founders' Fund by FY 1996-97, \$6,803,243 of which was expended on capital projects, as shown in Exhibit 3.1.3 of this report. Exhibit 3.1.4 of this report lists the capital projects and amounts that were funded by the Founders' Fund.

The Zoological Society has raised a total of \$14.2 million in Capital Campaign cash and written pledges as of June 30, 1999, as shown in Exhibit 3.1.5 of this report (As reported by the Zoological Society, approximately \$21 million in cash, written pledges, contingency pledges, and verbal pledges had been recorded as of December of 1999 for the Capital Campaign).

The Zoological Society developed a planning document in July of 1993 entitled "5-Year Plan: 1993-1998." The 5-Year Plan was approved in concept on July 19, 1993, and, according to Zoo management, was used to guide the Zoo's development although never formally adopted. The 5-Year Plan, in our opinion, is an excellent document that covers the Zoo's key results areas of conservation, education, research, recreation, and economics.

Exhibit 3.1.9 of this report (16 pages) contains portions of the 5-Year Plan. Exhibit 3.1.9 shows that the Zoological Society planned to raise and expend \$30 million (\$5 million in Founders' Fund monies and \$25 million in Capital Campaign) on new capital improvements and renovation projects during the first five years of the Management Agreement. A motion to approve a Capital Budget in the amount of \$30 million was passed unanimously by the Board of Directors of the Zoological Society on February 28, 1994. However, as shown in Exhibit 3.1.6 of this report,

only a total of \$3,573,967 (\$912,645 in FY 1996-97 plus \$2,661,322 in FY 1997-98) of the Capital Campaign objective of \$25 million had been expended through FY 1997-98.

In the professional judgment of the Budget Analyst, the failure to raise the necessary funds to execute the renovation and new exhibit projects shown in Exhibit 3.1.9 was the primary reason the Zoological Society was unable to generate the attendance necessary to meet its Admission Fee and Retail Services revenue objectives, and thus generate the operating funds necessary to sufficiently improve the visitors' experience at the Zoo

Debt Financing of Operating and Capital Expenditures

In order to fund Zoo operations at a reasonable level though not generating sufficient operating revenues to do so, the Zoological Society began to incur higher long-term debt. The information that follows in this section provides an understanding of the Zoological Society's financial operations and shows why the Zoological Society found it necessary to incur the long-term debt. Most of the financial information in this section has been extracted and arrayed from the Zoological Society's Annual Audited Financial Statements. Summaries of those audited financial statements are included in Exhibit 3.1.7 of this report.

Operating Revenues and Expenses

Table 3.1.4, "Operating Revenues and Expenses," shows that operating revenues, including bequests, increased by \$1,952,207 or 15.8 percent, from \$12,361,753 (\$11,237,423 plus \$1,124,429) in FY 1994-95 to \$14,313,960 (\$13,805,634 plus \$508,326) in FY 1997-98, which computes to an annual compound rate of 5.0 percent.

Table 3.1.4
Operating Revenues and Expenses

	<u>FY 97-98</u>	<u>FY 96-97</u>	<u>FY 95-96</u>	<u>FY 94-95</u>	<u>FY 93-94</u>
Support & Revenues	\$13,805,634	\$13,660,485	\$12,251,313	\$11,237,324	\$9,708,173
Expenses	<u>14,088,015</u>	<u>14,615,865</u>	<u>13,341,740</u>	<u>12,387,744</u>	<u>10,236,250</u>
Change in Net Assets before Bequests & Adjustments	(\$282,381)	(\$955,380)	(\$1,090,427)	(\$1,150,420)	(\$528,077)
Bequests	508,326	359,043	144,445	1,124,429	
Acctng Change/Donation	<u>0</u>	<u>375,564</u>	<u>0</u>	<u>0</u>	<u>0</u>
Change in Net Assets	\$225,945	\$220,773	(\$945,982)	(\$25,991)	(\$528,077)

Table 3.1.4 also shows that Operating Expenses increased by \$1,700,271 or 13.7 percent, from \$12,387,744 in FY 1994-95 to \$14,088,015 in FY 1997-98, or at a compound rate of 4.4 percent. However, given the underfunded financial position and unsatisfactory physical condition the San Francisco Zoo was in at

the time the Zoological Society assumed management of the facility, a growth rate of 4.4 percent in expenses has not been sufficient to upgrade the quality the facility to a desired state.

As recorded in the Zoological Society's audited financial statements and as shown in Table 3.1.4, Operating Revenue and Support, which includes the \$4,000,500 management fee payment by the City to the Zoological Society, fell short of Operating Expenses by a total of \$4,006,685 for the five-year period, or by an average of \$801,337 per year. Bequests reduced the Support and Revenue shortfall by \$2,136,243, from \$4,006,685 to \$1,870,442, or by an average of \$427,248 per year. The audited financial statements and Table 3.1.4 also show that the Zoological Society first broke even on an accrual accounting basis in FY 1996-97 by showing a positive \$220,773 change in Net Assets for that fiscal year.

Cash Flows and Long-term Debt

Operating Revenues and Expenses are but one way of evaluating an organization's financial status. Additional valuable information is contained in an organization's audited Statements of Cash Flows.

Revenue and Expense accounts, accounts from which an organization's Statement of Activities (Income Statement, for private sector organizations) are derived, contain items that do not affect inflows or outflows of cash, such as contribution pledges, as a revenue source, and depreciation, as an expense source. Organizations require cash to thrive and to survive. The figures extracted from the Zoological Society's Statements of Cash Flow, displayed in Table 3.1.5 below, show that significant net outflows of cash, in the amounts of \$896,042 and \$788,589, occurred in fiscal years 1996-97 and 1997-98, respectively.

Table 3.1.5
Unrestricted Fund Cash Flows

	FY 97-98	FY 96-97	FY 95-96	FY 94-95	FY 93-94
Cash & Equiv:					
Beginning of Year	\$1,852,764	\$2,748,806	\$2,148,687	\$2,138,329	\$391,921
Net cash provided by (used in):					
Operating Activities	(\$96,756)	(\$1,893,583)	(\$302,464)	\$148,572	\$1,487,776
Investing Activities	(93,328)	208,096	(68,996)	(38,446)	(28,883)
Financing Activities	<u>(598,505)</u>	<u>789,445</u>	<u>971,579</u>	<u>(99,768)</u>	<u>287,515</u>
Net Increase (decrease)	(\$788,589)	(\$896,042)	\$600,119	\$10,358	\$1,746,408
Cash & Equiv:					
End of Year	\$1,064,175	\$1,852,764	\$2,748,806	\$2,148,687	\$2,138,329

The figures also show that the Zoological Society ended each of those fiscal years with cash and cash equivalents in the amounts of \$1,852,766 and \$1,064,177, respectively. However, as shown in the Table 3.1.6, the Zoological

Society required those funds to cover the significant accounts payable less accounts receivable balances.

Table 3.1.6
Accounts Payable compared to Accounts Receivable

	<u>FY 97-98</u>	<u>FY 96-97</u>	<u>FY 95-96</u>	<u>FY 94-95</u>	<u>FY 93-94</u>	<u>FY 89-90</u>
Accounts Receivable	\$377,978	\$689,970	\$721,757	\$495,932	\$608,743	\$0
Accounts Payable	<u>1,611,830</u>	<u>2,047,932</u>	<u>3,321,456</u>	<u>2,468,834</u>	<u>2,580,304</u>	<u>119,903</u>
Receivables less Payables	(\$1,233,852)	(\$1,357,962)	(\$2,599,699)	(\$1,972,902)	(\$1,971,561)	(\$114,746)

The great majority of the accounts receivable amounts were due the Zoological Society by the City. Also, the majority of the accounts payable amounts were due the City by the Zoological Society.

As shown in Table 3.1.7 on the following page, the Zoological Society began to incur significant amounts of long-term debt in FY 1994-95, which peaked in FY 1996-97 in the amount of \$2,428,741.

Table 3.1.7
Long-term Debt

	<u>FY 97-98</u>	<u>FY 96-97</u>	<u>FY 95-96</u>	<u>FY 94-95</u>	<u>FY 93-94</u>
Current Portion of Long-term Debt	\$8,389	\$2,405,791	\$1,604,296	\$960,805	\$62,485
Long-term Portion of Long-term Debt	<u>1,821,847</u>	<u>22,950</u>	<u>35,000</u>	<u>95,000</u>	<u>355,000</u>
Total	\$1,830,236	\$2,428,741	\$1,639,296	\$1,055,805	\$417,485

In its most recent long-term debt agreement, the Zoological Society, in August of 1998, entered into an unsecured revolving line-of-credit agreement with a bank. According to the audited financial statements for FY 1997-98, the Zoological Society may borrow up to \$5 million at the Bank's Reference Rate minus 0.25 percent through August 1, 2005. Interest is due monthly with principal payments starting August 1, 2000, at \$33,333 per month. As of August 20, 1999, the balance owed on the unsecured revolving line-of-credit was \$1,194,350.45.

In addition to Cash and Cash Equivalents balances averaging \$1,990,552 for fiscal years 1993-94 through 1997-98 in its Unrestricted Fund, the Zoological Society had Unrestricted Fund Investment balances averaging \$1,693,184 for the same time period. Some have suggested that the Zoological Society's long-term debt could be eliminated by using Investment funds to repay the revolving line-of-credit balance, but that to do so would be unwise because the Investments are achieving a much higher rate-of-return than the loan rate. Table 3.1.8 shows the Zoological Society's Unrestricted Fund Investment balances for FY 1993-94 through FY 1997-98 and the Investment Income derived there from for the same time period.

Table 3.1.8
Unrestricted Fund Investments and
Investment Income

	<u>FY 97-98</u>	<u>FY 96-97</u>	<u>FY 95-96</u>	<u>FY 94-95</u>	<u>FY 93-94</u>
Unrestricted Investments	\$1,895,779	\$1,631,356	\$1,933,372	\$1,622,781	\$1,382,633
Investment Income	\$397,722	\$306,125	\$225,690	\$173,077	226,415

In FY 1997-98, the Zoological Society achieved an investment return of approximately 22.6 percent (determined by adding the fiscal year 1997-98 and 1996-97 ending balances, dividing that sum by two, and then dividing that sum into the investment income figure of \$397,722), which is far in excess of the approximately 6.95 percent paid on its revolving line-of-credit. Also, it is true that the Investment balance could be used to pay off the loan balance, but only for the existing loan balance. And then the Investment Income, which is used to fund Operating Expenses, would be significantly reduced. If subsequent years bore sizeable cash outflows, as occurred in FY 1996-97 and FY 1997-98, the Zoological Society would have to borrow additional funds, because the Investment balances would be depleted.

The Budget Analyst is not suggesting that the Zoological Society should use its Investment balance to pay off its long-term loan balance. We are simply stating that the Zoological Society is not generating sufficient cash to fund its current level of expenses and that the Zoological Society should take steps to enhance operating revenues. Although we believe that there are some efficiencies that can be achieved in the Zoo's operations, as are discussed in this audit report, we also are not suggesting that the level of outlays be reduced in total, which we think would result in reduced revenues. Our point is that the Zoological Society must increase revenues to fund activities that will increase Zoo attendance or it will be saddled with a significant level of debt as the Master Plan exhibits are completed and become operational.

Meeting Minutes of the Zoological Society's Finance Committee

The Budget Analyst obtained the meeting minutes of the Zoological Society's Finance Committee for the period of January 1997 through March of 1999. The following two quotes included in the meeting minutes for the dates indicated further attest to the Society's cash needs:

Friday, December 12, 1997

"Item 4. Cash availability for operations is week to week with no reserves for the winter slow business cycle. (Name) directed (Name) to clear his calendar and prepare a schedule of cash flow for the next meeting."

Friday, January 16, 1998

“Item 3 An eight-week cash flow analysis was presented to the committee indicating an immediate (End of January) need for cash to fund operating deficits generated in the first five months of the fiscal year. After a thorough discussion a motion was made to increase Bank Borrowing up to an additional \$500,000 to cover interim cash needs. Funds to be repaid by the end of the Fiscal Year.”

What the Zoological Society Should Do in the Near Term to Increase Revenues and Improve the Zoo

The first six recommendations of this report section are a near-term action plan that is based on our total evaluation of the Zoo’s operating and financial status and how best to bridge the time span from now until substantial completion of Phase II in 2002/2003. Some of these recommendations also appear in other sections of this audit report pertaining to the particular subject they address.

Expense Control

The Budget Analyst has developed detailed expense schedules from the Zoo’s Trial Balance reports for fiscal years 1989-90 through 1997-98, which we used for analytical reviews in some of the sections of this audit report. The schedules consist of 22 pages, 11 for each half of the total period covered. One page of the schedules is shown in Exhibit 3.1.8 of this report.

Concerning Exhibit 3.1.8, the Food Services section highlighted in the upper portion of the exhibit shows Food Sales and Cost of Goods Sold figures for fiscal years 1994-95 through 1997-98. Although externalities can skew expected relationships, in general, a positive correlation between Food Sales and Cost of Goods Sold for Food Services in any given year should occur. Note that Food Sales decreased by \$258,898 from FY 1996-97 to FY 1997-98, from \$1,691,136 to \$1,432,238. However, instead of decreasing, Cost of Sales increased between the two fiscal years by \$2,973, from \$564,693 to \$567,666. According to Zoo management, Cost of Goods Sold did not show a corresponding decrease with the reduction in Food Sales because a new Visitor Services Manager experimented with food service promotions that proved to be unprofitable.

The Zoological Society needs to closely control expenses on a monthly basis, and for that purpose the Director of Finance publishes a Statement of Income and Expenses. However, the schedule shown in Exhibit 3.1.8 provides detailed revenue and expense information over an extended time base that normalizes seasonal effects. We recommend that the Zoological Society develop and use revenue and

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expense schedules of the type shown in Exhibit 3.1.8. Accordingly, we have provided the set of schedules covering fiscal years 1989-90 through 1997-98, in electronic form to the Zoological Society's Deputy Director.

Effects of Revenue Shortfalls on Zoo Staff

The revenue shortfalls experienced by the Zoological Society have had a very negative effect on Zoo staff. Many questions to Zoo staff concerning an operational issue have been answered with "that's not in the budget" or with "we don't have funding for that." As Dr. Parrott states in his evaluation beginning at the bottom of page 34 of this audit report, "The revenue urgency and sense of vulnerability permeates the organization."

Compliance with Management Agreement Requirements

By virtue of the provisions contained in the Management Agreement between the City and the Zoological Society, the Zoological Society assumed a set of obligations and compliance requirements contained in various City, state, and federal laws, rules, and regulations. This audit report section cites certain compliance requirements and provides a description of the Zoological Society's adherence to the requirements.

Section 6.1: This section is concerned with the **timeliness of payments** made by the San Francisco Zoological Society to the City for services rendered.

Status: Payments for services due the City by the Zoological Society have not always been made in a timely fashion, as documented in Section 1.3 of this audit report.

Section 9.1: This section requires that the Zoological Society shall cause both itself and the Zoo to be at all times (1) **accredited in good standing** with the American Zoological Society, and (2) **licensed** with the United States Department of Agriculture.

Status: The Zoo has maintained its accreditation with the AZA and its license with the USDA. However, Zoo management has not appropriately addressed the inspection findings of the USDA, as covered in Section 1.1 of this audit report. Zoo management has taken steps to correct this situation.

Section 10.1: This section is concerned with the **capital improvements** made by the Zoological Society and specifies that (1) the Zoological Society shall provide copies of the final, as-built plans to the Department of Recreation and Park, and (2) any alterations of capital improvements made by the Zoological Society shall comply with applicable local, state, and federal laws, rules and regulations, and the Zoological Society shall obtain permits for such alterations and capital improvements.

Status: A major deficiency exists with respect to the requirement to obtain permits for alterations and for capital improvements. Table 3.1.9 shown below lists alterations and capital projects performed at the Zoo for which our review of Department of Building Inspection permit files indicate that building, electrical, plumbing, or mechanical permits, as may be required by the individual project, were not obtained by the Zoological Society. Table 3.1.9 also contains approximate costs for DBI plan check and building permit fees, but not additional fees, such as electrical and plumbing permit fees, that may be applicable to individual projects. The Budget Analyst is recommending that DBI defer such fees so that the Zoo can apply those funds to construction modifications needed to bring the capital projects constructed without permits into compliance with the Building Code. Zoo management has begun to work with staff of the Department of Building Inspection (DBI) to comply with permit requirements.

Table 3.1.9
Zoo Projects without Building Permits on File

Project	Date	Cost	Bldg. Permit Cost	Plan Check Cost	Total Plan Check and Permit Costs
Triple Grotto Project	93/94	\$12,816	\$264.55	\$132.28	\$396.83
Visitor Services Renovation	93/94, 94/95	69,345	900.90	450.45	1351.35
Flamingo Project	93/94, 94/95	38,600	619.45	309.73	929.18
Monkey Island	95/96	18,221	362.05	181.03	543.08
Service/Support Renovation	93-98	118,418	1,253.75	629.75	1,883.50
Warthog Exhibit	95/96	105,481	1,172.50	587.60	1,760.10
Children's Zoo Renov.	95-98	148,216	1,441.25	727.35	2,168.60
Elephant Renovation	95-97	113,575	1,222.50	613.60	1,836.10
Mothers Bldg. Renov.	95-97	27,593	494.33	247.16	741.49
Aye Aye Exhibit	97-98	67,429	885.30	442.65	1,327.95
Kodiak Bear Exhibit	97-98	28,526	505.70	252.85	758.55
South American Gateway	94/95	8,845	199.35	99.78	299.13
Picnic/Overnight	97/98	34,196	573.95	286.98	860.93
Lion Cub Exhibit	96/97	280,825	2,266.25	1,156.35	3,422.60
Improvement LGFP&R	95/96	8,438	199.55	99.78	299.33
Demolition Cat/Monkey	95/96	163,994	1,535.00	776.10	2,311.10
Macropod Exhibit	94/95	475,616	3,485.00	1,790.10	5,275.10
White Alligator	95/96	150,681	1,447.50	730.60	2,178.10
Support Facilities	95/96	104,168	1,166.25	584.35	1,750.60
Puente Al Sur	98/99	250,671	<u>2,078.75</u>	<u>1,058.85</u>	<u>3,137.60</u>
Total			\$22,073.88	\$11,157.34	\$33,231.22

Section 12.2: This section specifies that the Zoological Society shall **care for all Zoo animals** in accordance with all federal, state, and local laws and regulations, and in accordance with the policies and guidelines adopted by the AZA.

Status: As reported in Section 1.1 of this audit report, based on Dr. Joel Parrott's comprehensive evaluation, veterinary care at the San Francisco Zoo is excellent and general care is good, although the existing Zoo facilities limit the ability of management to provide desirable habitats. Further, according to Dr. Parrott, current animal care is vastly superior to that which was provided in the late 1980's and the early 1990's. As stated in Dr. Parrott's report, the Zoo should continue to improve its animal enrichment activities.

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Section 12.4: This section specifies that the Zoological Society shall **provide animal and veterinary care to the bison at Golden Gate Park** and consultation regarding capital improvements to the bison exhibit located therein.

Status: Section 1.1 of this audit report covers the actions required of the Department of Recreation and Park to improve conditions for the bison in Golden Gate Park.

Section 13.1: This section specifies that the Zoological Society shall **maintain the Zoo in a clean, safe, and sanitary and sightly condition.**

Status: As reported in Sections 1.4 and 2 of this audit report, much remains to be accomplished to bring the buildings and grounds up to an attractive condition.

Section 15.1 Founders' Fund: \$10 million

Section 15.2. Capital Campaign. \$25 million

Section 15.3. SFZS Revenue: Payment of Expenses

Under Section 15.1 of the Management Agreement, the SFZS agreed to establish a "Founders' Fund" from private sources in the minimum amount of \$10 million within the first five year term of the Management Agreement. Section 15.1 further specifies that monies expended from the Founders' Fund would be approximately as follows: \$5 million for Zoo capital improvements; \$2 million for Zoo operating expenses; and \$3 million to increase the SFZS Endowment Fund (a fund containing restricted contributed assets whereby only income generated by the assets may be used for operating purposes). Exhibit 3.1.3 of this report shows that the Zoological Society collected a total of \$11,494,465 in fulfillment of its Founders' Fund commitment. Exhibit 3.1.4 of this report shows the specific projects, totaling \$6,803,246 in Founders' Fund monies, which were funded in accordance with the Agreement.

Under Section 15.2 of the Management Agreement, the SFZS agreed to use its reasonable efforts to initiate and complete a fund-raising campaign (the "Capital Campaign") in the minimum amount of \$25 million to finance the construction of capital improvements at the Zoo. Exhibit 3.1.5 of this report shows the periods in which Capital Campaign funds in the amount of \$14,174,411 (\$9,380,309 in cash and \$4,794,102 in written pledges) have been received. Exhibit 3.1.6 shows the projects to which Capital Campaign funds in the amount of \$5,775,870 have been applied.

Section 15.10: This section specifies that within 30 days after the end of each fiscal year, the Zoological Society shall arrange for an audit of its books and records by an independent, certified public accountant approved by the Controller. Section 15.10

Section 3.1: Financial and Operational Status; Compliance Issues

further specifies that the Zoological Society shall deliver to the Recreation and Park Commission for its acceptance an original, signed copy of such annual report by the earlier of 30 days after the completion of the audit or 120 days after the end of the fiscal year covered by the audit.

Status: *For fiscal years 1993-94 through 1997-98, the letters signed by the auditors transmitting the audited financial statements to the Zoological Society are dated no later than September 12. However, for fiscal year 1998-99, the audited financial statements had not been presented to the Recreation and Park Commission by November 19, 1999.*

Section 16.2: This section specifies that the Zoological Society shall **provide public access to information** concerning the operation of the Zoo to the same extent that such information would have been available to the public pursuant to local ordinances if the Department had continued to operate the Zoo in the same manner as it did prior to the date of the Agreement.

Status: *The Joint Zoo Committee reviews major Zoo activities and decisions in public and solicits public comment. The Zoological Society is now serving an expanded function with a citizenry accustomed to reviewing and questioning everything. In our opinion, the Zoological Society has nothing to hide and in certain respects, has performed admirably. We therefore urge a more “open door” policy to public inquiries and requests for information.*

Section 17: Insurance.

Status: *Insurance requirements and issues are covered in Section 13.3 of this audit report.*

5-Year Plan: 1993 – 1998

As previously stated, The Zoological Society developed a planning document in July of 1993 entitled 5-Year Plan: 1993-1998. The 5-Year Plan was not formally adopted, but was used as a working document to guide the Zoo’s development. The 5-Year Plan covers the Zoo’s key results areas of conservation, education, research, recreation, and economics. The Zoological Society has accomplished many of the objectives contained in the 5-Year Plan, including a significant number of new capital improvements and renovation projects that we have included in the Introduction to this audit report. The 5-Year Plan included objectives and, in some cases, detailed plans for specific capital projects with an estimated cost of \$10 million, including an African Savanna project, visitor pathways, options for empty exhibit spaces, and renovation projects

Section 3.1: Financial and Operational Status; Compliance Issues

One Year Plan (Of the 5-Year Plan)

- Objective: Eliminate caged feeling and improve animal conditions
Renovate or demolish empty exhibits
Reduce chain link, asphalt, replant and add color, particularly at Entrances and Loop System.
- Objective: Improve visitor experience
Improve cleanliness throughout park.
Provide more information on Zoo programs, animals, and plans.
Establish visual identity, unified graphics.
- Comment: We cannot emphasize too strongly how important a clean, attractive facility with informative and unified graphics signage is to the impression made on Zoo visitors. This issue is addressed in Sections 1.1, 1.4, and 2 of this audit report.
- Objective: Develop integrated trained professional staff
Improve customer service skills of all staff and volunteers
Improve internal communications and build pride in institution
Improve planning skills of senior management
- Comments: Zoo management should continue to stress the importance of good customer service.

Internal communications, particularly within the Animal Management Department, are in great need of improvement. A significant communications problem exists between many of the Animal Keepers and Zoo management, as cited in Section 1.1 of this audit report.

The Zoo needs to improve its planning processes, particularly at the top level. The Zoo Director, with the assistance of his primary staff, but with the opportunity for feedback from everyone who works at the Zoo, should establish ambitious but attainable objectives, measurable in construct and numbering between five and seven, that everyone in the Zoo can relate to. Those objectives should be based on the Zoo's "Key Results Areas" (KRAs) and should, in general, provide the basis for objective setting down through the organization.

The Oakland Zoo has a workable set of objectives, which we have provided to San Francisco Zoo management. Also, we have provided the Zoo Director with a time-tested text on setting goals and objectives that should assist the organization in developing good objectives, action plans, and controls.

The One Year-Five Year Plan: Goal #6: Community

Objective: Establish target objectives to increase ethnic diversity in Board of Directors, staff, volunteers, and community served.

Comment: The San Francisco Zoological Society has not achieved ethnic diversity within its Board of Directors. Table 3.1.10 shows the ethnic status of the Zoological Society's Board of Directors.

**Table 3.1.10
Ethnic Diversity: San Francisco Zoological Society
Board of Directors
April 1999**

<u>Ethnicity</u>	<u>Number</u>	<u>Percentage</u>
White	53	93.0
African American	2	3.5
Hispanic	0	0.0
Asian	2	3.5
Native American	<u>0</u>	<u>0.0</u>
Total	57	100.0

As shown, as of September 1999, the San Francisco Zoological Society Board of Directors consisted of 53 White members, two African American members, no Hispanic or Native American members, and two Asian members.

In addition to the foregoing, ethnic minorities are not represented in any of the management positions reporting to the Director of the Zoo.

Women are especially well represented throughout the management and staff of the Zoo.

CONCLUSIONS

The Zoological Society has met or is meeting the minimum financial obligations contained in the Management Agreement. However, those financial obligations do not insure the development of a quality facility.

The Zoological Society developed a planning document in July of 1993 entitled "5-Year Plan: 1993-1998." The 5-Year Plan was approved in concept on July 19, 1993, and, according to Zoo management, was used to guide the Zoo's development although never formally adopted. The 5-Year Plan shows that the Zoological Society intended to

significantly upgrade and improve Zoo facilities and the overall Zoo experience within the first five years of the Zoological Society's operation, by expending \$30 million in funds raised by the Zoological Society on capital improvements and by instituting managerial and other improvements. A motion to approve a Capital Budget in the amount of \$30 million was passed unanimously by the Board of Directors of the Zoological Society on February 28, 1994. However, only \$10,377,210 of the planned \$30 million was expended on capital improvements (\$6,803,246 in Founders' Fund monies and \$3,573,964 in Capital Campaign monies). The Zoological Society shifted its capital campaign strategy to correspond with the City's Zoo Bond program after recognizing that obtaining significant capital contributions from its donor base was not feasible without the City's capital funding commitment, given the condition of the Zoo. In the professional judgment of the Budget Analyst, the Zoological Society's inability to raise and expend the additional funds on capital projects to upgrade the Zoo and the two-year delay in Zoo Bond sales are the primary reasons the Zoological Society was unable to achieve its major operating and financial objectives during the first five years of the Management Agreement.

Over the first five years of the Management Agreement, actual operating revenues, including bequests, were \$63,885,195 or \$15,633,805 less than the projected sum of \$79,519,000, which was the five-year operating revenue estimate presented by the Zoological Society when the Zoo Management Agreement was submitted to the Board of Supervisors for approval. Thus, the average annual operating revenue shortfall for the five-year period was \$3,126,761. Actual operating expenditures over the five-year period were \$65,755,637, or \$15,004,259 less than the projected operating expenditure estimate of \$80,759,896. Thus, the average annual operating expenditure shortfall for the five-year period was \$3,000,852.

The retail sales contribution to Zoo revenue generation has been particularly poor. As shown in Table 3.1.3, for the five-year period of FY 1993-94 through FY 1997-98, actual retail sales revenue was \$7,567,200 less than projected. Further, a financial report generated by the Zoological Society entitled "Revised Expected Budget Fiscal Year 1998-99" shows a \$537,428 negative variance for "Retail Operations," which constitutes approximately 81 percent of the entire negative variance amount of \$664,444.

The Zoological Society has significantly increased its long-term debt to cover operating deficits and to provide advanced funding for capital projects. Long-term debt peaked in FY 1996-97 at \$2,428,741.

The revenue shortfalls experienced by the Zoological Society have had a very negative effect on Zoo staff. Many questions to Zoo staff concerning an operational issue have been answered with "that's not in the budget" or with "we don't have funding for that." As Dr. Parrott states in his evaluation beginning at the bottom of

Section 3.1: Financial and Operational Status; Compliance Issues

page 34 of this audit report, “The revenue urgency and sense of vulnerability permeates the organization.”

Zoological Society staff did not obtain required building and other permits for numerous capital projects and alterations at the Zoo. Thus, required plan checks and inspections were not accomplished and the Zoological Society did not pay required fees to the City. Accordingly, the City Attorney advises that if something happens to one of the structures because of the lack of plan checks and inspections, the City could be held liable.

Our review of the “5-Year Plan: 1993-1998” revealed that the Zoological Society has accomplished many of that document’s objectives and goals, including many of the accomplishments cited in the Introduction to this audit report. However, in addition to effectively managing Phase II of the Master Plan, other objectives important to the Zoo’s success, such as improving internal communications and developing a Board of Directors and that reflects the ethnic diversity of the City, need to be emphasized.

The Zoo has maintained its accreditation with the AZA and its license with the USDA. However, Zoo management has not appropriately addressed the findings resulting from USDA inspections, as covered in Section 1.1 of this audit report.

For FY 1998-99, the Zoological Society did not transmit its audited financial statements to the Recreation and Park Department within 120 days of the end of the Society’s fiscal year (June 30th of each year), as required by Section 15.10 of the Management Agreement.

RECOMMENDATIONS

The Zoological Society should:

- 3.1.1 Thoroughly clean up the Zoo and keep it that way.
- 3.1.2 Construct high quality signage.
- 3.1.3 Increase the number of mammals and birds in the Zoo collection commensurate with being able to care properly for the animals.
- 3.1.4 Beautify empty exhibits with conservation projects, landscaping, or anything else that is attractive and fits the motif of a Zoo whose primary concerns are conservation, education, and quality animal care.
- 3.1.5 Set goals for the Zoo that all of its employees can relate to and feel a part of.

Section 3.1: Financial and Operational Status; Compliance Issues

- 3.1.6 Increase efficiencies by controlling expenses, including using the type of expense schedule shown in Exhibit 3.1.8.
- 3.1.7 Continue working with the Department of Building Inspection to obtain permits on all facilities maintenance projects and capital projects that require permits but that were not obtained prior to performing the work.
- 3.1.8 Emphasize to the Zoo staff that City, state, and federal rules and regulations are to be followed, especially with regard to obtaining building permits.
- 3.1.9 Emphasize to the Zoo staff that USDA inspections are to be responded to in an appropriate manner.
- 3.1.10 Enhance efforts to achieve the objectives and goals set in the 1993 planning document that have not yet been accomplished.
- 3.1.11 In accordance with Section 15.10 of the Management Agreement, deliver to the Recreation and Park Commission for its acceptance an original, signed copy of the Zoological Society's audited annual financial statements by the earlier of 30 days after the completion of the audit or 120 days after the end of the fiscal year covered by the audit.
- 3.1.12 Adopt a more "open door" policy to public inquiries and requests for information.

COSTS/BENEFITS

The recommendations contained in the section will enhance expense control and have the potential to significantly increase Zoo attendance and thus, Zoo revenues. Costs for signage and additional custodial resources would be incurred, but are required to improve the attractiveness of the Zoo and for educational purposes in any case. Our recommendations will not result in any increase in Zoo operating costs for maintenance since the recommended increase in maintenance department staff to address deferred maintenance items should be assigned strictly for the Phase II program approved repair items, thereby qualifying all costs for the force-account labor category in the Phase II program. Additional costs, in excess of currently planned A-1 exhibit costs, may be required to fund first-class A-1 exhibits.

Although there are no direct savings that can be attributed to the objectives and compliance issues covered in this section, by implementing the recommendations contained herein the Zoo will strengthen its organization and avoid any costs which may accompany non-compliance with the Management Agreement or other City, state, or federal rules and regulations.