Summary Title: Discussion of & Potential Direction for Next Steps Regarding the Roth Building, 300 Homer Avenue

Title: Review of the Report on the Palo Alto History Museum's Fundraising Status for the Roth Building Rehabilitation Project (300 Homer Avenue), Discussion of Options for Roth Building use and Rehabilitation, and Direction for Next Steps; Approval of an Agreement With Sea Scouts/Environmental Volunteers to Provide $65,000 in Dedicated Funding for Uses Related to the Mission of the Environmental Volunteers

From: City Manager

Lead Department: Administrative Services

Recommendation
Staff recommends that the City Council:

1. Review the status of the fundraising for the Roth Building rehabilitation project and provide direction on possible next steps for the Roth Building;
2. Approve allocation of $65,000 from the FY 2020 City Council Contingent account to the Sea Scouts/Environmental Volunteers, consistent with direction provided by Council on December 17, 2018; and
3. Authorize the City Manager to negotiate and execute an agreement with Sea Scouts/Environmental Volunteers for use of the $65,000 in dedicated funding from the City Council Contingent account.

Executive Summary
For more than a decade, the Palo Alto History Museum (PAHM) has engaged in various strategies and activities to raise funds from private and public sources to undertake a seismic and historical rehabilitation of the Roth Building, 300 Homer Avenue, and to operate a historical museum at this location. This staff report is intended to provide an update on the direction provided to staff at the December 17, 2018 City Council meeting (CMR 9767) including the validation of fundraising by PAHM as performed and reported by an outside firm. The report builds on information provided in the most recent updates provided to Council in September (CMR 10600) and December (CMR 10868) 2019. Staff is seeking review of the status of this project in the context of this validation of fundraising and potential direction on next steps as
part of this project.

**Background**

The City acquired the Roth Building in April 2000. In 2002, the City issued a Request for Proposals (RFP) for proposed uses of the Roth Building, and received one response, from the PAHM. In 2007, the City and PAHM entered into a two-year option agreement to lease the Roth Building. Since 2007, PAHM personnel and City staff have examined a variety of proposals to fund the capital and operating needs of the Roth Building historical museum and the City Council has extended the option agreement several times. Additional background information can be found by referring to prior staff reports, CMRs: 2197, 2891, 4703, 5365, 5551, 5879 and 8612. The 2007 option agreement was extended several times over the past 13 years, but finally lapsed in late 2018 and is no longer in effect.

In December 2018 (Report #9767) the City Council reviewed the status of the Roth Building project and directed staff, over the next six months, to validate the PAHM’s recent fundraising milestone of $1.75 million - a target set by Council for a certain period of time, between 2017 and present. At that time, Council did not choose to extend the option agreement further but directed staff to update the option and lease agreement, which had not been updated since 2007, for later consideration by Council.

On December 17, 2018 Council approved the following motion (9-0):

A. *Extend the deadline by six months for the Palo Alto History (PAHM) to achieve the goal of raising $1.75 million as set by Council in 2017 (to allow for validation of PAHM fundraising);*

B. *Direct Staff to revise and update the lease agreement between the Palo Alto History Museum and return to City Council in six months for approval;*

C. *Adopt a Resolution designating the Roth Building as a park and committing to use the Roth Building consistent with park use for a period of no less than 20 years and making other representations to apply for historic preservation grant funds from the County of Santa Clara to rehabilitate the Roth Building roof;*

D. *Transfer the $665,000 of Sea Scout Building Transferable Development Rights (TDRs) proceeds to the Roth Building Rehabilitation Reserve Fund; and*

E. *Direct Staff to return to Council to dedicate $65,000 from the Council Contingency Fund to the Sea Scouts.*

Staff has provided updates to the City Council on work towards this direction, both in September 2019 and December 2019. The most current status on each component of the motion is included in this report for consolidation purposes at the end of the Discussion section.

**City Council Previous Funding Actions**

In order to provide the background of funding actions, staff has consolidated the funding actions and direction to date below for Phase one of the project, consisting of capital investment expenses, the general construction and rehabilitation of the facility to prepare the building to move to Phase 2, the build-out of the museum space. The City Council has approved
two primary funding sources thus far.

1) Council approved the designation of the Roth Building as a “Sender Site” in the Transfer of Development Rights (TDR) program. Staff followed the provisions for eligible City owned buildings to participate in the TDR program as outlined in Sections 18.18.080 and 18.28.060 of the Palo Alto Municipal Code (PAMC). The program allows a Category 2 resource, such as the Roth Building, to be eligible as a “sender site” for a 9,592 square foot floor area bonus to be utilized at an eligible “receiver site”. The TDRs were put to bid and sold raising $2.88 million.

2) On December 15, 2015, City Council passed a motion instructing staff to identify $1.0 million to fund rehabilitation costs for the Roth Building. All potential sources were examined, and staff recommended that the Budget Stabilization Reserve be drawn down to provide the $1.0 million. The Museum representatives asserted that with this contribution and the sale of Transferable Development Rights (TDRs), further fundraising would gain traction.

On June 29, 2015, the Council approved a budget amendment in the Capital Improvement Fund to establish a Roth Building rehabilitation reserve in the fund in the total amount of $3.88 million.

Palo Alto History Museum has been working to fundraise the gap in funding for Phase one. After identifying $1.4 million in fundraising and a remaining gap of $3.5 million in identified project funding, in 2017, the City Council challenged the PAHM to raise 50% of the identified gap, or $1.75 million in the coming 12 months. In December 2018, the PAHM tentatively confirmed completion of fundraising the additional $1.75 million. The City Council directed staff to validate these funds for further project progress towards Phase one.

In September 2019 staff provided an update to Council indicating that additional time was need to perform the validation of fundraising, the expansion of the scope of validation of fundraising to the full $3.2 million anticipated to assist in funding the phase one capital investment, and that a firm would be hired to assist in the completion of this work. The City hired Macias Gini and O’Connel (MGO) to validate the PAHM fundraising to accomplish item A from Council’s motion, Extend the deadline by six months for the Palo Alto History (PAHM) to achieve the goal of raising $1.75 million as set by Council in 2017 (to allow for validation of PAHM fundraising). This report provides a summary of the findings from MGO and the report is attached (Attachment A).

Also, due to the timing of staff’s return to the City Council, staff recommended and the City Council approved on October 21, 2019 (CMR 10658) a reappropriation of the FY 2019 City Council contingent account in the amount of $65,000 to FY 2020 for the implementation of item E in the original motion.
Discussion
The City hired MGO to review and validate the entire population of fundraising that was reported by the Palo Alto History Museum in 2018. At that time Council had set the goal of PAHM meeting a fundraising target of $1.75 million and directed staff to validate that amount. In researching the Museum’s fundraising, staff found that the earlier reported figure of $1.4 million had also not been validated. Together this fundraising totaled $3.15 million. The City and PAHM agreed it best to expand the scope of validation to all funds, not just the $1.75 million target. The expanded population of fundraising and validating expertise needed increased the time staff required to perform the review. It should be noted that MGO did not perform an official financial audit of the Palo Alto History Museum financials; this engagement focused solely on the evaluation of progress towards fundraising goals and identification of available funds for investment in the construction project at the Roth Building.

The work performed by MGO included interviews with PAHM staff, review of records in the donations database, review of data from the accounting system and review of donations and pledges along with available supporting documents. MGO’s work culminated in a final report (Attachment A). A draft final report was reviewed with PAHM and their edits and comments where incorporated into the final report. PAHM provided a letter in response to the report (Attachment C).

The key conclusion in the report is that PAHM has fundraised and received donations and pledges totaling $7.7 million, however, PAHM does not currently have sufficient cash on hand to meet the fundraising target of $3.15 million for contribution to the rehabilitation construction (Phase 1) of the Roth Building. Since approximately 2000, the museum has received donations of $4.8 million and pledges of $2.9 million which is inclusive of the $3.15 million amount that PAHM reported to the City. However, expenditures for the PAHM have been in the $3.6 million range for that same period, since 2000.

As of November 2019, PAHM has an available operating cash balance of approximately $1 million. In addition to the cash balance, PAHM has total pledges of $2.9 million of which $2.0 million is restricted for other uses as discussed below. MGO reviewed the pledges and after identifying levels of risk, has deemed $0.2 million (up to $580,000) likely to be collected – these are the pledges that are less than three years old.

---

1 Page 3 of the MGO report Assessment of Palo Alto History Museum (PAHM) Fundraising Efforts for Phase 1.
2 An aging chart for pledges is provided on page 8 of the MGO report Assessment of Palo Alto History Museum (PAHM) Fundraising Efforts for Phase 1.
Donations
The detailed history of all donations shown in the MGO report since 2000 is presented in the table below.

### TABLE 1: Summary of All Donations received since 2000

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt;2000</td>
<td>$250</td>
<td>2010</td>
<td>$192,879</td>
</tr>
<tr>
<td>2000</td>
<td>$14,415</td>
<td>2011</td>
<td>$598,577</td>
</tr>
<tr>
<td>2001</td>
<td>$1,000</td>
<td>2012</td>
<td>$165,943</td>
</tr>
<tr>
<td>2002</td>
<td>$8,675</td>
<td>2013</td>
<td>$93,635</td>
</tr>
<tr>
<td>2003</td>
<td>$125,351</td>
<td>2014</td>
<td>$269,397</td>
</tr>
<tr>
<td>2004</td>
<td>$62,856</td>
<td>2015</td>
<td>$143,642</td>
</tr>
<tr>
<td>2005</td>
<td>$308,642</td>
<td>2016</td>
<td>$440,775</td>
</tr>
<tr>
<td>2006</td>
<td>$250,637</td>
<td>2017</td>
<td>$463,602</td>
</tr>
<tr>
<td>2007</td>
<td>$128,215</td>
<td>2018</td>
<td>$976,619</td>
</tr>
<tr>
<td>2008</td>
<td>$131,078</td>
<td>2019</td>
<td>$394,595</td>
</tr>
<tr>
<td>2009</td>
<td>$111,595</td>
<td>Total</td>
<td>$4,882,378</td>
</tr>
</tbody>
</table>

A summary of PAHM revenue and expense is shown below. A graph of revenue and expenses since 2005 is shown on page 8 of the MGO report.

### TABLE 2: Summary of PAHM Revenues & Expenses

<table>
<thead>
<tr>
<th>PAHM Revenue and Expenses</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Revenue since 2005 (page 6 MGO)</td>
<td>$4,330,654</td>
</tr>
<tr>
<td>Other sources*</td>
<td>$269,349</td>
</tr>
<tr>
<td>Operating expenses since 2005</td>
<td>($3,599,559)</td>
</tr>
<tr>
<td>Cash on hand*</td>
<td>$1,000,444</td>
</tr>
</tbody>
</table>

---

3 Some donations were recorded in the year shown above after they were migrated from a prior system.

4 The MGO review could not verify all revenue sources, MGO did not review records prior to 2000 as the ROTH building purchase in 2000 was the catalyst for PAHM capital campaign fundraising efforts.

5 Page 4 of the MGO report Assessment of Palo Alto History Museum (PAHM) Fundraising Efforts for Phase 1.
Pledges
MGO reviewed outstanding pledges that totaled approximately $2.9 million and determined that $2.01 million have restrictions from the donor and cannot be used for Phase 1 construction. MGO determined that of the remaining pledges approximately $681,500 have high risk factors that decrease the likelihood of the pledge being collected. Approximately $242,600 (or up to $583,000) in pledges are more likely to be collectable according to the MGO report.

Summary of Project Funding
The overall funding picture for the Roth Building rehabilitation project is shown in the table below. Following the table are additional updates to the financial status of Phase 1 capital investment and construction that may impact the overall funding picture. The PAHM has expended $57,000 to date on this project for the construction contract. Not itemized below is the award of $100,000 in grant funding from the County of Santa Clara County Parks Historical Grant for reimbursement of costs associated with the roof replacement.

<table>
<thead>
<tr>
<th>Description</th>
<th>Other Funding Sources Identified and Projected</th>
<th>Projected Cost</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Building Project Total Rehabilitation Cost</td>
<td></td>
<td>$9.2 million</td>
<td></td>
</tr>
<tr>
<td>City’s contribution: TDRs, BSR, interest, Library Impact Fees (est. $300k)</td>
<td></td>
<td>$5.2 million</td>
<td></td>
</tr>
<tr>
<td>PAHM cash on hand as of November 2019</td>
<td></td>
<td>$1.0 million</td>
<td></td>
</tr>
<tr>
<td>Phase 1 Pledges as of December 2019</td>
<td>$583,000-$242,600</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Phase One – Capital Shortfall (as of 2019)</td>
<td></td>
<td>~($2.8m - $2.4m)</td>
<td></td>
</tr>
</tbody>
</table>

The Phase 1 construction cost estimate of $9.2 million is from 2016. According to PAHM’s construction contractor, Vance Brown, who City and Museum staff met with in January 2020, this cost estimate has likely escalated by at least ten percent making the current project cost anticipated to exceed $10 million. Another factor that may add costs to the project is the fact that the subcontractor costs since initial estimates have not been updated by Vance Brown. Only once the project has a firm start date does the contractor update these estimates with a firm quote from the subcontractors. This step will likely result in additional cost increases.

---

6 Page 7 of the MGO report Assessment of Palo Alto History Museum (PAHM) Fundraising Efforts for Phase 1
7 Page 7 of the MGO report Assessment of Palo Alto History Museum (PAHM) Fundraising Efforts for Phase 1; factors include donation and payment history of the donor, age of the pledge, amount owed/pledged; and documentation status (written or verbal)
Discussion of Next Steps
Given the findings in the MGO report as well as the updated discussion of overall Phase one project construction costs, staff is bringing back to the City Council these findings for discussion and potential direction on next steps. The fact that the passage of over a decade of time has not fared well for the structure nor has it resonated with stakeholders and fundraising efforts. Over the span of nearly two decades, despite best intentions, the work needed to preserve the building has been postponed as the necessary private funds have not fully materialized, leaving the building in an increasingly degraded physical state.

Over the past year as staff have been completing these fundraising validation efforts with the necessary stakeholders – City departments, the PAHM, and Vance Brown – ideas on the potential path forward for this building and project have been discussed. The ideas below spring from these conversations with the core tenet of building preservation in mind and staff is seeking input and direction from Council on the next steps in this potential project given the current status of project funding. These ideas are not intended to be holistic or mutually exclusive but rather resurrect prior potential paths forwards for this valued community asset as well as new options. The City would coordinate with PAHM on these revised paths forward pending City Council direction.

Request for Proposal
The last request for proposals RFP for the Roth Building was completed in 2005, over a decade ago. The City Council considered the development of a RFP for the Roth Building in 2017 (CMR 8612) as the Council was faced with an approximately $3.5 million funding gap in the construction project then. At the Council’s direction, staff could resume this option and dedicate staff time and resources to the execution of a new RFP. An RFP would inform what the market would bear for this property and may identify new interest as well as alternative ideas for use. The zoning for this land is currently Public Facilities (PF) and this along with the City’s Comprehensive Plan and other planning and development codes would be necessary to consider in soliciting and evaluating potential options. This process would extend the time the building remains vacant and could be done in conjunction with other options described below.

As discussed previously, the high-level steps needed for issuing a new RFP would include:
- Prepare a timeline for the RFP
- Obtain input from Council on goals, concepts and core variables for the RFP
- Solicit a request for qualifications to set a prequalification level which firms must meet to respond to the RFP (optional)
- Issue the RFP to qualified firms and allow a one-to-two-month window for firms to respond
- Hold interviews and presentations with firms, the City, and the community representatives
- Consider alternatives presented by proposing firms and develop options for review with the City Manager
- Present options and a recommendation to the Council along with related contract
awards
It is estimated that the RFP selection process would take approximately one year to complete.

Physically Stabilize the Roth Building
Allow PAHM to begin initial construction to stabilize the Roth Building from water intrusion and repair a back wall based on the current building permit and design that PAHM holds. This would stabilize the facility; however, the building would not be ready for occupancy. The estimated cost for this work is $8.5 million\(^8\) according to initial estimates from PAHM contractor Vance Brown. This idea leverages the existing building and approved planning permits and starts the rehabilitation of a City owned property and the overall project. PAHM estimates that this activity, demonstrating capital investment in the facility, would motivate additional fundraising. However, as noted above, funding of $6.2 million ($5.2 million from City contributions and $1.0 million in PAHM operating cash balance) would be insufficient to fully fund a project this size. This option would require identification and commitment of additional funding prior to the commencement of work.

Sharing of Facility
The City and PAHM could work together and/or potentially with another party to share the 20,000 square foot facility so that it would not be solely occupied by PAHM. This co-tenancy could lessen the cost burden on the PAHM by sharing costs with another party both for construction and the ongoing operating costs associated with maintaining and running a building of this size. Parking would potentially be an issue depending on the use and volume of customers/users if any. The PAHM has expressed an openness to discuss a shared occupancy concept including shared square footage on the first and/or second floor of the facility.

One example of sharing the facility could be PAHM co-tenancy with City operations or common/community facilities. For illustration purposes only, the City currently leases space for City staff at satellite locations such as the Development Center (approximately 12,000 square feet) and Utilities staffing at Elwell Court (approximately 16,000 square feet) and an average City Hall floor is 6,000 square feet.

Co-tenancy with the City or another party will necessitate detailed discussions and formal agreement(s) to address issues such as but not limited to parking needs/requirements, allocation of space, expenses, and building access, constraints related to the County grant designation of the building as parkland, and building permit amendment or new application. Per PAHM, the Conditional Use Permit (CUP) allows for some sub-leasing to appropriate nonprofit entities; this option could be resurrected. Sharing of the facility would necessitate PAHM staff to coordinate with the organization’s board as well.

Lastly, although not a path forward for the physical Roth Building facility, it is notable that the MGO report also provides recommendations, which may be considered by PAHM and the City should the parties wish to continue the current project path. These include:

---

\(^8\) Estimate from Vance Brown/PAHM
• The City and PAHM should consider an agreement which could include requirement for a regular report on fundraising, an approved PAHM operating budget, operating reserve and review of financial policies and procedures.
• Establishment of a PAHM operating reserve, which is an unrestricted fund balance to provide a cushion against unexpected events together with a realistic plan to replenish the reserve.
• PAHM should continue to expand its comprehensive policies and procedure manual to establish a control environment and to address internal control risks.
• Establish an account that is used by PAHM to estimate the true collectability of receivables by accounting for doubtful accounts.

Summary of Council’s December 17, 2018 direction and the current status of each item:

<table>
<thead>
<tr>
<th>Council Motion</th>
<th>Background/Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. <strong>Extend the deadline by six months for the Palo Alto History (PAHM) to achieve the goal of raising $1.75 million as set by Council in 2017 (to allow for validation of PAHM fundraising);</strong></td>
<td>Review of fundraising completed.</td>
</tr>
<tr>
<td>B. <strong>Direct Staff to revise and update the lease agreement between the Palo Alto History Museum and return to City Council in six months for approval</strong></td>
<td>Development of option and lease agreement in progress. The updated draft of the agreement is being reviewed by City departments, including Public Works, Planning and Community Services. While this effort is moving forward it has been separated from the review of fundraising. Depending on Council’s direction as a result of reviewing the fundraising this may impact the terms of the option and lease agreement, or whether to proceed with the agreement.</td>
</tr>
<tr>
<td>C. <strong>Adopt a Resolution designating the Roth Building as a park and committing to use the Roth Building consistent with park use for a period of no less than 20 years and making other representations to apply for historic preservation grant funds from the County of Santa Clara to rehabilitate the Roth Building roof;</strong></td>
<td>Resolution approved and County grant secured.</td>
</tr>
<tr>
<td>D. <strong>Transfer the $665,000 of Sea Scout Building Transferable Development Rights (TDRs) proceeds to the Roth Building Rehabilitation Reserve Fund; and</strong></td>
<td>Complete</td>
</tr>
</tbody>
</table>
E. Direct Staff to return to Council to dedicate $65,000 from the Council Contingency Fund to the Sea Scouts.

Pending approval in this report (Recommendation 2). The original request for this funding was made by the Environmental Volunteers (Sea Scouts) in December 2018 (Attachment B).

Other Updates

Building permit
PAHM’s construction contractor currently holds an approved (in February 2019) building permit for the rehabilitation project of which PAHM was the applicant. The building permit remains active and has been extended through February 2020. PAHM has initiated a second six-month extension of the building permit to adjust for timing of this project including but not limited to the Lease and Option Agreement review and approval by the City Council. Building permits may be extended up to three times.

County grants
The City in partnership with PAHM has submitted two new grant applications to the 2019 Santa Clara County Historical Grant Program. One grant is to provide additional funding for the roof replacement project and the other grant is to provide funding to preserve the art frescoes on the outside front wall of the building. These grants will be determined in 2020 after award recommendations, which are scheduled for February 2020. As discussed above, an earlier grant submitted in the County’s prior grant cycle to help support roof repair was granted by the County in the amount of $102,992; the contract was recently signed.

Stakeholder Outreach
Throughout this project staff has maintained regular and open communications with PAHM and its staff as well as the construction contractor. The collaboration between the City and PAHM has been positive as a result. Internally, staff have been coordinating among the Public Works, Community Services, Planning and Administrative Services departments on different aspects of the project.

Resource Impact
City Financial Contributions
As discussed earlier, the City Council previously took actions to set aside $3.88 million in resources for the Roth Building rehabilitation. Funding primarily resulted from the sale of TDRs ($2.88 million), plus an additional contribution from the Budget Stabilization Reserve ($1.0 million). These funds plus interest earned remain accounted for in the General Capital Improvement Fund (471) in a reserve; as of February 2020, this reserve stands at $4.2 million.

In addition, the Sea Scout Building Transferable Development Rights (TDRs) proceeds ($665,000) for historical restoration only also remain in a reserve in the General Capital
Improvement Fund; as of February 2020, this reserve stands at $700,030. Lastly, it is expected that $300,000 in Library impact fees will assist in coverage of costs associated with the archive build out. Therefore, in total, City funding of $5.2 million is available.

Environmental Review
The Roth Building rehabilitation project is categorically exempt from review under the California Environmental Quality Act (CEQA) pursuant to CEQA Guidelines Section 15331, Historical Resource Restoration/Rehabilitation, as a project limited to maintenance, repair, and rehabilitation in accordance with the Secretary of Interior Standards for Historic Preservation.

Attachments:
- Attachment A: Assessment of Fundraising Efforts; MGO report
- Attachment B: Sea Scouts-Environmental Volunteers Letter
- Attachment C: Palo Alto History Museum Letter Response
February 26, 2020

David Ramberg  
Assistant Director, Administrative Services  
City of Palo Alto  
250 Hamilton Avenue  
Palo Alto, CA 94301

Dear Mr. Ramberg:

On behalf of Macias Gini & O’Connell LLP (MGO), we are pleased to provide the following reports related to our assessment of donations and pledges received by the Palo Alto History Museum (PAHM) for the construction rehabilitation project of the historic Roth Building in Palo Alto (Phase 1):

- Executive Summary
- Assessment of Palo Alto History Museum (PAHM) Fundraising Efforts for Phase 1

We thank you and your staff for your time, cooperation, and information extended throughout this consulting engagement.

Sincerely,

Scott P. Johnson, CPA, CGMA  
Partner
Executive Summary

Why We Conducted the Assessment

The City engaged Macias Gini & O’Connell LLP (MGO) to document, validate, and report on the total amount of donations and pledges received by the Palo Alto History Museum (PAHM) for the construction rehabilitation project of the historic Roth Building in Palo Alto (Phase 1). This summary report provides the results of our limited-scope consulting engagement and provides the results and status on funds available for Phase 1.¹ See Appendix A for Objectives, Scope, and Methodology.

To meet its initial funding goal of $9.2 million for Phase 1 of the project, PAHM’s strategy involves a mix of the following funding streams:

- private donations that have been received;
- unrestricted pledges that have been committed, but funds not yet received, that can be used for Phase 1;
- City of Palo Alto funding previously committed; and
- other governmental grants.

What the Assessment Found

Based on our analysis at this time, there is no evidence to support that PAHM has the required $9.2 million available for Phase 1. We estimate that PAHM need to secure approximately a minimum of $2.36M, and at most, $2.85M for Phase 1 expenses to meet this goal. The following description provides details on total and projected funding for all funding streams, also shown in Exhibit 1 below:

- $5.1 million dollars in governmental funding not yet released for Phase 1.
- $1,000,443.76 balance of cash on hand as of November 30, 2019 derived from (1) donations, and (2) pledges that have already been received, less (3) expenditures made to-date. Future funding from pledges or commitments, but funds not yet received, were classified as pledges and were not considered as cash on hand.
- Phase 1 pledges as of December 2019 range from $250,000 to $583,000².
- $157,000 in prospective County grants committed to the PAHM Phase 1 project and funds paid on construction to-date.

¹ We did not evaluate financial health of PAHM, nor did we assess internal controls, or analyze controls related to revenues and expenditures. Although we did review the agency’s policies as they related to our objective, we did not perform testing to ensure that policies were implemented.
² This range represents the estimated collections of pledges currently on record.
Executive Summary

Exhibit 1: Phase 1 Funding for Palo Alto History Museum Rehabilitation Project

<table>
<thead>
<tr>
<th>Description</th>
<th>Other Funding Sources Identified</th>
<th>Projected Cost</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Building Project Total Rehab Cost</td>
<td></td>
<td>$9.2 million</td>
<td></td>
</tr>
<tr>
<td>All Governmental Funds (City of Palo Alto TDRs,</td>
<td>$5.1 million</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Library Impact funds, Back Wall fund, Santa Clara</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>County grant)*</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash on hand, as of November, 2019</td>
<td>$1.0 million</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Phase 1 Pledges as of December 2019**</td>
<td>$583,000-250,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Phase 1 funding gap estimate</td>
<td></td>
<td>~$2,850,000 – 2,517,000</td>
<td></td>
</tr>
</tbody>
</table>

| Prospective Funding                                   |                                  |                |                       |
| County Roof grant***:                                 | $100,000                         | ~$2,750,000- 2,417,000 |           |
| Funds already paid on construction contract***:       | $57,000                          | ~$2,693,000 – 2,360,000 |           |

* City of Palo Alto representatives are in the process of verifying the approvals for these funds.
** This amount represents an estimate of collectable pledges based on a pledge risk assessment.
*** Documentation not provided. Attestation from the PAHM Executive Director.

As noted, PAHM is also relying on pledges from private donors to fund Phase 1. Current reported unrestricted pledges total $937,000; and we determined that approximately only $909,000 could be potentially available for Phase 1. However, in order to provide an accurate picture of pledge funds available for the project, collectability of those pledges must be considered. Therefore, MGO reviewed pledges on file and assessed risk to collectability for each. Although there is not an established methodology to estimate the collectability of pledges, our estimates included the following factors; 1) donation and payment history of the donor, 2) age of the pledge, 3) amount owed/pledged, and 4) documentation status of the pledge (written or verbal). It should also be noted that even signed pledge letters are not a guarantee that the pledge will be collectable in full.

Based on our assessment, we identified that of the $937,000 in unrestricted pledges, approximately $242,600 were more likely to be collectable because they were less than three years old (this could include updated pledge documents), or the donor had a strong and recent history of financially supporting the project and the pledge did not have associated financial contingencies. Our evaluation of pledge risk for non-collection concluded that from pledges available for Phase 1, approximately $681,500 had high risk factors associated with the pledge, which decreased the likelihood that PAHM will be able to collect the pledge. Although a high percentage of pledges on file do have high risk factors associated with them, this does not mean that all pledges with risk will be uncollectable. Additionally during our assessment, we noted that some pledges have payment terms that include provisions that payment will commence upon or after the start of construction.³

³ The $909,000 available for Phase 1 accounts for the following adjustments; (1) one pledge that should be written off; (2) an additional restriction on a pledge; and (3) a duplicate entry.
Executive Summary

Appendix A

OBJECTIVES

The objectives of this assessment were to document, validate, categorize, and provide a report on the total amount of donations and pledges received by the Palo Alto History Museum (PAHM) for Phase 1 fundraising efforts. Additionally, we determined the amount of funds available for the Phase 1 project. Under a separate cover, we will provide best practices for monitoring and reporting of donations and pledges.

SCOPE

The scope of this engagement involved PAHM’s fundraising efforts from inception to-date, primarily related to the construction rehabilitation project of the historic Roth Building in Palo Alto (Phase 1). Our assessment focused on funds available for Phase 1. We did not evaluate the financial health of PAHM, nor did we assess controls related to their revenues and expenditures. Although we did review PAHM’s policies, we did not perform testing to ensure that policies were implemented, nor did we review their internal controls. Although we obtained an extract of revenues from the financial software, we did not review the financial system for accuracy.

This consulting engagement was conducted in accordance with the Statements on Standards for Consulting Services issued by the American Institute of Certified Public Accountants (AICPA) and the terms of the agreement between MGO and the City of Palo Alto. The work performed is only for the use and benefit of the City.

Because the scope of work does not constitute an examination or audit in accordance with attestation standards established by the AICPA, we have not expressed an opinion on the results of our work, but instead provided a report with our financial analysis and observations. We have no obligation to perform any procedures beyond those listed in the report. If, however, as a result of the procedures we performed, or through other means, matters came to our attention, we have disclosed those matters to the City. Such disclosures, if any, may not include all matters which might have come to our attention had we performed additional procedures or an examination.

METHODOLOGY, INCLUDING LIMITATIONS

To document, validate, and categorize pledges and donations, we sought to gain an understanding of PAHM’s policies, procedures, and processes related to pledge and donation collections and reporting through the following activities:

- conducted interviews with the PAHM Executive Director, Assistant Director, and Bookkeeper;
- obtained extract of donation database;
- reviewed record retention policies and other policies and procedures;
- performed walk through of mail handling procedures;
- obtained extract of revenues from accounting system;
- reviewed donations listed in donation database;
- obtained internal listing of pledges and available supporting documents;
- reviewed outstanding pledges to assess collectability and risk; and
- lastly, we analyzed funds available for Phase 1 of the PAHM project.

One significant limitation we encountered was related to data in the donation database, which we determined was incomplete.
Assessment of Palo Alto History Museum (PAHM) Fundraising Efforts for Phase 1
# TABLE OF CONTENTS

OBJECTIVES, SCOPE, AND METHODOLOGY ................................................................. 1
BACKGROUND ........................................................................................................... 2
PRINCIPAL RESULTS .............................................................................................. 3
RECOMMENDATIONS FOR BEST PRACTICES ....................................................... 9
APPENDIX A - MATTERS FOR CONSIDERATION ............................................... 10
OBJECTIVES, SCOPE, AND METHODOLOGY

OBJECTIVES
The objectives of this assessment were to document, validate, categorize, and provide a report on the total amount of donations and pledges received by the Palo Alto History Museum (PAHM) for Phase 1 fundraising efforts. Additionally, Macias Gini & O’Connell LLP (MGO) determined the amount of funds available for Phase 1.

SCOPE
The scope of this engagement involved PAHM’s fundraising efforts from inception to-date, primarily related to the construction rehabilitation project of the historic Roth Building in Palo Alto (Phase1). This report focuses on funds available for Phase 1. We did not evaluate the financial health of PAHM, nor did we assess controls related to their revenues and expenditures. Although we did review PAHM’s policies, we did not perform testing to ensure that policies were implemented. Additionally, we did not analyze expenditures. Although we obtained an extract of revenues from the financial software, we did not review the financial system for accuracy.

This consulting engagement was conducted in accordance with the Statements on Standards for Consulting Services issued by the American Institute of Certified Public Accountants (AICPA).

Because the scope of work does not constitute an examination or audit in accordance with attestation standards established by the AICPA, we have not expressed an opinion on the results of our work, but instead provided a report with our financial analysis and observations. We have no obligation to perform any procedures beyond those listed in the report. If, however, as a result of the procedures we performed, or through other means, matters came to our attention, we have disclosed those matters to the City. Such disclosures, if any, may not include all matters which might have come to our attention had we performed additional procedures or an examination.

METHODOLOGY, INCLUDING LIMITATIONS
To document, validate, and categorize pledges and donations, we sought to gain an understanding of PAHM’s policies, procedures, and processes related to pledge and donation collections and reporting, through the following activities:

- conducted interviews with the PAHM Executive Director, Assistant Director, and Bookkeeper;
- obtained extract of records in the donation database;
- reviewed record retention policies and other policies and procedures;
- performed a walk-through of mail handling procedures;
- obtained an extract of revenues from the accounting system;
- reviewed donations listed in donation database;
- obtained internal listing of pledges and available supporting documents;
- reviewed outstanding pledges to assess collectability and risk; and
- made conclusions related to funds available for Phase 1 of the PAHM project.

One significant limitation we encountered was related to data in the donation database, which we determined was not complete.
BACKGROUND

Effective February 2005, the Palo Alto History Museum (PAHM) was qualified by the Internal Revenue Service of the United States as a private nonprofit 501(c)(3) organization. Since that time, PAHM has been working towards the goal of developing the first history museum for the Palo Alto and Stanford community. In part, the mission of the PAHM is to showcase the legacy of innovation and remarkable heritage that are unique to Palo Alto and the Stanford community through the collection and preservation of local artifacts, oral histories, documents, and other media. To achieve this mission, PAHM has an initial goal of identifying $9.2 million to rehabilitate the City of Palo Alto’s Roth Building for its museum location. During its existence, PAHM has had three executive directors — with much of their time being the directors of a one-person organization. Although PAHM reports there have been several volunteers that have helped with administrative functions, additional paid staff were not hired until late in 2016, when Ms. Bajuk, the current Executive Director, was hired as Development Director. She was formally appointed Executive Director in 2018.

During her period as Executive Director at PAHM, Ms. Bajuk has focused on the goals of the PAHM, including fundraising goals, and also has been dedicated to improvement or standardization of process controls. During our assessment, she noted that part of her efforts as Executive Director/Development Director has been to review all records available to try to ensure that all hard copy information on file is added to the donation/pledge database or other internal tracking log. Additionally, she has taken steps to develop and update key operational policies such as the mail handling process, Whistleblower policy, document retention schedule, and an employee manual. She also reports that since the hiring of an Assistant Director in 2018, she now oversees the process of data entry and reporting.

Additionally, after implementing the donation database in 2017 and online donation portal, Ms. Bajuk is now in the process of ensuring that all new pledge forms and donation documentation are scanned and attached to donation and pledge records in the database. She is also in the process of implementing a monthly reconciliation process between the financial system and the donor database.

We reviewed PAHM’s fundraising efforts related to the capital project to rehabilitate the historic Roth Building in Palo Alto (Phase 1). This summary provides the status on funds available for Phase 1 of the Roth Building construction. We did not evaluate the financial health of PAHM, nor did we assess its internal controls, analyze controls related to revenues and expenditures, or verify the accuracy of information reported on its balance sheet. Although we did review the agency’s policies as they related to our objective, we did not perform testing to ensure that policies were implemented.
PRINCIPAL RESULTS

Section 1: Donation Documentation

Historically low staffing levels, use of volunteers and other contract workers, and lack of permanent office space may have contributed to the lack of standardized document retention practices for donations received by PAHM. No formalized policies and procedures were in place for donation recordkeeping until 2019. In addition, the Executive Director noted that although consultants and contractors were retained to perform administrative duties during certain periods in the past, for much of PAHM’s existence the organization has only had one employee, an Executive Director. Because of the minimal staffing, this position has had responsibility for a wide scope of duties; and few formalized policies and procedures existed until recently. Further, prior to the shared office space that PAHM rented during a period from 2015-2017, volunteers conducted PAHM business from their homes and consultants provided their own workspace. According to PAHM, as of August 2019, it has operated from a donated office space to run daily operations.

PAHM has not had a consistent way or location to file or store documentation until recently.\(^1\) Without a central repository for donation documentation, hard copy donation files dating back to 2017 are kept onsite, and any documentation kept by PAHM dated prior to 2017 is located in various storage locations. Due to this situation, the Executive Director has found documents that were not recorded in the database.\(^2\) The Executive Director explained the donation retention policy is that records were to be kept for either 10 years or permanently, depending on donation restrictions. A procedure was established in October 2019 for donations and pledges received, which includes scanning donation and pledge documentation for electronic retention in its database, as part of the mail collection process.\(^3\)

Section 2: Donation Validation

The state of historical donation record keeping impacts the accuracy of the donation information in the database, which is the system of record. Our review of the PAHM’s Live Impact donation database (database) indicates that total donations received by PAHM are recorded as $4,882,380.\(^4\) Total donations, by year, are shown below, in Exhibit 1. Although PAHM has been fundraising since prior to 2005, it was not until June 2017 when the database was implemented. Donations dated previous to mid-2017 are historical records that were imported into the system, and we cannot be certain the database is complete, or that it contains all donations made before that time frame, because a reconciliation has not been completed between all the documentation and the database. In total, as of November 4, 2019, the database lists 2,342 donations (funds received only), with the oldest donation listed as being made in 2000.

During our site visit, we tested some of the donation entries in the database against the donation documents retained. However, (1) because the majority of historical records are stored off site, (2) the Executive Director’s concerns about the completeness of both documentation and the information in the database, and (3) the fact that there has never been a full reconciliation of the database, we instead focused our efforts on testing pledges.

---

\(^1\) The records retention policy was developed in 2019.

\(^2\) The Executive Director noted that she has found letters or other written documentation referencing a donation or a pledge. She has not found un-recorded checks or other financial contributions.

\(^3\) We requested a report indicating which database entries have scanned documentation. PAHM indicated that the database will not produce a report that shows which entries or transactions within the database have associated electronic files.

\(^4\) This amount includes all private donations listed in the database, including any payments, whether full or partial, made towards a pledge. Pledge amounts that are unpaid will be discussed in a later section of this report. Additionally, this amount does not include any government funding committed, even if it was recorded in the database.
Assessment of Palo Alto History Museum Fundraising Efforts for Phase 1

Exhibit 1: Donor Database- Donations by Year

<table>
<thead>
<tr>
<th>Year donation was received</th>
<th>Total Amount received by year</th>
</tr>
</thead>
<tbody>
<tr>
<td>2005</td>
<td>$100,000</td>
</tr>
<tr>
<td>2006</td>
<td>$200,000</td>
</tr>
<tr>
<td>2007</td>
<td>$300,000</td>
</tr>
<tr>
<td>2008</td>
<td>$400,000</td>
</tr>
<tr>
<td>2009</td>
<td>$500,000</td>
</tr>
<tr>
<td>2010</td>
<td>$600,000</td>
</tr>
<tr>
<td>2011</td>
<td>$700,000</td>
</tr>
<tr>
<td>2012</td>
<td>$800,000</td>
</tr>
<tr>
<td>2013</td>
<td>$900,000</td>
</tr>
<tr>
<td>2014</td>
<td>$1,000,000</td>
</tr>
<tr>
<td>2015</td>
<td>$1,100,000</td>
</tr>
<tr>
<td>2016</td>
<td>$1,200,000</td>
</tr>
<tr>
<td>2017</td>
<td>$1,300,000</td>
</tr>
<tr>
<td>2018</td>
<td>$1,400,000</td>
</tr>
<tr>
<td>2019</td>
<td>$1,500,000</td>
</tr>
</tbody>
</table>

Source: This graph uses information from the Palo Alto History Museum’s donation database, based on year the donation was given.

Section 3: Funding Categorizations

For this analysis, to determine funds available for Phase 1, we considered the balance of cash on hand derived from (1) donations, and (2) pledges that have already been received, less (3) expenditures made to-date. Future funding from pledges or commitments, but funds not yet received, were classified as pledges and were not considered as cash on hand. According to a bank statement we reviewed for the period ending November 30, 2019, PAHM had an account balance of $1,000,443.76. This amount represents cash on hand in the bank, as of November 30, 2019.

To meet its initial funding goal of $9.2 million for Phase 1 of the project, PAHM’s strategy involves a mix of the following funding streams:

- private donations that have been received;
- unrestricted pledges that have been committed, but funds not yet received, that can be used for Phase 1;
- City of Palo Alto funding previously committed; and
- other governmental grants.

PAHM is currently counting on approximately $5.1 million dollars in governmental funding that is yet to be released for Phase 1. Total and projected funding for the PAHM is shown in Exhibit 2.
Exhibit 2: Phase 1 Funding for Palo Alto History Museum Rehabilitation Project

<table>
<thead>
<tr>
<th>Description</th>
<th>Other Funding Sources Identified</th>
<th>Projected Cost</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Building Project Total Rehab Cost</td>
<td></td>
<td>$9.2 million</td>
<td></td>
</tr>
<tr>
<td>All Governmental Funds (City of Palo Alto TDRs, Library Impact funds, Back Wall fund, Santa Clara County grant)*</td>
<td>$5.1 million</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash on hand, as of November, 2019</td>
<td></td>
<td>$1.0 million</td>
<td></td>
</tr>
<tr>
<td>Phase 1 Pledges as of December 2019**</td>
<td></td>
<td>$583,000-250,000</td>
<td></td>
</tr>
<tr>
<td>Phase 1 shortfall estimate</td>
<td></td>
<td></td>
<td>~$2,850,000 – 2,517,000</td>
</tr>
</tbody>
</table>

Prospective Funding

<table>
<thead>
<tr>
<th>Description</th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>County Roof grant***:</td>
<td>$100,000</td>
<td>~$2,750,000 – 2,417,000</td>
<td></td>
</tr>
<tr>
<td>Funds already paid on construction contract***:</td>
<td>$57,000</td>
<td>~$2,693,000 – 2,360,000</td>
<td></td>
</tr>
</tbody>
</table>

* City of Palo Alto representatives are in the process of verifying the approvals for these funds.
** This amount represents an estimate of collectable Phase 1 pledges based on a pledge risk assessment.
*** Documentation not provided. Attestation from the PAHM Executive Director.

Based on our analysis at this time, there is no evidence to support that PAHM has the required $9.2 million available for Phase 1. We estimate that PAHM will need to secure a minimum of $2.36M, and at most, $2.85M for Phase 1 expenses to meet this goal.

Section 4: Operating Expenses

Currently, PAHM has not established an operating expense reserve. An operating reserve is an unrestricted fund balance set aside to stabilize a non-profit's finances by providing for unexpected cash flow shortages, expenses, or losses. This is important to the success of Phase 1 because all operating expenses are paid through fundraising, which can vary from year to year. In our analysis of documents that PAHM provided to us, we noted that both revenues and expenditures fluctuated significantly year-to-year. However, to be able to establish an adequate operating reserve, PAHM will need to develop a forecast of cash flow needs necessary to cover operations and expenses. This forecasting is critical in establishing fundraising goals for operations as well as Phase 1 funding and beyond.

Another reason an operating reserve is important is that PAHM’s revenues and expenditures have varied significantly over time, as shown below in Exhibit 3. Our review of PAHM’s Income & Expense statement showed that historical income over the past five years ranged from about $160,000 to $978,000, with the last three years averaging around $630,000. The expenses for the same period ranged from $89,000 to $804,000 with the last three years averaging about $518,000. Defining and planning for income and expenses related to operations will help PAHM to ensure its success in meeting its goals.
Section 5: Risk Profile - Pledge Records and Collectability

In addition to cash on hand from donations, PAHM is also relying on pledges from private donors to fund Phase 1. We determined that the data related to pledges in the database were not sufficiently reliable to draw conclusions from, in terms of collectability. We then relied on internal record keeping documents, pledge documents, and when available, PAHM staff notes or comments, in order to assess collectability of pledges for Phase 1. For purposes of this assessment, in order to provide an accurate picture of funds available for the project, collectability of pledges must be determined. Although there is not an established methodology to estimate the collectability of pledges, our estimates included the following factors: 1) donation and payment history of the donor, 2) age of the pledge, 3) amount owed/pledged, and 4) documentation status of the pledge (written or verbal). It should also be noted that even signed pledge letters are not a guarantee that the pledge will be collectable in full.

When discussing pledges and accounts receivable with PAHM, the Executive Director noted that it is the current practice of PAHM to keep all pledges on the books unless the donor states that the pledge will not be fulfilled. However, this practice does not provide the most accurate estimate of collectability, making it difficult to assess progress in meeting fundraising goals. A best practice recommended in the accounting profession is the development of an “Allowance for Doubtful Accounts” — a contra-asset account that is associated with Accounts Receivable and is reflected as a current asset on the balance sheet. This is one way to reduce expected receivables; in this case, pledges in the financial system, to reflect a more accurate value of pledges receivable and the collectability of the pledges. The annual reductions can also
be applied to pledge amounts in the donation database in order to adjust expected pledge amounts. The development of an allowance for doubtful account policy would provide guidelines to ensure uniform accounting for the allowance of doubtful accounts and the net realizable value of pledges receivable.

We reviewed all pledges that PAHM had on record to determine total pledges recorded and noted any restrictions on these pledges. Further, we reviewed payment terms, if any, that were associated with the pledge. To the extent possible, we used historical donation information, pledge documents, or other information such as staffs’ notes, to make pledge-by-pledge assessments of the collectability of the pledges on record.

We found that of the approximately $2,948,000 in total pledges on record, $2,010,000 have restrictions from the donor and cannot be used for Phase 1 of the PAHM project. Of the remaining $937,000 that are eligible for Phase 1 use, we noted concerns about collectability for a significant portion of these funds. We rated some pledges as high risk for collectability based on lack of written or signed pledge documents and little to no donation history from the donor to show commitment to the project. Other pledges were rated high risk for collectability based on contingencies written into the pledge, such as business success of the donor or donor company. Some pledges were rated as high risk for collectability based solely on age of the pledge and age of past donations. For instance, we rated one mid-sized pledge as high risk because the pledge was made in January 2013; and the last cash donation received from the donor was in 2012.  

We found that of the $937,000 in pledges that PAHM reported as unrestricted, we determined that approximately $909,000 was available for Phase 1. Our evaluation of pledge risk for non-collection concluded that from pledges available for Phase 1, approximately $681,500 had high risk factors associated with the pledge that decreased the likelihood that PAHM will be able to collect the pledge. Although a high percentage of pledges on file do have high risk factors associated with them, this does not mean that all pledges with risk will be uncollectable. Based on this assessment, we identified approximately $242,600 in pledges that were more likely to be collectable because they were less than three years old (this could include updated pledge documents), or the donor had a strong and recent history of financially supporting the project and the pledge did not have associated financial contingencies.

Exhibit 4 below shows the age of pledges based on initial pledge date and last donor activity date. As noted previously, our risk assessment was not based solely on the age of pledges, but the age of the pledge or the last activity date was a consideration. For this assessment, “Age of Last Donor Activity” could represent the date of the most recent verbal or written confirmation of the pledge on record, a payment made towards the pledge, or a donation made separate from the pledge.

5 The Executive Director of PAHM noted that she has been actively engaging with pledge donors to try to ensure current and written documentation is on file for all pledges. Due to her active outreach and her on-going relationship with donors and pledges, we did not attempt to contact any pledge donors.

6 The $909,000 (rounded to the nearest thousand) available for Phase 1 accounts for the following adjustments; (1) $15,000 that should be written off; (2) a $10,000 restriction on a $25,000 pledge; and (3) a $3,000 grant that is a duplicate entry.
### Exhibit 4: Aging Chart for Pledges on Record, As of November 2019

<table>
<thead>
<tr>
<th>Age of Pledges in Months</th>
<th>Total Amount Pledged</th>
<th>Number of Pledges</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-12 months</td>
<td>$112,350</td>
<td>8</td>
</tr>
<tr>
<td>12.1 months-24</td>
<td>$477,000</td>
<td>11</td>
</tr>
<tr>
<td>24.1 months-48</td>
<td>$1,000</td>
<td>2</td>
</tr>
<tr>
<td>48.1 months-72</td>
<td>$1,200</td>
<td>1</td>
</tr>
<tr>
<td>72 plus months</td>
<td>$311,000</td>
<td>8</td>
</tr>
<tr>
<td>Pledge date not clear</td>
<td>$6,600</td>
<td>2</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Age of Last Donor Activity</th>
<th>Total Amount Pledged</th>
<th>Number of Pledges</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-12 months</td>
<td>$166,550</td>
<td>14</td>
</tr>
<tr>
<td>12.1 months-24</td>
<td>$597,100</td>
<td>14</td>
</tr>
<tr>
<td>24.1 months-48</td>
<td>$3,500</td>
<td>2</td>
</tr>
<tr>
<td>48.1 months-72</td>
<td>none</td>
<td>0</td>
</tr>
<tr>
<td>72 plus months</td>
<td>$142,000</td>
<td>2</td>
</tr>
</tbody>
</table>

* Last donor activity could include activity such as a donation or re-confirmation of the pledge.

Source: These tables were developed using internal records and notes maintained by the Executive Director of PAHM. Note: The pledges shown in the tables are related to pledges that are allowable for Phase 1 use.

---

During our assessment, we noted that some pledges have payment terms that include a provision that payment will commence upon or after the start of construction. Additionally, some of the pledges include payment terms that specify payments will begin after construction commences; also note that pledge fulfillment will be made in payments. Of the $909,000 we identified as pledges eligible for use in Phase 1, approximately $528,000 contained language limiting payment to “upon or after construction began.” Of the $528,000 in pledges, approximately $127,000, or 24 percent, did not have any characteristics that may make them a risk for collection.
RECOMMENDATIONS FOR BEST PRACTICES

1) PAHM should establish an operating reserve. An operating reserve is an unrestricted fund balance set aside to stabilize a nonprofit’s finances by providing a cushion against unexpected events, losses of income, and large unbudgeted expenses. The most common trigger for use of operating reserves is on the income side, such as when a previously reliable source is reduced or withdrawn. Since operating reserves are most valuable if they are reliable, an important factor in using reserves is also having a realistic plan to replenish them.

2) PAHM should incorporate into its accounting practices the guidance of GASB 33 on non-exchange transactions. This standard establishes accounting and financial reporting standards for non-exchange transactions involving financial or capital resources recognition (for example, private donations). GASB 33 provides guidance that donations be recognized as cash when they are received and that pledges should be recorded as receivables.

3) PAHM should create a comprehensive policies and procedure manual to incorporate key components to establish a control environment and to address key internal control risks. This should include accounting practices, Sarbanes-Oxley Act, general organization-level controls, information technology controls, and key internal controls such as cash management (donation and pledge collection and recording), payroll, and general accounting procedures such as reconciliations.

4) Because not all receivables will be collected, the true collectability of receivables must be determined in order to give an accurate picture of PAHM’s cash on the balance sheet. To help estimate the collectability of receivables, organizations can establish an allowance for doubtful accounts. The allowance for doubtful accounts is an account on the statement of financial position that is used to reduce the reported amount of receivables to what is expected to be collected.

To do this, PAHM should set up an accounts receivable -- pledges receivable for doubtful accounts. This account would be a contra asset to the accounts receivable and pledges receivable accounts. That means it reduces the total amount of accounts receivable. Each year, an estimate of the portion of receivables that will not be collected is recorded through a journal entry to bad debt expense.

Recommendations to the City

5) The City of Palo Alto (City) should consider an agreement as a condition of funding or at a minimum, develop some operational and performance measures to help PAHM strengthen its operations, and promote accountability and transparency. The agreement could include the following provisions:
   a. PAHM to provide to the City annually for review, a listing of all financial policies that have been approved by the board and if applicable, when the policy was last updated. Additionally, PAHM’s annual update to the City could include a copy of a procedures manual and a highlight of which position is responsible for ensuring that key internal controls are present and working.
   b. A requirement that the PAHM Board of Directors develop and approve an operating budget and an operating reserve policy that includes forecasts of cash flows based on clearly established and agreed upon assumptions, income and expense estimates, and other non-operational expenses. This policy should include working towards establishment of an operating reserve equal to 10-15% of PAHM’s operations.
   c. Annual or bi-annual reporting updates from PAHM that presents standardized information (to be compared year-to-year) including its fundraising achievements and progress made toward Phase 1 and Phase 2 project funding.
APPENDIX A - MATTERS FOR CONSIDERATION

The information contained herein is general in nature and is not intended, and should not be construed, as legal, accounting advice or opinion provided by MGO to the reader. The reader also is cautioned that this material may not be applicable to, or suitable for, the City’s or PAHM’s specific circumstances or needs. PAHM should contact their accounting or tax professional prior to taking any action based upon this information. MGO assumes no obligation to inform the reader of any other factors that could affect the information contained herein.

Section 6: Practices for Safeguarding Assets through Strong Controls

Some nonprofit organizations, such as PAHM, must rely heavily on public donations to raise funds to carry out their mission, as well as to fund itself operationally. This level of public trust requires nonprofit organizations to be held to a high standard of integrity, transparency, and accountability. As such, nonprofits must be proactive in guarding against any appearance of impropriety, misappropriation of funds, waste, or fraud. Considering nonprofits, such as PAHM, often operate on very narrow financial margins, with a mandate to invest as much of their resources as possible in achieving its mission, efficiency and control activities for operations is important for ensuring that it will meet its mission. This memo outlines the importance of these concepts and provides a general summary of areas where PAHM should pay close attention.

Since nonprofits need to safeguard assets to preserve public trust and operate efficiently, while ensuring external compliance, it is vital that nonprofit organizations have comprehensive and formalized financial policies and procedures. Policies are defined as the rules that organizations use to govern their activities. They can serve an internal purpose, such as clarifying roles and responsibilities or articulating internal principles (e.g., organizational ethics), and ensure compliance with external rules and standards, such as tax reporting requirements. Policies and procedures can also provide expectations and key guidance to staff and board members on how financial transactions are handled, and the roles and authorities of each party that are tasked with carrying out each function.

Safeguarding Assets

Strong policies can create public trust and convey integrity by ensuring the sound stewardship of organizational assets, accountability, transparency, and ethical practices. Internal controls should be incorporated into financial policies and procedures as a tool for achieving these goals. Internal controls also address risks by specifying security procedures and plans to protect against damages and loss. Internal controls can be designated into four main categories:

- **Authorization and approval** includes having a budgeting and financial planning process and plan that is followed, as well as having a system to determine and approve proper expenditures.

- **Documentation and recording** involves having proper backup for every expenditure or purchase to ensure legitimate purposes.

---

- **Security** involves both physical and electronic measures such as locking up blank checks and protecting financial data with passwords, as well as having specific procedures related to bank transactions.

Early detection involves creating checks and balances to ensure that more than one person is engaged in any financial transaction, as well as engaging independent review such as an annual external financial audit.

While there is no single standard for internal controls that nonprofits must adhere to, individual organizations can have different control structures that are customizable to their size and complexity.

Other common internal controls include measures such as having more than one person handle receipt of gifts or cash, ensuring that checks are endorsed “For deposit only” immediately upon receipt, retaining records of all expenditures with backup documentation, segregating duties such as bookkeeping from check signing so that funds cannot be misappropriated and records cannot be manipulated. Additional controls include ensuring that more than one person examines bank statements, tracking inventory consistently, instituting computer and office security, and engaging in external audits.

Sound internal controls are key to maintaining public support. Potential disclosure of internal control weaknesses is associated with a decline in public support and government contributions. Negative internal control information, “appears to affect, either directly or indirectly, …funders’ giving decisions.”8 It is estimated that organizations with internal control problems receive 3.8 percent less public support and 2.1 percent less government support.

While engaging an external auditing firm for annual review is a key way to provide accountability and transparency to the public, nonprofits with revenues under $2M are not required to have an external audit, so internal controls formalized in written policies and procedures is key to develop a culture of compliance.

**Internal Controls Provide for Sound Management**

Internal controls are policies and procedures that protect the assets of an organization, create reliable financial reporting, promote compliance with laws and regulations, and facilitate effective and efficient operations. They relate to accounting, reporting, and the organization’s communication processes.9 A policies and procedures manual should specify how financial planning will be conducted, what kind of financial reports will routinely be produced and distributed, and how other routine tasks will be carried out. The ability to make sound financial plans in the form of budgets and then generate timely and accurate financial reports to measure performance is a key element of creating organizational efficiency. Accurate reports facilitate tracking of income and expenses so that board members and managers understand how their activities are being carried out and can make adjustments in response to trends and ensure mission alignment. Accurate reports also facilitate timely external reporting to comply with grantor or government guidelines, a key element of maintaining continued support and credibility.

In addition, procedures ensure efficiency at a basic level simply by stating how routine tasks will be completed. If there are no written procedures, employees are at risk for making their own rules, or will have to create a new method or system every time they need to complete a task such as recording income or paying a check, which is inefficient. Without any standard process for completing and tracking tasks, certain reports on past activities would be difficult to generate because information or data may have been generated and entered inconsistently.

---

Ensuring Compliance with External Regulations and Standards

Financial policies and procedures can incorporate the key practices needed to ensure compliance with minimum legal and regulatory requirements and accepted accounting standards. The primary external regulations affecting nonprofit organizations are the IRS Form 990; the Sarbanes-Oxley Act; and the accounting standards set forth by the Financial Accounting Standards Board (FASB), the American Institute of Certified Public Accountants (AICPA), and the U.S. Federal Office of Management and Budget (OMB).

In addition, the Governmental Accounting Standards Board (GASB) issued Statement No. 33, which addresses reporting certain nonexchange transactions. Nonexchange transactions are typically described as taxes, fines, and certain grants; however, this standard also provides guidance on recognizing promises made by private donors (pledges). The standard provides guidance on the timing and recognition of voluntary nonexchange transactions, such as pledges to not-for-profits and when they should be recognized as cash or when they should be recorded as receivables. Appendix D of that standard also provides illustrative examples of recording pledges with and without restrictions. Generally speaking, the standard recommends that the exchange be recorded as revenue when the cash is received and the pledge be recorded as a receivable.

IRS Form 990

The IRS Form 990 is intended to provide transparency and accountability to the public and ensure that nonprofit organizations are fulfilling their tax-exempt purposes. As the annual return that most federally tax-exempt nonprofit organizations must file annually with the IRS, it captures basic financial information and includes a series of questions related to governance and organizational policy. Since 2009 for the 2008 tax year, additional disclosures relating to items such as accountability, governance, and fraud prevention have been added as a required reportable. The form includes questions on policies related to conflict of interest, executive compensation, decision-making, and whistleblower protections, among others.\(^{10}\)

According to the IRS (2011), the purpose for these additional governance and accountability questions is to "help ensure that the organization’s assets will be used consistently with its exempt purposes."\(^{11}\) In addition, the IRS states, "well-governed and well-managed organizations are more likely to be transparent with regard to their operations, finances, fundraising practices, and use of assets for exempt and unrelated purposes."\(^{12}\) Thus, while many of the governance policies asked about on the Form 990 may not be required, the request for disclosure can help the public distinguish organizations who have such policies in place from those who do not, to help identify which organizations may be more transparent, accountable, and well run.

Sarbanes-Oxley Act

The Sarbanes-Oxley Act (Act) was passed in 2002 to rebuild public trust in the wake of corporate accounting scandals. It created new standards for governance, financial transactions, and audit procedures in publicly traded companies. Although most of the Act’s provisions apply only to publicly traded companies, many organizations in the nonprofit sector have adopted the recommended standards in anticipation of future legislation. BoardSource and Independent Sector have made recommendations on how charities and foundations can voluntarily incorporate certain provisions of the Act into their

---


operations in their publication, The Sarbanes-Oxley Act and Implications for Nonprofits. They include recommendations related to managing conflicts of interest, external audits, certification of financial statements such as the IRS Form 990, disclosure, whistleblower protection, and document destruction.

Importantly, two provisions of the Act apply to all entities, including nonprofit organizations, because they are amendments to the federal criminal code: the whistleblower policy and the document destruction policy. Therefore, among other recommendations, these two provisions should be included in any financial policies and procedures manual.

**Professional Standards – FASB, AICPA, and OMB**

There are three entities that issue standards for nonprofit financial accounting: the Financial Accounting Standards Board (FASB), the American Institute of Certified Public Accountants (AICPA), and the U.S. Federal Office of Management and Budget (OMB) (for organizations that receive federal grants). These standards are what auditors and other regulators use when assessing the appropriateness of a nonprofit organization’s financial accounting. FASB and AICPA standards together form what are called generally accepted accounting principles (GAAP), principles and standards that govern the preparation of financial reports.

FASB has issued only a small number of standards specific to nonprofit organizations, but they are important. FASB No. 116, “Accounting for Contributions Received and Contributions Made,” requires nonprofits to record contributions according to whether they increase permanently restricted net assets, temporarily restricted net assets, or unrestricted net assets. FASB No. 117, “Financial Statements of Not-For-Profit Organizations,” sets standards for external financial statements, including that all nonprofit organizations provide a statement of financial position, a statement of activities, and a statement of cash flows. It also requires nonprofit organizations to classify expenses by “functional expense categories” (program services, management and general, and fundraising, at a minimum).

The AICPA’s Statement of Auditing Standards 115 (known as SAS 115) was instituted in 2009 and emphasizes that management staff are responsible for establishing and maintaining internal controls. It further requires external auditors to convey in writing any control deficiencies or material weaknesses that they observe to be present in the course of their audit. This increased level of transparency about deficiencies in internal controls should create an impetus for nonprofit organizations to improve their internal controls in the interest of having a “clean” management letter attached to their audit.

Nonprofit organizations must ensure that they are following GAAP as laid out by these entities to ensure public trust. Financial policies and procedures should indicate an organization’s compliance with GAAP and should create systems to ensure that GAAP recommendations are followed.

---


14 PAHM enacted a Whistleblower policy and a document retention and destruction policy in 2019.
Honorable Mayor and Council Members

Reference Item 2, December 17, 2018

As Council considers the staff recommendation of an extension of the agreement with the Palo Alto History Museum, I would like to suggest consideration of the allocation of the $665,000 funds raised by the sale of the TDR funds made available through Environmental Volunteers.

EV continues to make effective and efficient use of the City owned EcoCenter. The EcoCenter houses a small staff, equipment used for classroom and outdoor education, and meeting center. It hosts environmental home-school classes, meetings and EV training. EV works in close cooperation with the Baylands rangers and in a few weeks EV will co-host a king-tide event with the city.

Originally Environmental Volunteers was awarded only $300,000 of the $965,000 sale of TDR benefits. At the time EV misspoke, saying and incremental funds would simply be used for operating costs including maintenance. EV previously used funds raised for operating to complete the reconstruction and now has further capital improvement projects for the EcoCenter. Under its new ED, Elliott Wright, EV is successfully focused on generating the needed operating funds.

I would like to ask for the Council’s consideration of allocating 10% of the $665,000 EV-generated TDR funds to Environmental Volunteers when and if the funds become available. Or please explore alternative sources for this purpose.

Thank you for your consideration of support for this valuable community resource.

Don McDougall
Palo Alto resident
650 815 1455

This letter is submitted as a resident, not as a representative of Environmental Volunteers. A copy is attached.
February 27, 2020

TO: City Council
FR: Laura Bajuk, ED
RE: Museum on City Council Agenda for March 2, 2020

Thank you to you and your hard-working staff for the opportunity to update you on the Museum project, our current status, and thoughts on moving forward.

We last appeared before Council on December 11, 2017, where Council unanimously accepted a “carrot and stick” approach. We were challenged to raise $1.75 million in just over a year. If we proved we could raise the funds, we could gain additional funds from the Sea Scout TDR sale. If we didn’t meet the challenge goal, City staff could be directed to release a new RFP to develop the Roth Building.

The carrot won - we exceeded the City challenge. Since that time, we have:

- Seen the Sea Scout TDR funds allocated by the City and received a County grant (payable to the City) for $102,992.00 towards the Roth rehabilitation,
- Added seven dynamic new board members (just over half the board) and critical policies such as whistleblower and document retention policies,
- Pulled our building permit, are keeping it active and are maintaining our 2016 contract with Vance Brown,
- Updated our fundraising materials, created a corporate campaign, and are working on a more effective web site,
- Controlled expenses tightly, have seen increased annual revenue, and have held about a million dollars in our bank and investment accounts (for the first time in our history) and have maintained that despite regular expenses.

Meeting the City challenge triggered the verification by MGO. While not a full audit, it was a comprehensive, in-depth review of our financial and fundraising history since the project began. The process was positive and all professionals involved were efficient and cooperative. The process drew out how our increasing professionalism over time has improved operations; we continue to make recommended improvements. That brings us to the present.

As you are well aware, regional construction costs continue to escalate. Our not-to-exceed contract with Vance Brown (2016) is stretched to its limit, and sub-contractor estimates are rising. A review of potential expenses, undertaken recently at the request of City staff, shows that the margin to construction has increased substantially due to regional pressures.

Our shared goal is to develop a museum that will enrich this community, and we appreciate your ongoing support. Clearly, the rehabilitation costs are a financial challenge. We are open to all reasonable opportunities to achieve this goal, and ask that you direct staff to explore such options with the Museum board and staff.

Thank you for your consideration, and for the aid of City staff who are part of this process. We are very grateful for your support.

Laura Bajuk, Executive Director