

METRO

Oregon Zoo

Management of Relationship with Oregon Zoo Foundation Needs Improvement

September 2004

A Report by the Office of the Auditor



METRO

PEOPLE PLACES
OPEN SPACES

Alexis Dow, CPA
Metro Auditor



METRO

OFFICE OF THE AUDITOR

September 20, 2004

To the Metro Council and Metro-area Citizens:

In response to a suggestion by the Metro Council, we assessed the relationship between the Metro-owned Oregon Zoo and the Oregon Zoo Foundation to determine whether financial activities between the two organizations are conducted in an accountable and transparent manner. The Foundation is a not-for-profit organization that exists solely to support the Zoo, primarily by funding Zoo programs.

We found that while the Zoo and Foundation together accomplish many positive things for patrons and the region, Metro's system for controlling the relationship is weak. Problems identified that point to a need for improvements include:

- Revenue from some Zoo activities was improperly sent to the Foundation and returned to the Zoo, which treated it as a donation to avoid paying Metro excise taxes on the revenue.
- The Zoo Director entered into unauthorized contracts that the Foundation paid, subjecting Metro to financial and legal risk.
- Zoo financial records have not properly reflected donations as well as revenues and costs for some projects and activities.
- The Zoo is not receiving adequate compensation for benefits provided to Foundation members.
- Required information is not coming to Metro about the Foundation's financial activities, plans and accomplishments, weakening effective oversight and the ability to make budgetary decisions affecting the Zoo.

Our report makes several recommendations for improving Metro's system of management controls over the relationship. Metro Chief Operating Officer Michael Jordan's response to specific recommendations is at the end of the report. Mr. Jordan agrees with most recommendations; however, we are concerned that he disagrees with our recommendation to take appropriate action to hold the Zoo Director accountable for departures from Metro's contracting requirements. Such action is essential if Metro is to maintain an environment that fosters conscientious management, integrity and accountability.

Mr. Jordan also defers to the Metro Council a decision on our recommendation to renegotiate the agreement with the Foundation. Renegotiating the agreement is the best way to clarify the relationship issues discussed in the report and we encourage the Council to consider taking action on this recommendation.

We appreciate the cooperation and assistance provided by Metro staff during this study.

Very truly yours,

A handwritten signature in cursive script, appearing to read 'Alexis Dow'.

Alexis Dow, CPA
Metro Auditor

Auditor: Jim McMullin, CPA

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Executive Summary

The Oregon Zoo, a Metro agency, is Oregon's most popular paid attraction, with more than 1.2 million visitors each year. Besides funding from Zoo related sales and property taxes, the Zoo also receives funding from the Oregon Zoo Foundation, a tax-exempt, nonprofit organization that is not part of Metro. The Foundation supports a number of Zoo-related projects, and money flows back and forth between the two entities. Metro Councilors asked the Metro Auditor to examine the relationship between the two organizations. Councilors were particularly interested in assuring that the relationship is conducted in an accountable and transparent manner that allows for meaningful oversight by Metro management and the Metro Council.

The results show a need for improvement. While the Zoo and Foundation together accomplish many positive things for patrons and the region, the current system for controlling this relationship is weak. Problems identified include:

- Revenue from some Zoo activities was sent to the Foundation and returned to the Zoo as a donation to avoid paying Metro excise taxes on the revenue
- The Zoo is not receiving adequate compensation for benefits provided to Foundation members.
- The Zoo entered into unauthorized contracts that the Foundation paid, subjecting Metro to financial and legal risk
- Zoo financial records have not properly reflected revenues, costs, and donations for some projects and activities
- Required information is not coming to Metro about the Foundation's financial activities, accomplishments and plans, weakening Metro's ability to make budgetary decisions and perform effective oversight.

Establishing a more manageable and accountable system requires Metro to change how the relationship is conducted. These changes include:

- Making the contractual Agreement between Metro and the Foundation more specific
- Strengthening Metro's control environment to help ensure that employees carry out operations in ways that are consistent with Metro policies
- Recognizing and mitigating risks associated with the current Zoo/Foundation relationship
- Creating a better flow of financial and performance information
- Monitoring the relationship and terms of the contractual Agreement.

Specific recommendations for accomplishing these aims follow.

Recommendations

Strengthening the Contractual Agreement

Metro should renegotiate its contractual Agreement with the Foundation. Objectives of this renegotiation should include:

1. More clearly defining the Foundation's major duties and the expectations associated with them. This could potentially be done by having each duty be the subject of a separate subagreement or Memorandum of Understanding (MOU) setting forth such matters as (1) the nature of the duty and how it relates to the Zoo's mission, (2) the relative roles of the Foundation and Zoo in conducting the duty, (3) the way in which Metro and the Foundation will evaluate how the duty is carried out, and (4) the information needed from the Foundation in order to carry out the evaluation and Metro's other oversight, management and budgetary responsibilities.
2. Defining a payment process to assure that the Zoo is adequately compensated for the value of benefits Foundation members receive from the Zoo.
3. Prescribing how to account for in-kind donations made by the Foundation. The Agreement should provide that, as a general rule, the Foundation should contribute funds to the Zoo from which the Zoo will purchase agreed-upon goods and services. Exceptions to this procedure should be justified and documented and the Zoo should recognize the nature and amount of such contributions on its books.
4. Providing that Metro will charge the Foundation for the cost of services and facilities Metro provides to the Foundation. Doing this will make these expenses transparent and accountable.

Strengthening the Control Environment

The Chief Operating Officer should take appropriate action to hold the Zoo Director accountable for departures from Metro's regulations relating to construction of the condor breeding facility.

Acknowledging and Mitigating Risks

The recommendations we are making for improving the contractual Agreement and Metro's management controls are intended to address the high risks we identified in Metro's relationship with the Foundation. One of these risks, for example, involves the Zoo Director also serving as the Executive Director of the Foundation. There may be other risks that we did not identify that need to be controlled. Accordingly, the Chief Operating Officer, in conjunction with other Metro personnel such as the Chief Financial Officer and Metro Attorney, should review the contractual relationship with the Foundation to assure that all major risks are identified and procedures are in place to mitigate them.

Creating a Better Flow of Information

The Chief Operating Officer should define the information and reports needed by Metro officials to perform their oversight responsibility, and take steps—including specifying the information requirements in the contractual Agreement if necessary—to ensure that the Zoo and the Foundation make this information available. At a minimum, in addition to an audited financial statement, the Foundation should report on its activities, accomplishments, revenues and expenses associated with each major duty defined in the Agreement. This reporting should document the Foundation’s financial contributions to the Zoo and provide a basis for evaluating the Foundation’s performance.

Making Provisions for Monitoring

With regard to the Zoo/Foundation relationship, the Chief Operating Officer should establish appropriate procedures to independently monitor Metro’s contractual relationship with the Foundation and assure that terms of a revised Agreement are complied with. Because the Zoo Director is a party to both sides of the contractual Agreement, the Chief Operating Officer needs to designate someone else as the responsible official for monitoring the terms of the Agreement.

For monitoring activity that affects not only the Zoo/Foundation relationship but also other aspects of Metro operations, two additional steps should be taken:

1. Metro should enhance the role of the Contract Office by giving it the authority and resources needed to:
 - Identify high risks in contracts and assure that appropriate controls are in place to mitigate these risks.
 - Monitor departments to assure they are complying with contracting policies and procedures.
 - Monitor high risk contracts to assure compliance with contract terms and assure that identified risks are being adequately controlled.
 - Establish a performance reporting system to make contract results visible and identify areas needing improvement.

2. Metro should implement the full range of recommendations made in the Metro Auditor report of December 2000, *Contracting: A Framework for Enhancing Contract Management*. That report made detailed recommendations for establishing an appropriate Metro contract management system, including as just stated enhancing the role of the Contract Office. At the time, Metro’s Executive Officer agreed to implement the recommendations, but although progress has been made, more needs to be done. If all the processes recommended in that report were in place, some of the problems identified in this report may have been avoided. The full set of recommendations is included in this report as Appendix C.

Introduction

This review stems from interest expressed by members of the Metro Council in evaluating the operating relationship between the Oregon Zoo and the Oregon Zoo Foundation. The Zoo, a Metro agency, is the most popular paid attraction in the State of Oregon, with more than 1.2 million visitors annually. The Foundation, a tax-exempt, nonprofit organization that is not part of Metro, was established to encourage and aid the development of the Zoo. While only one of these two entities is a Metro agency, both are involved in Zoo-related projects, and money flows back and forth between them. When the Metro Auditor asked the Metro Council to suggest audit topics that Councilors thought would help the Council in its management and oversight efforts, they included the relationship between the Zoo and Foundation as one of the topics. Four Councilors considered it a high priority. Specific interests expressed by Councilors in follow-up discussions included

- The relationship between the Zoo and Foundation in the financing and administration of certain Zoo exhibits, and
- The extent to which the relationship between the Zoo and Foundation is transparent and allows for meaningful oversight by the Metro Council.

We conducted our review to provide information on these and related issues. We focused the review on assessing the extent to which the current relationship between the Zoo and Foundation is managed within a framework of reliable accountability and management controls. Broadly defined, management and accountability controls are systems that help managers and policy makers ensure that an organization's activities are carried out consistently with policy objectives, organizational goals, and established procedures.

Background: The Zoo/Foundation Relationship

Metro and its predecessor, the Portland Metropolitan Service District, has been operating the Zoo since 1971. The Metro Council is responsible for setting policy and providing budgetary oversight of the Zoo, and Metro's Chief Operating Officer is responsible for assuring that the Zoo is managed effectively and in compliance with Metro requirements. The Zoo is administered by a Director, who is a Metro employee. The Zoo Director is accountable to the Chief Operating Officer and is responsible for complying with Metro budgetary, contracting, accounting, and other prescribed policies, procedures and legal requirements. The Zoo has about 160 employees, and its budget for fiscal year 2003-04 was \$26.1 million.

The Oregon Zoo Foundation ("Foundation") has existed for many years and was formerly known as the Friends of the Washington Park Zoo. The Foundation, which has 12 employees, is guided by a Board of Trustees,

including two Metro Councilors who serve as nonvoting members. The Foundation's duties are broadly defined in a written agreement (called here "the Agreement") between Metro and the Foundation. These duties are as follows:

- Raising significant funding for the Zoo
- Recruiting a broad-based membership in the Foundation
- Developing general community support for the Zoo
- Promoting volunteer participation at the Zoo
- Performing such other services to benefit the Zoo as agreed to by the parties.

Since 1997, the Zoo Director has been the administrative head of both the Zoo and the Foundation. In that year, the Zoo/Foundation agreement was amended to provide that the Zoo's Director would also serve as the Foundation's Executive Director. The Zoo Director performs the Executive Director's duties under the direction and control of the Foundation Board of Directors. Metro pays the Zoo Director's salary and benefits and the Zoo Director receives no additional compensation from the Foundation for these duties.

Objectives, Scope, and Methodology

The objectives of this audit were developed after interviewing six Councilors who either considered the Zoo/Foundation relationship a high-priority project or who are or have been members of the Foundation's Board of Trustees. A brief summary of the comments and issues they raised is in Appendix A. As a result of these interviews, the audit focused on issues of accountability and oversight as well as the handling of revenues and expenses in various projects involving the Zoo and the Foundation.

We focused our work on the following main steps:

- Reviewing the Metro Council resolution approving the Agreement between Metro and the Foundation and the associated staff report
- Reviewing the Agreement between Metro and the Foundation to determine whether it contains the elements of a sound contract
- Identifying the major activities the Foundation engages in to support the Zoo
- Obtaining information from Metro through interviews with Metro's Chief Operating Officer, Chief Financial Officer, Contracting Officer, and Finance Department staff
- Obtaining information on Zoo operations through interviews with the Zoo's Director, Finance and Budget Manager, and Construction Manager

- Obtaining information on Foundation activities through interviews with the Executive Director and other Foundation staff, including the Director of Development, Finance Manager, and Membership Manager
- Reviewing numerous documents, including Zoo budgets, Foundation budgets, Foundation audited financial statements for FY 2001 through FY 2003, Metro Attorney files, prior audits and studies relating to the Oregon Zoo, and audit reports from other Zoos that addressed the relationship between the Zoo and the Zoo's non-profit support organization
- Determining the Zoo's procedures for authorizing and awarding contracts for designing and building a breeding facility for California condors
- Determining the Zoo's and Foundation procedures for accounting for the revenues and expenses related to two exhibits (a simulator ride and a butterfly exhibit called "Wings of Wonder"), as well as obtaining relevant financial data
- Discussing the legal implications of our findings with the Metro Attorney

To provide an objective set of criteria for assessing the degree to which the current Agreement and relationship is effectively managed and allows the Council to exercise its oversight responsibilities, we used the following:

- Management control standards developed for the Committee of Sponsoring Organizations (COSO) of the Treadway Commission¹ in 1994. A COSO report titled *Internal Control – Integrated Framework*² establishes a definitive framework against which public and private organizations can assess and improve their internal control systems. The framework developed by COSO consists of five interrelated components, as shown in Table 1. We have used this framework in assessing management and accountability controls in other Metro departments and operations, and Metro's Internal Control Policy is modeled on this framework³
- Metro contract policies and excise tax requirements contained in Metro Code Chapters 2.04 and 7.01, respectively
- Metro's Code of Ethics contained in Executive Order No. 66 effective January 21, 1997

¹ COSO concepts have been incorporated into professional standards in the United States, including the Government Audit Standards issued by the United States Government Accountability Office (GAO) that the Metro Auditor is required to abide by. The Sarbanes-Oxley Act requires publicly traded companies to have a COSO-like control framework in place.

² Internal Control – Integrated Framework Executive Summary can be viewed at:
http://www.coso.org/Publications/executive_summary_integrated_framework.htm

³ Metro's internal control policy is the subject of Executive Order No. 85, effective April 9, 2004.

- Standards and criteria contained in the Metro Auditor December 2000 report entitled “Contracting: A Framework for Enhancing Contract Management”. This report deals with the need for Metro to establish a comprehensive contract management system and outlines the elements of such a system. The report makes several detailed recommendations for improving Metro’s contracting system. Where appropriate, we refer to these recommendations in this report

Table 1
Components of Management Control in the COSO Framework

Component	Explanation
Control environment	Includes integrity, ethical values and competence; attention and direction provided by the policy makers; and management's philosophy and operating style
Risk assessment	Identifies and analyzes relevant risks to achievement of the organization's objectives, forming a basis for determining how the risks should be managed
Control activities	Comprises the policies and procedures that help ensure management directives are carried out
Information and communication	Information must be identified, captured and communicated in a form and timeframe that enable people to carry out their responsibilities. Effective communication also must occur in a broader sense, flowing down, across and up the organization
Monitoring	Assesses the quality of the system's performance over time, through ongoing management and supervisory oversight activities and other evaluations.

Our audit was conducted in accordance with generally accepted government auditing standards. These standards required that we review internal controls and report significant deficiencies that are relevant to audit objectives. As noted above, we used the COSO internal control framework as criteria in evaluating the relationship between Metro and the Foundation. Significant deficiencies found during the course of the audit are described in the report.

Problems Indicate Better Management Control Needed Over Zoo/Foundation Relationship

Metro and the Council currently do not have an adequate framework for overseeing and managing the relationship between the Zoo and the Foundation. Such a framework, often referred to as management controls, is important for providing the Metro Council and management a clear understanding of how monies are being spent and whether activities are being carried out consistently with prescribed policies and procedures.

The Metro/Foundation Agreement provides that the Zoo Director will also serve as the Executive Director of the Foundation. This arrangement, while apparently making it easier for the two organizations to work together, presents risks for Metro in that a Zoo Director is in a position to use the Foundation and its resources to avoid Metro requirements. Such risks are not recognized in the Agreement and Metro does not have controls in place to identify and manage them.

We identified several instances in which the current relationship between the Zoo and the Foundation has been managed inconsistently with Metro's best interests and lessened the Council's and Metro management's ability to monitor operations and exercise decision making authority. In several cases, the seriousness of these issues has already led Metro management to take corrective action. These instances relate to three primary areas, as shown in Figure 1: visibility and control over revenues, contracting practices, and information flow. Each area and example cited is discussed more fully below.

Figure 1
Overview of Problem Areas Identified

Problem Areas	Examples
<div style="border: 1px solid black; padding: 5px; width: fit-content;"> Visibility and control over revenues </div>	<ul style="list-style-type: none"> • Zoo revenue was improperly shifted to the Foundation for two separate revenue-generating activities. • The Zoo is not adequately compensated for benefits provided to Foundation members.
<div style="border: 1px solid black; padding: 5px; width: fit-content;"> Contracting practices </div>	<ul style="list-style-type: none"> • The Foundation paid for contracts that did not comply with Metro requirements resulting in liability, accounting and oversight issues.
<div style="border: 1px solid black; padding: 5px; width: fit-content;"> Information flow </div>	<ul style="list-style-type: none"> • The Agreement requires the Foundation to submit a proposed budget and an annual report. Neither has been submitted. • The Zoo's accounting records do not reflect the value of direct purchases or payments made by the Foundation. • The Zoo is not accounting for the cost of services and facilities provided to the Foundation.

Zoo Revenue Improperly Shifted to the Foundation

For two separate Zoo revenue-generating activities, the relationship between the Zoo and Foundation was used to shift Zoo revenues and expenses to the Foundation. This shifting of revenues had two main negative effects: Excise taxes were not properly collected on the revenue, and the Metro Council and other stakeholders received an incorrect view of Zoo revenues and expenses. Since these incidents were brought to Metro management's attention, accounting adjustments have been made and more than \$56,000 of excise taxes has been retroactively collected.

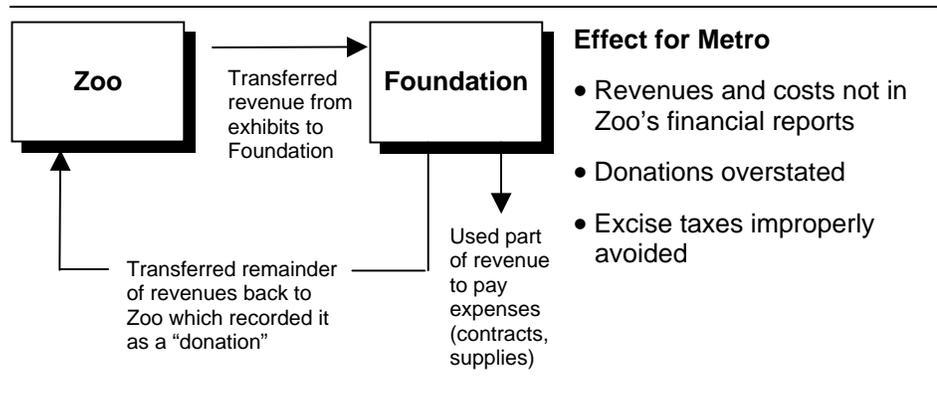
The two revenue-generating activities were:

- A butterfly exhibit, called "Winged Wonders" which was held during April-September 2002 and April-September 2003. Metro built and operated the exhibit, and Zoo (that is Metro) employees sold the tickets for it.
- A thrill ride, known as a simulator, which began operation in May 2003 and is still operating.⁴ Metro leased the simulator and was responsible for the lease payments, and Zoo employees sold the tickets for it.

⁴ The original lease agreement would have ended April 30, 2004, but was extended with modifications to April 30, 2006.

Although the Foundation had no role in any of the activities related to these two activities, revenues from ticket sales were channeled through the Foundation. The treatment of revenues and expenses for accounting purposes worked as shown in Figure 2. Instead of recognizing ticket sales as Zoo revenue on which Metro excise taxes must be paid, the Zoo’s accountant treated the sales as though they were Foundation revenue. Accordingly, Metro’s accounts payable staff sent a check to the Foundation for the amount of revenues collected each month. From these revenues, the Foundation paid invoices for butterfly “livestock” and made \$197,600 in payments on the simulator lease entered into by Metro. The Foundation then returned nearly all of the revenue, net of these expenses, to the Zoo where it was treated as a “donation” exempt from excise taxes.

Figure 2
Overview of Revenue Shift and Its Impact on Metro



This accounting treatment of revenues and expenses produced inaccurate Zoo financial statements. Because these revenues and associated expenses were not shown on the Zoo’s books, over the three-year period involved Zoo revenues were understated by \$809,681 and Zoo expenses were understated by \$250,257. Donations, which did show on the Zoo’s books, were overstated by \$469,159. The excise taxes owing and finally collected on this revenue amounted to \$56,489.⁵

The Zoo Director provided a rationale for these actions, but the rationale is not sound. The Director said he did not want to use taxpayer money to pay for unproven sources of revenue like the simulator ride and butterfly exhibit. If losses were incurred, the Foundation would bear the loss. As for the collection of excise taxes, he said Metro was not entitled to excise taxes on the revenue because it does not collect excise taxes on donations. Our concerns about this rationale are as follows:

⁵ This calculation assumes that Metro’s 7.5 % excise tax is collected from the \$809,681 in revenue, as Metro Excise Tax Code, Section 7.01.025, provides that the tax is included in the charge.

- This clearly was Zoo revenue. The revenue stemmed solely from Zoo activities and the Foundation had nothing to do with it other than to act as a conduit for the money. The Foundation, in fact, accounted for these monies as “Funds Held for Others.” In addition, given that the revenue was the Zoo’s, excise taxes were clearly due on it.
- The responsibility for paying the simulator lease was also clearly Metro’s. The lease agreement was properly authorized and signed by Metro officials, committing Metro to make the lease payments. Having the Foundation make the payments in case losses were incurred is inconsistent with the Zoo’s public responsibility to properly account for and report the results of all activities the Zoo engages in and produces a misleading financial picture of the Zoo’s financial performance.

In November 2003, prior to our audit, the Metro Attorney advised the Zoo Director and the Chief Financial Officer that (1) the revenue from both exhibits should not be sent to the Foundation and (2) excise taxes must be paid on the revenue. During our fieldwork in February 2004, however, we found that revenues from the simulator were still being sent to the Foundation and that no excise tax had been collected on either the butterfly exhibit or simulator revenue. The Zoo’s Assistant Director told us that they did not plan to pay excise taxes on the revenues until the next fiscal year beginning July 1, 2004.

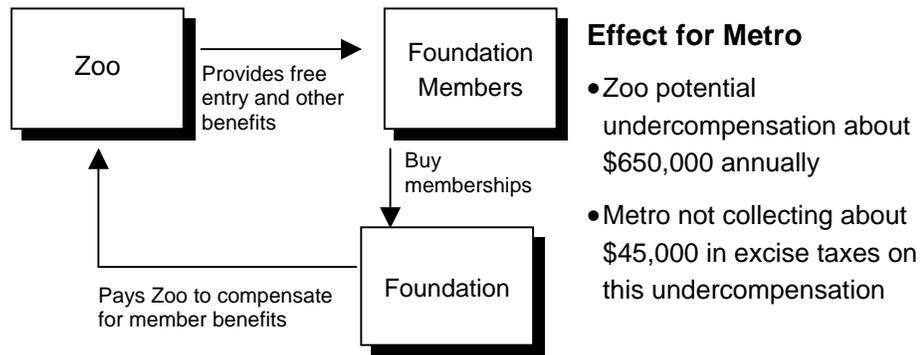
We discussed this matter with Metro’s Chief Operating Officer, Chief Financial Officer, and Attorney. In May 2004 excise taxes of \$56,489 were retroactively collected and accounting adjustments were made to correct the understated revenues and expenses and overstated donations on Metro’s books.

Zoo Not Adequately Compensated For Benefits Provided To Foundation Members

The Zoo is not being adequately compensated for the value of benefits the Zoo provides to Foundation members. Under the Agreement, the Foundation conducts a membership program to raise funds and the Zoo allows these members free entry to the Zoo and provides them other benefits. To compensate the Zoo, the Foundation pays the Zoo an agreed-upon amount per membership. We found that the basis for this payment is not well founded, resulting in the Zoo’s being undercompensated by about \$650,000 annually. This money is now retained by the Foundation and is potentially available to fund Zoo activities, but at the discretion of the Foundation.⁶ Accordingly, the Metro Council does not have direct oversight and budgetary control of the money, and because the money is considered a donation when the Zoo receives it, Metro is not collecting about \$45,000 annually in excise taxes from it. The compensation process and its impact on Metro are illustrated in Figure 3.

⁶ As Executive Director of the Foundation, the Zoo Director influences the timing and amount of money made available to the Zoo.

Figure 3
Overview of Compensation Process and Its Impact on Metro



Foundation members are potentially doing two things when they buy a membership: purchasing certain Zoo benefits (such as admission to the Zoo) and making a donation that is over and above the value of benefits received. Because Foundation members would otherwise have to purchase the benefits they receive from the Zoo, the Zoo should be compensated an amount that covers the market value of these benefits.

The Foundation’s membership structure provides a means for estimating the amount of compensation involved. The Foundation has three categories of membership. The first category, called Membership Dues, consists of basic memberships ranging from \$39 (for an individual) to \$84 (for a family membership). According to the Foundation, people buy these basic memberships to receive the benefits provided by the Zoo. The remaining two dues categories, called Donor Club Dues and Conservation Circle Dues, begin at \$125 and \$1,000 respectively, and people who buy these memberships are clearly making a donation to the Foundation in addition to receiving the value of benefits provided by the Zoo. Thus, the revenue from the Membership Dues category represents a reasonable value of the benefits the Zoo provides to Foundation members and the amount of compensation the Zoo should receive.⁷

The Zoo, however, is receiving only about half of the Foundation’s revenues from these basic memberships, even after the Foundation’s administrative costs are taken into account. In FY 2003 the Foundation received \$1,963,000 from the basic memberships. That same year, the Foundation’s reported costs for administering the entire membership program totaled \$672,200. After subtracting these administrative costs,⁸ the Foundation’s net revenue from

⁷ To assure that our estimate is conservative, we assumed that Metro would not be compensated for the value of Zoo benefits provided to members with higher level memberships. In FY 2003, these higher-level memberships totaled \$547,000.

⁸ To further ensure that our estimate is conservative, we assumed that Metro would cover all of the Foundation’s costs of administering the program.

basic memberships totaled \$1,290,800. The Zoo was compensated only half this amount or \$645,100 in FY 2003 under the current payment formula.

For the Zoo to receive this greater amount of compensation is reasonable considering that the Zoo could receive this revenue directly by selling its own memberships.⁹ Persons buying memberships in the Foundation would buy them directly from the Zoo because they are buying the membership to obtain the benefits offered by the Zoo. Many Foundation members likely believe that they are already buying their membership from the Zoo because Zoo employees are already selling about one-third of the Foundation's memberships from the Zoo office located next to the main gate and membership materials have the appearance that the Zoo is selling the memberships.¹⁰

The low payment the Zoo receives relative to the value of benefits provided is a result of the agreed upon payment formula. For each membership, the Foundation currently pays the Zoo an amount equal to the cost of 2.5 adult admissions. An adult admission is currently \$9, so the Foundation's payment is \$22.50 per membership. We believe this payment formula is inappropriate for several reasons:

- First and foremost, the payment formula does not result in the Zoo being adequately compensated. The compensation the Zoo received in FY 2003 was only half of the amount Foundation members were paying to obtain Zoo benefits.
- Second, the payment formula does not consider the number of persons who can gain free entry to the Zoo. The payment is set at a fixed amount per membership regardless of how many persons use it or how often they use it. Thus, the Foundation pays the Zoo the same amount for an individual membership or for a family membership where two adults, all children under age 18 and an unrelated guest gain free entry.
- Third, the payment formula is apparently not designed to reimburse Metro for the full range of benefits available to Foundation members. The Agreement provides that the payment is to reimburse the Zoo for the cost of membership passes, gift shop discounts, and complementary admissions for members of other Zoos. This provision does not recognize

⁹ The Metro Attorney confirmed that even though Metro has contractually granted the Foundation the right to conduct a membership program, this grant could be revoked and the Zoo could sell its own memberships.

¹⁰ The Foundation's marketing brochures tout "Zoo membership" and the Zoo's website has a webpage entitled "Oregon Zoo Membership." The first sentence on the page reads, "Share our commitment to wildlife preservation by becoming a Zoo member and enjoy exclusive benefits and privileges." Only on the third and last page of the website does it state: "Membership is a program of The Oregon Zoo Foundation." This is followed by the logo of the Oregon Zoo, which includes the phrase "A Service Of Metro."

that the Zoo is providing Foundation members many benefits in addition to these, including (1) free admissions to concerts, the Zoo's Christmas lights display, and member-only events and (2) discounts on camps and classes and Zoo train rides.

There may be several methods of payment that can assure the Zoo is reasonably compensated. One method we identified appears to be worthy of consideration. The Cleveland Zoological Society pays its Zoo 70% of membership dues that are \$100 or less. The 30% of membership dues retained by the Society provides funding for Society expenses. Such an agreement is realistic for Metro and the Foundation. In FY 2003 the Foundation could have paid the Zoo 66% of its basic Membership Dues and the remaining 34% would have covered the Foundation's costs of administering its entire membership program. A copy of the Cleveland Agreement is attached as Appendix C.

**Foundation
Improperly Used
To Pay Contracts
On Condor
Project**

The California condor project reflects the second problem area we identified in the Zoo/Foundation relationship—contracting practices. In keeping with its program to help conserve endangered species, the Zoo was selected to participate in a recovery program to breed California condors prior to their release to the wild. On this project, the Zoo Director circumvented Metro's contracting policies by using the Foundation to pay for contracts that Metro had not authorized. This procedure placed Metro at risk from a liability standpoint, and according to the Metro Attorney, was not appropriate. Besides the liability concerns, this use of the Foundation again resulted in giving the Metro Council and other stakeholders an incorrect view of Zoo revenues and expenses.

From the outset of this project, it was understood that the Foundation would provide the funding for the breeding facility. The facility was included in Metro's Capital Improvement Plan for FY 2003-04, which the Metro Council approved in November 2002. The FY 2003-04 approved budget provided \$2,000,000 for the facility, to be funded by donations from the Foundation.

While the Foundation was to be the funding source, Metro procedures called for Metro to enter into the contracts to build the facility and for the Foundation to raise funds and donate them to the Zoo so that Metro could pay the contractors. The Zoo Director decided not to follow these procedures. Instead, on his own authority, he directed the Zoo's Construction Manager to enter into and sign contracts for the design and construction of the breeding facility, and when the bills came in, he had the Foundation pay them. These actions violated Metro's contracting policies and procedures that, among other things, require the Zoo to:

- Obtain review and approval by Metro's Contract Management Office and Metro Attorney

- Obtain Metro Council authorization for a steel mesh contract that was over \$50,000 (actually \$462,000) and not included in the Metro budget
- Follow required contract solicitation and bidding requirements, including consideration of disadvantaged, minority, and women owned businesses
- Use standard Metro contracts that contain provisions requiring contractors to meet State of Oregon and other contracting requirements

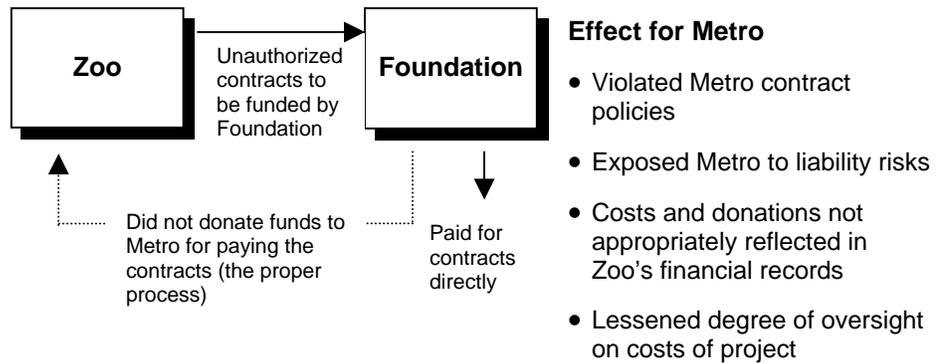
Deviating from Metro policy was a problem in several respects:

- It exposed Metro to liability risk. The breeding facility was located on Metro property and was therefore was subject to all the requirements normally applied to Metro projects. However, the contracts did not contain provisions for such things as performance bonds, compliance with prevailing wages law, and compliance with building codes.¹¹ Metro was also at risk because there was no assurance that the contracts were awarded based on adequate competition, lack of favoritism and low price, as required by State contracting law.
- The Metro Attorney told us that the Foundation is not an appropriate vehicle for constructing an improvement on Metro-owned public property. He said the Zoo Director was not authorized to engage the Foundation to construct the facility on Metro property and the Foundation was not authorized to construct the facility on Metro property. Such improvements should be included in Metro's budget and paid for from Metro funds. In addition, the contracts that were entered into to build the facility were not properly authorized and the Zoo Director did not have the authority to enter into such contracts.
- It lessened the degree of oversight that the Metro Council and management had over the costs of the project. Because the Foundation paid almost all bills related to the project while it was under construction, Metro's books did not show the construction costs until an adjustment was made to the Zoo's capital accounts.

Figure 4 provides an overview of the improper contract practices and their impact on Metro.

¹¹ The Metro Attorney told us that all contractors were paid and prevailing wages were paid to their employees.

Figure 4
Overview of Improper Contract Practice and Its Impact on Metro



The Zoo Director said he knew the contracting approach he was using would violate Metro's contracting requirements, but he took the action for the following reasons:

- After talking with potential donors, he said it became clear that the Foundation would have difficulty soliciting the level of cash contributions needed to build the facility. The Director said that because he believed the Foundation would not be able to raise cash and then transfer the cash to Metro to build the facility, it would be better to obtain as many "in-kind" contributions as possible. This would make it easier for firms like PGE, Hoffman Construction and Weyerhaeuser to make donations without having to give cash and would make it easier for the Foundation to raise the level of cash needed to complete the facility.
- The Director said the approach of soliciting in-kind donations resulted in the project costing less to build than if Metro's contracting procedures had been followed. He said the bigger contractors were willing to donate time and materials, but not willing to go through the hassle of bidding on the project. He also said that nothing in the Agreement states that the Foundation can only donate cash in support of the Zoo.

The Zoo Director apparently did not try to find a way to achieve his objective of getting in-kind donations while still complying with Metro's contracting requirements. The current Contracting Officer told us that in his professional judgment a method could have been devised to both allow in-kind donations and still meet the letter and spirit of the Metro's contracting requirements.

Metro has taken steps to address the problems that arose from the Zoo Director's activities. Metro's Chief Operating Officer and the Foundation entered into an after-the-fact agreement that documents the role the Foundation played in paying contractors for what is termed Phase 1 of the project. The agreement provides that the Foundation will not pay contractors under Phase 2 of the project, but instead will donate money to the Zoo from which payments will be made. The Zoo has also taken steps to address and

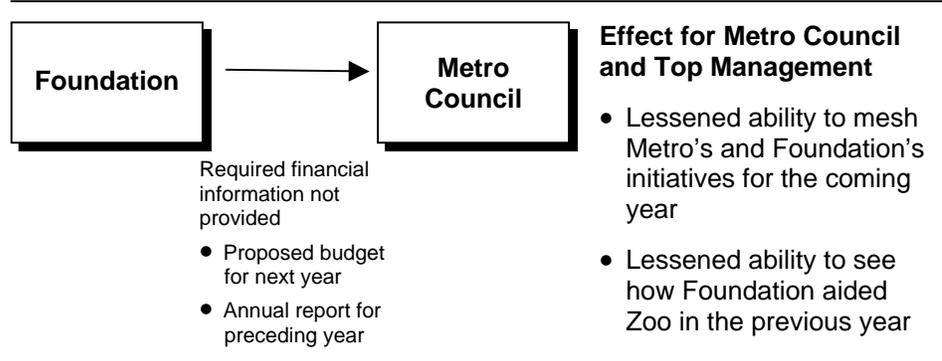
remedy accounting issues associated with the project. In March 2004 the Zoo's Finance Manager recognized the breeding facility as a Zoo asset by capitalizing the Foundation's \$929,000 in payments and in-kind donations in the Zoo's Capital Fund and showing this as a donation.

Metro Council Not Receiving Required Information

The Metro Council and Chief Operating Officer need relevant and accurate information to effectively perform their oversight and management responsibilities in relation to the Zoo and Metro's contract with the Foundation. The current agreement between Metro and the Foundation requires the Foundation to supply certain information, but this information is not being generated—or if it is generated, it is not being distributed to those who need it for oversight purposes. Figure 5 provides an overview of the required information that has not been provided and its impact on Metro.

- **Budget information not provided.** The Agreement requires the Foundation, in consultation with the Zoo Director, to adopt and publish an annual operating budget and to send its proposed budget to Metro so that Metro may consider the proposed budget in conjunction with Metro's budget for the Zoo. The Agreement does not state who in Metro is to receive the information, but the staff report accompanying the Metro Council resolution approving the Agreement states that it should go to the Metro Council. This information has not been provided to the Metro Council or to the Chief Operating Officer. Such information would better help the Council and the Chief Operating Officer determine how much funding they can expect each year from the Foundation in support of the Zoo.
- **Annual report not prepared.** The Agreement also requires the Foundation, in consultation with the Zoo Director, to adopt and publish an annual report, including an audited financial statement. The Agreement does not define what this report should contain, other than the financial statement, but even so the Foundation is not preparing any kind of an annual report. The kind of information often included in an annual report—such as information about the Foundation's performance and its major initiatives—could help the Metro Council make funding and policy decisions regarding the Zoo.

**Figure 5
Overview of Required Information Not Provided and Its Impact on Metro**



**Council Lacks
Other Relevant
Information**

While the problem above relates to information the Foundation is required to provide, we identified other unmet information needs that lie outside the current requirements. The Zoo’s books have not been recognizing and accounting for two types of information that are important from a public accountability standpoint:

- **Information about in-kind payments.** While direct monetary contributions from the Foundation to the Zoo show up on the Zoo’s books, direct purchases and payments made by the Foundation do not. As discussed above, the Foundation improperly paid for a Zoo simulator lease and for contracts on the condor project that required Metro to make after the fact adjustments to the Zoo’s books to recognize the payments. In addition, the Zoo Director told us that the Foundation routinely purchases medical equipment, veterinary supplies and other things that do not show on the Zoo’s books. We discussed this matter with Metro’s Chief Operating Officer, who agreed that such purchases should be accounted for on the Zoo’s books.
- **Information about cost of services and facilities provided to the Foundation.** The Zoo is generally not accounting for the cost of services and facilities it provides to the Foundation free of charge. Under terms of the Agreement, Metro agreed to provide Zoo space for Foundation meetings, staff offices, a membership booth, and other space as agreed. It also agreed to assist the Foundation in performing such duties as assisting with membership drives, newsletters, and annual reports. We did not attempt to identify all the types and costs of services and support that the Zoo and other Metro units provide to the Foundation, but we did note that overall Metro is providing more than token support and that some of the services are not obvious from the Agreement. For example, Zoo staff sell about one-third of all Foundation memberships from an office next to the main gates - for FY 2002-03, these sales amounted to \$837,000 of the Foundation’s \$2,510,000 of membership revenue. In addition, Metro’s Information Technology department assisted the

Foundation for almost a week to install a new computer system, and Metro administers the Foundation's employee benefits program.¹² Information on the nature and cost of such services is essential for the Metro Council to assure that the relationship is administered in a transparent and accountable manner.

¹² Conversely, we noted that the Foundation charges the Zoo's Education Division \$20,000 annually for program listings in the Foundation's newsletter.

Improving Management Control Requires Actions In Several Areas

The problems described above demonstrate a need to make systemic changes to the arrangement between Metro and the Foundation. While a number of problems have been corrected or are currently being addressed, the current set of management controls is not sufficient to prevent similar problems from recurring in the future. We evaluated the current set of management controls using two sets of criteria described earlier in our methodology—the COSO internal control framework and the contract management standards we developed from previous work. This evaluation pointed to a need for improvements in the following areas:

- The contractual Agreement needs to be revised to establish a basis for accountability, including defining expected performance and producing information needed for oversight and accountability
- Metro’s control environment needs to be strengthened to help ensure employees carry out operations in ways that are consistent with Metro policies
- Risks in the relationship need to be acknowledged and controlled
- Better financial and performance information needs to be generated and reported to the Metro Council and other stakeholders to enable them to carry out their oversight and budgetary decision making responsibilities
- Terms of the contract and the relationship need to be monitored

Agreement Needs To Be Revised and Strengthened

The contractual agreement between Metro and the Foundation is the key document for defining the relationship and providing the basis for managing it in the best interests of Metro and the public. The Agreement, however, does not establish a basis for accountability because it does not contain:

- Clear statements of services and activities expected from the Foundation
- Clearly defined performance standards and measurable outcomes
- Clear statements of how the Foundation’s performance will be evaluated and reported¹³

The Agreement states the Foundation’s basic duties in very general terms: raise significant funding, recruit a broad-based Foundation membership, develop general community support for the Zoo, promote volunteer participation, and perform such other services as agreed to by the parties. This is the only statement and description of duties.

¹³ Metro Auditor report entitled “Contracting: A Framework for Enhancing Contract Management,” December 2000, page 18.

Table 2 lists these duties and shows whether the Agreement covers some basic elements that, from a management control standpoint, should be defined to provide a basis of accountability for the duty. These elements include such things as clearly describing the nature of the duty, defining the roles of the parties in relation to each duty, and specifying the information needed to ascertain that the roles are being carried out. As the table shows, this level of specificity is largely absent. The only category in which the Agreement contains provisions is for reporting requirements. And even for this category, as pointed out earlier, the requirements for an annual report are not clearly defined and required reports have not been submitted as required.

**Table 2
Summary of Accountability Provisions In Contractual Agreement**

Duty	Nature of the duty defined?	Basis for evaluating performance?	Financial transaction procedures specified?	Roles and responsibilities of staff specified?	Monitoring or evaluation approach established?	Reporting requirements specified?
Fundraising	No	No	No	No	No	Not for this duty
Membership Program	No	No	Yes ¹⁴	No	No	Not for this duty
Community Support	No	No	No	No	No	Not for this duty
Volunteer Promotion	No	No	No	No	No	Not for this duty
Other Services ¹⁵	No	No	No	No	No	Not for this duty

Another deficiency of the Agreement is that it does not recognize that the relationship between the Zoo and the Foundation differs for each Foundation duty. For example, respective Zoo and Foundation staff roles and responsibilities are very different in relation to fundraising and volunteer promotion activities. To provide a basis for transparency and accountability, these differing roles and responsibilities, as well as such things as the treatment of revenues and expenses, should be recognized and defined.

One way to accomplish this greater specificity is by providing in the Agreement for each major duty to be the subject of a separate sub-agreement or “Memorandum of Understanding (MOU)” that is an attachment to the basic Agreement. These MOU’s would establish the basis for making clear and transparent the roles and responsibilities of Zoo and Foundation staffs, how performance will be evaluated and reported, how revenues and expenses will be accounted for and how Metro will monitor terms of the Agreement. Our specific recommendations for what the MOU’s should address are in the Contractual Agreement subsection of the Recommendations section of this report.

¹⁴ Provides for a payment to Metro to cover certain costs. The adequacy of this payment is discussed in the report section entitled “Zoo Not Adequately Compensated for Benefits Provided to Foundation Members.”

¹⁵ For example, acquiring grants.

Defining these matters in the Agreement does not necessarily correlate with having a successful relationship. However, specificity is essential for Metro to have a sound basis for public accountability and to assure that Metro interests are protected.

While the Agreement is not specific about the Foundation's duties, it is specific about the purpose of the payment that the Zoo is to receive from the Foundation's membership program. The Agreement provides that the payment is to reimburse the Zoo for the cost of membership passes, gift shop discounts, and complimentary admissions for members of other Zoos. This provision does not recognize that the Zoo is providing Foundation members many benefits in addition to these, so to make the payment more fully representative of the value of benefits provided, this part of the Agreement would need to be changed.

**Control
Environment
Needs To Be
Strengthened**

A central component of an internal control system is what is called the "control environment." This component refers to the need for management and employees to establish and maintain an environment throughout the organization that sets a positive and supportive attitude toward internal control and conscientious management. Elements of a strong control environment involve such matters as:

- Using a formal code of conduct and other policies to address acceptable operational practices and conflicts of interest, and
- Taking appropriate disciplinary action in response to departures from approved policies and procedures.

Metro does have a code of conduct and policies and procedures to address acceptable operational practices, but the problems described earlier in the report relating to the contracting of the condor project demonstrate they were not followed. As a Metro official and head of a department, the Director of the Zoo is responsible for being knowledgeable of and complying with the public laws, policies and procedures that govern his activities. However, the Zoo Director's conduct in knowingly ignoring Metro contracting requirements on the condor project is clearly improper and inconsistent with Metro's Code of Ethics, as shown in Table 3.

**Table 3
Comparison of Zoo Director Conduct to Metro Ethics Code**

Ethics Code Provision	Zoo Director’s Conduct
Metro officials must obey both the letter and the spirit of all laws and regulations	Knowingly ignored Metro contracting regulations in constructing the condor project
Metro officials should be careful to act only within the authority for decision making they have	Exceeded authority by directing the Zoo’s Construction Manager to enter into and sign contracts for building the condor facility
Metro Administrators must implement policies in good faith regardless of their personal views	Knowingly ignored Metro’s contracting regulations on the condor project because in his personal view following them would make it difficult to raise enough cash to fund the condor breeding facility

According to the Metro Attorney, there is no mechanism of legal enforcement against a public employee who does not follow Metro’s contracting and other requirements where the employee does not have a personal financial involvement. The Metro Attorney said there is a management mechanism to deal with employees who do not comply with Metro policy and procedures. This mechanism is subject to the discretion of the Chief Operating Officer and could involve disciplinary actions.

The Chief Operating Officer reported to us that he has met with all of the employees involved in the problems disclosed in this report and as a result new procedures for contracting and excise tax collection were implemented. However, a fundamental element of any control system is individual accountability, which makes it important that appropriate disciplinary action be taken in response to departure from approved regulations, policies and procedures. Such action is essential to establish and maintain an environment throughout the organization that sets a positive and supportive attitude toward internal control and conscientious management.

Risks Need to be Acknowledged and Controlled

Assessing and controlling risks is another important part of a management control system. It involves identifying any factors that can negatively impact Metro or the operation of the agreement and taking steps to minimize their occurrence. In our view, the key risks are clear:

- The Zoo Director serves both as the head of the Zoo and the head of the Foundation. This dual status leaves operations open to manipulation.
- The Foundation can be used as a conduit to avoid payment of Metro excise taxes from Zoo revenue sources.
- The Zoo may not receive adequate compensation for the benefits Foundation members receive from the Zoo.
- The Foundation can be used as a way to purchase things without the Metro Council’s awareness and ability to exercise oversight.

This is not to say that such risks should be eliminated by changing the relationships; the important thing from a management controls standpoint is to identify risks and take steps to mitigate them. In the case of the Zoo Director's heading up both organizations, for example, this step was taken to address other problems and issues that had arisen in the Zoo/Foundation relationship in years past. Risk management is a central part of a management controls system principally because nearly every enterprise involves some element of risk. Mitigating these risks is what matters.

The types of problems that we found are indications that key risks are not being controlled. Establishing appropriate controls can protect both Metro and the Foundation from questionable activities and provides guidance for the key individuals who carry out executive responsibilities. Clearly identifying risks and describing what steps should be taken to avoid overstepping responsibilities or operating outside acceptable parameters would provide all parties with a clearer roadmap of how to proceed.

**Better Information
Is Needed For
Oversight and
Decision-Making**

Good information flow is essential for a well-functioning management control system. Without adequate and accurate data, managers have greater difficulty making informed decisions and learning what their policies and directives are accomplishing. The problems discussed above illustrate that this aspect of Metro's control system is deficient, because several of the problems center on information that is not being supplied. The Metro Council and Chief Operating Officer would be in a better position to provide oversight and evaluate the Zoo's direction and needs if they received the budgetary and annual report information that is required under the Agreement and if Metro and the Zoo accounted for and disclosed the support Metro provides to the Foundation and the types of in-kind purchases the Foundation makes for the Zoo.

**Monitoring is
Needed to Ensure
Compliance**

Metro is not monitoring the contractual Agreement with the Foundation. Monitoring is needed to assure that terms of the Agreement are complied with and to provide management control over the risks inherent in the Zoo Director also serving as the Foundation's Executive Director. These risks include the Zoo Director being in a position to use the Foundation to conduct activities that are outside of Metro's oversight and inconsistent with Metro and public accountability requirements.

Effective contractor monitoring begins before the contract is awarded by establishing clear, concise statements of expected performance in the contract to the extent possible. Such statements provide the basis for evaluating performance and assuring that the contractual relationship is conducted appropriately. By strengthening the Agreement between Metro and the Foundation, Metro will have the contractual basis for monitoring the relationship.

Metro also has to properly assign responsibilities for monitoring contracts. Under Metro's decentralized approach to monitoring contracts, department directors are responsible for assuring that contracts in their departments are monitored. In relation to the contract with the Foundation, however, the Zoo Director has a conflict - he is a principal player on both sides of the Agreement and he is the monitor in charge of overseeing whether Metro's interests are fully represented. This arrangement has resulted in Metro not having an independent and effective monitor of the Agreement and the relationship. From our discussions with the Zoo Director, it is clear that he is not monitoring the terms of the Agreement. For example, he said he did not know that the Foundation is required to prepare an annual report or that the Foundation's proposed annual budget is required to be sent to the Metro Council in conjunction with the Council's consideration of the Zoo's budget.

To resolve this deficiency in the accountability framework, Metro's Chief Operating Officer should establish a process to assure that the contractual relationship with the Foundation is independently monitored. In addition, the problems found in this review provide a clear demonstration of why Metro should implement the recommendations we made in a December 2000 report, "Contracting: A Framework for Enhancing Contract Management." One recommendation in that report was for Metro to give the Contract Office the authority and resources needed to provide effective oversight of departmental contracting activities. At the time, Metro's Executive Officer agreed to implement the recommendation, but progress has been limited. If such oversight were in place, some of the problems identified in this report may have been avoided. We recognize that this recommendation may require some modification to Metro's decentralized management culture, but we believe these changes are needed for Metro to provide effective and accountable oversight of departmental contracting activities.

Appendix A

Metro Councilor Interests and Concerns

Appendix A Metro Councilor Interests And Concerns

The Metro Council suggested that the Metro Auditor audit the relationship between the Oregon Zoo and the Oregon Zoo Foundation. To determine whether there were specific concerns driving the Council’s interest in this topic, we interviewed six Councilors who either listed this issue as one of their top concerns or who are or have been members of the Oregon Zoo Foundation’s Board of Trustees. Table 3 describes Councilor interests and concerns about the Zoo/Foundation relationship.

**Table 3
Metro Councilor Interests and Concerns About the Zoo/
Foundation Relationship**

<p>Relationship and Accountability</p>	<ul style="list-style-type: none"> • We have a balancing act in relation to the Zoo Foundation. They do very good work and raise money in support of the Zoo. But we also have a fiduciary responsibility to assure that the Metro/Foundation relationship is transparent and operates within acceptable standards. • I believe there are accountability and equity issues that should be addressed in relation to the Zoo and Zoo Foundation. The Auditor’s Office can provide a third party independent assessment of the Zoo/Foundation relationship, identify risks and make suggestions for improvements. • I think there should be clearly defined accountability processes to enable the Council to review the Foundation’s contribution to Metro.
<p>Circumvention of Oversight and Excise Taxes</p>	<ul style="list-style-type: none"> • The fact that the Zoo Director heads both organizations may enable the Director to make money that is off the Metro books. The Metro Council does not review the Foundation budget and no excise tax is paid to Metro from traveling exhibits operated by the Foundation. This gives the Director the ability to retain more money and use it for activities that are not visible to the Council. • The Foundation can potentially be a way to run a shadow business or off the books operation. This doesn’t trouble me if we are assured that the Foundation is pursuing the same goals as Metro and if it doesn’t inappropriately affect the revenues Metro is entitled to, such as the excise tax. I don’t know if we have these assurances. The Foundation’s sale of memberships and operations conducted on Metro Zoo property may not result in our getting the excise tax we are entitled to. And the structure of the relationship may be such that the incentives and alignments may not match Metro’s mission.

	<ul style="list-style-type: none">• Of particular concern to me is that admission fees for the Butterfly exhibit, simulator rides and even memberships are not being subjected to excise tax.• If there is a case to be made for not paying excise taxes, the Council should be given the opportunity to exempt the activity from tax.
Financial	<ul style="list-style-type: none">• The question is what distinguishes Zoo revenues from Foundation revenues? Revenue derived from some exhibits and the simulator goes to the Foundation, but I'm not sure why this is the case. It would seem like revenue from such operations should go to the Zoo, just as the Zoo train revenue does. These fee-for-service activities appear to be clearly distinguishable from charitable donations that rightly belong to the Foundation.

Appendix B

Cleveland Parks Zoo Agreement on Membership Revenue

Appendix B Cleveland Parks Zoo Agreement On Membership Revenue

AGREEMENT

This Agreement is made and entered into this 25th day of September, 1997, by and between the Board of Park Commissioners of the Cleveland Metropolitan Park District, a political subdivision of the State of Ohio ("Cleveland Metroparks") and the Cleveland Zoological Society, an Ohio not-for-profit corporation (the "Society"), collectively the "Parties."

Cleveland Metroparks owns, operates and administers the Cleveland Metroparks Zoo (the "Zoo"). The Society has as its principal purpose support of the Zoo. The Parties believe it is in their respective best interests for the Society to build and sustain a large membership. They further believe that to accomplish this goal, it is beneficial to provide admission to the Zoo without charge as a Society membership benefit. However, this benefit represents a significant loss of admissions revenue to Cleveland Metroparks.

Now, therefore, the Parties do agree as follows:

1. *Free Admission and Effective Date.* Effective January 1, 1998, Society members bearing valid credentials shall receive unlimited free admission to all permanent aspects of the Zoo including The RainForest.

2. *Consideration.* As consideration for the free admission privilege extended to Society members, and to help defray gate revenue lost, within thirty (30) days of each semiannual anniversary of the effective date of this Agreement, Society will pay to Cleveland Metroparks an amount equal to a share of all dues received during the preceding six (6) months from each class of Society membership the dues of which are One Hundred (100) Dollars or less. To the extent that the cost of a Society Sustaining Membership is

increased above its current One Hundred (100) Dollars, the ceiling on dues sharing shall increase by a like amount.

The following schedule sets forth Cleveland Metroparks percentage share of dues during each year of the term hereof and for renewal terms, provided however, in no event shall the share retained by the Society be less than \$450,000 per annum, except, however, should the aggregate of annual dues fall below \$900,000 in any year, each party's percentage for that year shall be 50%:

<u>Year</u>	<u>Cleveland Metroparks' Share (%)</u>
First	55
Second	57
Third	60
Fourth	65
Thereafter	70

Failure of the Society to pay the above consideration when due and within thirty (30) days after written notice of failure to do so shall entitle Cleveland Metroparks to terminate this Agreement, provided, however, that all current Society members at the time of such termination will retain their admission privileges until their respective memberships expire, and provided, further, that such termination shall not constitute a defense against payment of all sums owing from the Society to Cleveland Metroparks.

3. *Term.* This Agreement may be terminated at the end of any contract term by written notice from one party to the other party. This Agreement shall have an initial contract term of seven (7) years from its effective date. Unless either party shall give to the other a written notice of termination prior to the end of the sixth year of the initial contract term, the initial contract term shall be extended automatically for one additional (1) year. Thereafter, unless written notice shall be given by either party prior to

the end of any year, the then remaining one year contract term shall automatically be extended for one additional year.

4. *Other Society Support.* From time to time during the term of this Agreement, Society shall undertake to raise project-specific funds on behalf of the Zoo. In addition, the Society shall seek to continue its long-standing practice of supporting from its unrestricted income both operating and capital needs of the Zoo.

5. *Periodic Review.* Without the necessity of electing to allow this Agreement to expire, upon written notice the Parties agree to consider, in good faith, modification of the Agreement based upon material changes in the basic assumptions which lead to it.

6. *Record Keeping.* For the benefit of the Parties, Cleveland Metroparks will maintain complete and accurate records of free admissions by Society members, which records will be available to the Society for review on reasonable request during normal business hours. Similarly, Society shall maintain complete and accurate membership records which shall be available to Cleveland Metroparks.

7. *Notice.* Notice required pursuant to this Agreement shall be deemed given appropriately if mailed certified first class, return receipt request, to the address below listed:

Cleveland Metroparks
Administrative Offices
4101 Fulton Parkway
Cleveland, Ohio 44144
Attention: Executive Director

Cleveland Zoological Society
3900 Wildlife Way
Cleveland, Ohio 44109
Attention: Executive Director

IN WITNESS WHEREOF, the parties have executed this Agreement by their duly authorized representatives, effective as of the day and year first above written.

CLEVELAND METROPARKS

John K. O'Toole 10/1/97
John K. O'Toole, President Date
Board of Park Commissioners of the
Cleveland Metropolitan Park District

CLEVELAND ZOOLOGICAL SOCIETY

Joseph J. Mahovlic 10-3-97
Joseph J. Mahovlic, President Date
Cleveland Zoological Society

Vern Hartenburg 10/1/97
Vern Hartenburg Date
Executive Director-Secretary

Susan D. Marshall 10/2/97
Susan D. Marshall Date
Executive Director

Steve H Taylor 10/1/97
Steve H. Taylor Date
Zoo Director

Appendix C

Audit Recommendations from Metro Auditor Report
“Contracting: A Framework for Enhancing Contract Management”

Appendix C

Audit Recommendations From Metro Auditor Report “Contracting: A Framework For Enhancing Contract Management”

We recommend that Metro take the following specific actions to improve its management of contracts. Doing so will better ensure that contractors produce quality results and public funds are protected from fraud, waste or inefficient use.

1. Define and document the authority, roles and responsibilities of the various organizational units and positions involved in contracting activities, including the Contract Office, departments and project managers. In this regard, Metro should enhance the role of the Contract Office by providing it the resources, authority and responsibility for the following oversight, quality control and support activities.
2. Improve contract oversight by:
 - strengthening the role of the Contract Office in guiding and reviewing departmental contracting activities
 - conducting formal risk assessments to identify contracts requiring close monitoring and audits
 - establishing a management reporting system geared toward providing oversight information to top management and departmental managers.
3. Enhance departmental quality control by:
 - Designating a formal “Contract Coordinator” in each department responsible for assuring that contracts are properly planned and monitored. This would be a professional position with the authority to counsel and direct project managers in developing contracts and evaluating contractor performance.
 - Establishing minimum agency-wide qualifications for project managers and other contracting personnel. Persons would be considered qualified after attending appropriate training programs.
 - Formally evaluating the performance of project managers and other contracting personnel in relation to their contracting duties and responsibilities.

4. Provide better support to project managers and other contracting personnel by developing procedures, guidelines and training in:
 - determining the appropriate contract type
 - establishing scope of work requirements and performance standards
 - monitoring and evaluating contractor performance
 - evaluating contractor proposed prices and contractor billings
 - conducting risk assessments.
5. Capitalize on the depth of experience of some Metro contracting personnel by forming interdepartmental workgroups to develop procedures, guidelines and training programs.
6. Consider using performance-based service contracting methodology on a pilot basis. Federal experience shows that this methodology can reduce overall service contract costs 15 percent while obtaining better results.

Response to the Report

Metro Chief Operating Officer Michael Jordan

Audit: Management of Relationship with Oregon Zoo Foundation Needs Improvement

Date: September 2004

AUDIT RESPONSE

Recommendation 1

Metro should renegotiate their contractual Agreement with the Foundation. Objectives of this renegotiation should include:

1. More clearly defining the Foundation's major duties and the expectations associated with them. This could potentially be done by having each duty be the subject of a separate subagreement or Memorandum of Understanding (MOU) setting forth such matters as (1) the nature of the duty and how it relates to the Zoo's mission, (2) the relative roles of the Foundation and Zoo in conducting the duty, (3) the way in which Metro and the Foundation will evaluate how the duty is carried out, and (4) the information needed from the Foundation in order to carry out the evaluation and Metro's other oversight, management and budgetary responsibilities.
2. Defining a payment process to assure that the Zoo is adequately compensated for the value of benefits Foundation members receive from the Zoo.
3. Prescribing how to account for in-kind donations made by the Foundation. The Agreement should provide that, as a general rule, the Foundation should contribute funds to the Zoo from which the Zoo will purchase agreed-upon goods and services. Exceptions to this procedure should be justified and documented and the Zoo should recognize the nature and amount of such contributions on its books.
4. Providing that Metro will charge the Foundation for the cost of services and facilities Metro provides to the Foundation. Doing this will make these expenses transparent and accountable.

Agree

Yes N/A

No N/A (specify reasons for disagreement)

The contractual agreement between the Metro Council and the Zoo Foundation is the policy articulation of the relationship and thus changes to the agreement are under the purview of the Metro Council. However, the numbered points in the recommendation are generally management practices that are further delineated in the subsequent recommendations and are agreed to by management. Should the Metro Council decide to renegotiate the agreement with the Zoo Foundation then management will adjust its procedures based on that future policy articulation. In the meantime, many of the points in Recommendation 1 have been, or will be, implemented as per Recommendations 2 through 7.

What action will be taken (if any)?

Who will take action?

When will action be accomplished?

Follow-up necessary to correct or prevent reoccurrence.

Audit: Management of Relationship with Oregon Zoo Foundation Needs Improvement

Date: September 2004

AUDIT RESPONSE

Recommendation 2

The Chief Operating Officer should take appropriate action to hold the Zoo Director accountable for departures from Metro's regulations relating to construction of the Condor breeding facility.

Agree

Yes

No (specify reasons for disagreement)

What action will be taken (if any)?

The Chief Operating Officer has met with many of the employees involved from the Zoo, Contracts, and Finance departments including the Zoo Director, Chief Financial Officer, and Contracts Director.

Given-

- the length of time since many of these events occurred, and
- the significant change in organizational structure, and
- the personnel changes in key control positions, and
- that the issues relating to contracting and excise tax collection have been corrected

-it is management's opinion that appropriate actions have been taken to assure that Metro policies and procedures will be followed in the future.

Other than what is stated in the responses to recommendations #3 through #6 of this report, no further actions are necessary.

Who will take action?

Chief Operating Officer

When will action be accomplished?

This action is already accomplished.

Follow-up necessary to correct or prevent reoccurrence.

Implementation of control mechanisms as recommended in Recommendation #3-7 will help to prevent reoccurrence agency-wide.

Audit: Management of Relationship with Oregon Zoo Foundation Needs Improvement

Date: September 2004

AUDIT RESPONSE

Recommendation 3

The Chief Operating Officer, in conjunction with other Metro personnel such as the Chief Financial Officer and Metro Attorney, should review the contractual relationship with the Foundation to assure that all major risks are identified and procedures are in place to mitigate them. One of these risks, for example, involves the Zoo Director also serving as the Executive Director of the Foundation. There may be other risks that we did not identify that need to be controlled.

Agree

Yes

No (specify reasons for disagreement)

What action will be taken (if any)?

Identify potential risks in the contractual relationship with the Foundation and analyze them for potential major exposure.

Potential risks in a contractual relationship (based on Metro contract management practice) are:

- When remuneration exceeds \$250,000
- A claims dispute can arise
- It is an employment contract
- There are environmental impacts
- There are financial risks
- There are operational risks
- The contract is politically sensitive
- Project management is required
- The agency's reputation can be affected
- Standard risk issues (liability, insurance, etc.)

Remuneration exceeds \$250,000: The Foundation collects donations and sells Zoo memberships to help fund the Zoo. The financial reporting listed in the Recommendation 4 response addresses accounting for the financial transactions.

A claims dispute can arise: The contract is a very simple one in that the Foundation collects funds and sells memberships for the Zoo, and gives the Zoo the results. Claims arise in complex situations such as construction projects that involve labor and material costs, and safety issues. The potential for claims in this contract is small.

It is an employment contract: The Oregon Zoo/Zoo Foundation contract is not an employment contract.

There are environmental impacts: Environmental work is not part of the contract.

There are financial risks: There are no distinct financial risks apart from the donation process that is monitored in other ways.

There are operational risks: The sale of memberships by Zoo personnel is an operational function, however, it does not present the type of risk that operation of equipment or tools gives (such as can exist within the Oregon Zoo environment itself, such as the railroad and the simulator).

The contract is politically sensitive: Any contract can have political sensitivity. The contractual relationship between the Zoo and the Foundation does not present any untoward conditions.

Project management is required: The Foundation work is not a project in the sense of singular construction job or program implementation.

The agency's reputation can be affected: While any contract can have a reflection on Metro's reputation, the genesis of a problem would begin in another area, such as financial, rather than in the contractual relationship itself (such as contracting with a firm of questionable ethics or history).

Generic standard risk issues: As with any endeavor, there are general risk management issues (workers compensation, liability, property insurance, etc.). Standard insurance exists, including comprehensive general liability, workers' compensation, directors' and officers actions and employment practices liability, and indemnification language. All are appropriate to the relationship.

Who will take action?

The Metro Chief Financial Officer, Accounting Manager, Contracts Manager, Oregon Zoo and Zoo Foundation management.

When will action be accomplished?

By October 1, 2004

Follow-up necessary to correct or prevent reoccurrence.

Review of any contract changes in the future; date dependant upon changes being made.

Audit: Management of Relationship with Oregon Zoo Foundation Needs Improvement

Date: September 2004

AUDIT RESPONSE

Recommendation 4

The Chief Operating Officer should define the information and reports needed by Metro officials to perform their oversight responsibility, and take steps—including specifying the information requirements in the contractual Agreement if necessary—to ensure that the Zoo and the Foundation make this information available. At a minimum, in addition to an audited financial statement, the Foundation should report on its activities, accomplishments, revenues and expenses associated with each major duty defined in the Agreement. This reporting should document the Foundation’s financial contributions to the Zoo and provide a basis for evaluating the Foundation’s performance.

Agree

Yes

No (specify reasons for disagreement)

What action will be taken (if any)?

Management has already obtained the last audited financial statements from the Zoo Foundation. It is a requirement under GASB (Governmental Accounting Standards Board) No. 34 for this information to be included in Metro’s Comprehensive Annual Financial Report (CAFR), and this was done for the FY 02-03 Metro report. This will continue.

Management will review the contractual agreement and include, 1) information requirements to assure Metro’s financial reporting requirements are met, and 2) information enabling Metro to monitor the support relationship between the Zoo and the Foundation.

Who will take action?

The Finance and Administrative Services Department, management of the Oregon Zoo, the Office of Metro Attorney, and the Oregon Zoo Foundation finance staff will work together to take the appropriate actions.

When will action be accomplished?

The information will be required for the reports issued for the fiscal year ended June 30, 2005. The work to propose an amended contractual agreement will commence in September 2004.

Follow-up necessary to correct or prevent reoccurrence.

Contractual oversight by Metro management and implementation of appropriate administrative and financial reporting controls. (See Recommendation 5).

Audit: Management of Relationship with Oregon Zoo Foundation Needs Improvement

Date: September 2004

AUDIT RESPONSE

Recommendation 5

With regard to the Zoo/Foundation relationship, the Chief Operating Officer should establish appropriate procedures to independently monitor Metro's contractual relationship with the Foundation and assure that terms of a revised Agreement are complied with. Because the Zoo Director is a party to both sides of the contractual Agreement, the Chief Operating Officer needs to designate someone else as the responsible official for monitoring the terms of the Agreement.

Agree

Yes

No (specify reasons for disagreement)

What action will be taken (if any)?

Executive Order 85 issued in April 2004 by the Chief Operating Officer establishes the tone and nature of Metro's internal control environment. Oregon Zoo management will be trained on the internal control concepts early in FY 05.

The Chief Financial Officer will assess resources available to determine who will be primarily responsible for contractual oversight of the agreement between the Oregon Zoo and the Zoo Foundation.

Who will take action?

The Finance and Administrative Services Department will work with the Oregon Zoo management team.

When will action be accomplished?

Procedures will be developed as any amended contractual agreement is defined and entered into with the Zoo Foundation. Contractual oversight of the existing contract is currently underway in the Finance and Administrative Services Department.

Follow-up necessary to correct or prevent reoccurrence.

Continued monitoring.

Audit: Management of Relationship with Oregon Zoo Foundation Needs Improvement

Date: September 2004

AUDIT RESPONSE

Recommendation 6

Metro should enhance the role of the Contract Office by giving it the authority and resources needed to:

- Identify high risks in contracts and assure that appropriate controls are in place to mitigate these risks.
- Monitor departments to assure they are complying with contracting policies and procedures.
- Monitor high risk contracts to assure compliance with contract terms and assure that identified risks are being adequately controlled.
- Establish a performance reporting system to make contract results visible and identify areas needing improvement.

Agree

Yes X

No (specify reasons for disagreement)

What action will be taken (if any)?

Identification and initiation of contracts must originate with the using department, as they know their business needs. Assistance from Contracts and Purchasing in drafting and executing those contracts can then occur early in the process for best efficiency and effectiveness.

That connection comes from the quality of the professional relationships with the individuals responsible for those contracts. The Metro Contracts Manager and Contracts and Purchasing staff routinely and periodically discusses contractual matters with a number of Oregon Zoo managers and project managers. These include the Director, the Assistant Director responsible for Zoo operations, the Deputy Director responsible for the Living Collection (both plant and animal) and education, the Budget and Finance Manager, the Construction and Maintenance Manager, the Capital Project Manager, the Maintenance Projects Supervisor, the Contracts Consultant, and others responsible for contractual obligations.

Appropriate Oregon Zoo staff will be given training on various aspects of contracts, such as authority, how to mitigate risks, execution of grants, etc.

Lastly, use of Metro standardized contract forms by all Metro staff is a high priority for Purchasing and Contracts. In conjunction with a rewrite of Metro Code 2.04 to reflect major legislative changes made by the Oregon Legislature last year, the Metro Attorney is doing a complete review of these formats and content.

Any additional steps will be contingent upon the direction given by the Metro Council in terms of the relationship it expects between the Oregon Zoo and the Zoo Foundation.

Who will take action?

Chief Financial Officer, Contracts Manager, Purchasing and Contracts staff, Zoo management.

When will action be accomplished?

January 2005

Follow-up necessary to correct or prevent reoccurrence.

On-going

Audit: Management of Relationship with Oregon Zoo Foundation Needs Improvement

Date: September 2004

AUDIT RESPONSE

Recommendation 7

Metro should implement the full range of recommendations made in the Metro Auditor report of December 2000, *Contracting: A Framework for Enhancing Contract Management*. That report made detailed recommendations for establishing an appropriate Metro contract management system, including as just stated enhancing the role of the Contract Office. At the time, Metro's Executive Officer agreed to implement the recommendations, but although progress has been made, more needs to be done. If all the processes recommended in that report were in place, some of the problems identified in this report may have been avoided.

Agree

Yes

No (specify reasons for disagreement)

What action will be taken (if any)?

Five of the original eight recommendations listed in the Metro Auditor report of December 2000, *Contracting: A Framework for Enhancing Contract Management* are implemented.

The three remaining recommendations focus on larger efforts that are beyond immediate current resources, however, we are working to realign our methods of doing business to effectively meet these recommendations.

With respect to a management reporting system providing oversight information to top management and departmental managers, contract coordinators were designated for all departments in 2002. The contract cover sheet provides additional information to managers to alert them to special risk issues of a particular contract.

The Human Resources department is developing some approaches to enhance employee training and performance evaluation, and we hope to use that as a springboard to a project management training system.

We are currently working to integrate the contracts manual with electronic methods of readily available information (Intramet), which will provide self-service contract information (and to that extent, training) to contract managers. Realignment of job duties in Purchasing and Contracts is also part of the solution to better support contracts managers.

Any additional steps will be contingent upon the direction given by the Metro Council in terms of the relationship it expects between the Oregon Zoo and the Zoo Foundation.

Who will take action?

Chief Operating Officer, Contracts Manager

When will action be accomplished?

Unknown

Follow-up necessary to correct or prevent reoccurrence.

Continuation of training



Metro Auditor Report Evaluation Form

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Name of Audit Report: Management of Relationship with Oregon Zoo
Foundation Needs Improvement

Please rate the following elements of this report by checking the appropriate box.

	Too Little	Just Right	Too Much
Background Information	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
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Length of Report	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Clarity of Writing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
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Suggestions for our report format: _____

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Other comments, ideas, thoughts: _____

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