



Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Toni J. Taber, CMC
City Clerk

A handwritten signature in blue ink, appearing to read "Toni J. Taber", is placed over the printed name and title of the City Clerk.

SUBJECT: SEE BELOW

DATE: December 3, 2024

SUBJECT: Team San José and Convention and Visitors Annual Performance Audit

Recommendation

As recommended by the Community and Economic Development Committee on November 18, 2024, accept the report on the annual performance of Team San José and Convention and Visitors audit.

CEQA: Not a Project, File No. PP17-009, Staff Reports, Assessments, Annual Reports, and Informational Memos that involve no approvals of any City action. (City Auditor)
[Community and Economic Development Committee referral 11/18/2024 - Item (d)1]



Office of the City Auditor

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

**TEAM SAN JOSE
PERFORMANCE FY 2023-24**

**Report 24-07
November 2024**

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November 7, 2024

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

Team San Jose Performance FY 2023-24

Since 2004, Team San Jose, Inc. (TSJ) has operated the San José McEnery Convention Center and several other City-owned facilities on behalf of the City. Additionally, since 2009, TSJ has operated the San José Convention and Visitors Bureau (CVB). Under the terms of the management agreements between the City and TSJ, the City Auditor's Office is required to perform an annual performance audit to determine whether TSJ achieved agreed-upon performance targets. These targets are the basis for an incentive payment from the City.

Finding I: Team San Jose Exceeded Its Weighted Incentive Fee Score and CVB Performance Targets

In Fiscal Year (FY) 2023-24, Team San Jose:

- Exceeded its target in gross operating results,
- Booked 121,800 hotel room nights,
- Had an estimated economic impact of nearly \$76 million,
- Held 545 days of events at its cultural facilities, and
- Received 100 percent satisfaction ratings on its customer service surveys.

Overall, Team San Jose met its weighted incentive fee targets and qualifies for the incentive fee of \$250,000.

We plan to present this report at the November 18, 2024 meeting of the Community and Economic Development Committee of the City Council. We would like to thank Team San Jose and the City Manager's Office for their time and insight during the audit process.

Respectfully submitted,



Joe Rois
City Auditor

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This report is also available online at www.sanjoseca.gov/audits

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Background

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

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

The Convention Center and South Hall generally host trade shows, conventions, corporate meetings, social events, and consumer shows. The Cultural Facilities generally host performing arts, concerts, and events.

Team San Jose, Inc. (TSJ), a public benefit corporation, manages the facilities on behalf of the City. The City's agreements for TSJ's management of the facilities requires the City Auditor's Office conduct an annual audit to assess TSJ's performance using agreed upon performance measures.

Team San Jose Has Managed the Facilities Since 2004

TSJ was formed in 2003 in response to the City's request for proposal for the management and operation of the Convention Center.¹ The City entered into a Management Agreement with TSJ in 2004, and subsequent agreements in 2009 and 2014. In July 2019, the City and TSJ used the first option to extend the 2014 Agreement to June 30, 2024. In July 2024, the City and TSJ used the second and final option to extend the 2014 Agreement to June 30, 2029.²

The City and TSJ also have an agreement under which TSJ provides Convention and Visitors Bureau (CVB) services on behalf of the City, including tourism and marketing, public relations, and convention sales and services. TSJ has been providing CVB services since 2009.

¹ TSJ has a 19-member Board of Directors that includes representatives from local hotels, arts, business, and labor groups. It also includes two non-voting City members, represented by one City Councilmember and one member from the City Manager's Office. TSJ reports one open voting seat on its Board of Directors.

² For the final five-year option term beginning July 1, 2024, the Fixed Management Fee was recommended to be renamed to Fixed Minimum Guarantee of Funding, and the Incentive Fee renamed to the Performance-Based Fee.

Exhibit I: Team San Jose Managed Facilities

San José McEnery Convention Center



California Theatre



San Jose Civic



Center for Performing Arts



Montgomery Theater



Source: Team San Jose, Inc.

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

The Management Agreement requires that the City pay TSJ a fixed Management Fee of \$1 million per year “to provide, without limitation, for payment of a portion of the expenses incurred by TSJ for the management of the operations and maintenance of the City's Facilities, as determined by the TSJ Board of Directors.” If certain performance targets are met, the City also pays TSJ a \$250,000 incentive fee.

Under the Management Agreement, TSJ proposes performance targets, and then the City reviews and approves them. The Agreement requires the City to approve targets prior to the beginning of each fiscal year.³ The fiscal year (FY) 2023-24 targets were approved during the budget process in a Manager’s Budget Addendum.⁴

The Management Agreement outlines five measures that track TSJ’s overall economic impact, financial results, theater occupancy, and customer survey results. For each measure, the weighted percent is calculated by taking the percent of the target achieved multiplied by the assigned percentage. The sum of these measures equals the weighted incentive fee score. The incentive fee is granted if the weighted incentive fee score reaches 100 percent or more.

Exhibit 2: Incentive Fee Measures and Their Weighting

Incentive Fee Measures	
Gross Operating Results	40%
Economic Impact	40%
Hotel Room Nights (20%)	
Estimated Economic Impact (20%)	
Theater	10%
Theater Occupancy (10%)	
Customer Satisfaction	10%
Total	100%

Source: Management Agreement between the City and Team San Jose.

The Management Agreement allows for adjustments to the performance measures if hotel tax revenues change by 15 percent above or below the amount forecasted in the City’s Adopted Operating Budget.⁵ If this happens, the Management Agreement states that “the performance measures for the subject operating year

³ During the September 2024 TSJ Semi-Annual Update to the Community and Economic Development Committee, the Budget Office explained that performance targets should represent feasible markers of performance within expected market conditions. The fund is negatively impacted if performance targets are not met.

⁴ The Manager’s Budget Addendum for TSJ’s FY 2023-24 targets can be found at <https://www.sanjoseca.gov/home/showpublisheddocument/98752/638210616401570000>

⁵ For FYs 2019-20 and 2020-21, hotel tax revenues were below expectations by more than 15 percent, and the City adjusted performance targets accordingly.

may be concurrently adjusted commensurate with the additional or reduced funding.”

Performance Measures for the Convention and Visitors’ Bureau Agreement

Additionally, the agreement for management of the CVB outlines two measures that evaluate their performance. Each measure has a weight of 50 percent. These are:

- **Hotel Room Nights:** The same measure that is used in the incentive fee score, this measure is calculated based on the total number of hotel room nights sold by the CVB in the fiscal year and the total number of hotel room nights sold that can be directly or indirectly attributed to activities at the Convention Center and cultural facilities.
- **Direct Visitor Spending:** Calculated in the same manner as estimated economic impact, this measure is based on the spending activity estimated to be generated based on daily attendance at the events held at the Convention Center and cultural facilities.

The City Auditor’s Office has audited TSJ’s performance annually since 2005. We have issued 18 reports with 39 recommendations in total. Each of those recommendations has since been implemented.

Finding I Team San Jose Exceeded Its Weighted Incentive Fee Score and CVB Performance Targets

Summary

In FY 2023-24, TSJ:

- Exceeded its target gross operating results,
- Booked 121,800 hotel room nights,
- Had an estimated economic impact of nearly \$76 million,
- Held 545 days of events at its cultural facilities, and
- Received 100 percent satisfaction ratings on its customer service surveys.

Overall, Team San Jose exceeded its weighted incentive fee score of more than 100 percent. Team San Jose thus qualifies for the incentive fee of \$250,000.

Exhibit 3: Weighted Incentive Fee Score for the Convention and Cultural Facilities

Measures	Target	Actual	% of Target Achieved	Weighted Incentive Fee Score Percentage
Gross Operating Results (40%)	\$1,539,363	\$5,691,188	370%	148%
Hotel Nights (20%)	112,000	121,835	109%	22%
Estimated Economic Impact (20%)	\$55,108,300	\$75,560,244	137%	27%
Theater Occupancy (10%)	91%	94%	103%	10%
Satisfaction Rate (10%)	95%	100%	105%	11%
Total Weighted Incentive Fee Score				218%

Source: Auditor analysis of data from Team San Jose, audited financial statements for the San José Convention and Cultural Facilities, agreements between the City and Team San Jose, and Mayor’s Budget Addendum performance targets.

Further, TSJ’s performance exceeded its targets for its agreement with the Convention and Visitor’s Bureau.

Exhibit 4: Weighted Performance Score for the Convention Visitor’s Bureau

Measures	Target	Actual	% of Target Achieved	Weighted Performance Score Percentage
Hotel Nights (50%)	112,000	121,835	109%	54%
Direct Visitor Spending (50%)	\$55,108,300	\$75,560,244	137%	69%
Total Weighted Incentive Fee Score				123%

Source: Auditor analysis of data from Team San Jose, agreements between the City and Team San Jose, and Mayor’s Budget Addendum performance targets.

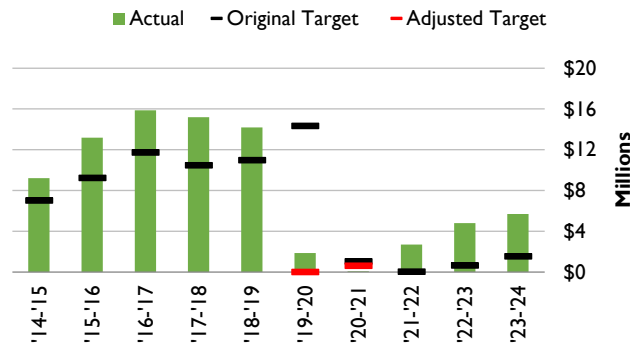
Gross Operating Results – 370% of Target

The Management Agreement defines gross operating results as gross revenues from operating the Facilities, plus hotel tax revenue, plus revenue from the parking garage at the Convention Center, minus certain direct and indirect expenses for operating the Facilities.⁶

For FY 2023-24, TSJ achieved gross operating results of \$5.7 million, compared to a target of \$1.5 million. The actual results were more than three times greater than the target. In its Semi-Annual Update to the City Council’s Community and Economic Development Committee in September 2024, TSJ noted that an increased scope for one large event and several short-term corporate opportunities led to them exceeding their goal.

While gross operating results have improved since FY 2019-20, they have not recovered to pre-COVID levels.

Exhibit 5: Gross Operating Results



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

Note: As described in the Background, targets for FYs 2019-20 and 2020-21 were adjusted due to hotel tax revenues being below expectations.

⁶ The calculation does not include City-directed expenses, including City oversight, fire insurance premiums, emergency capital repairs and maintenance, depreciation, and the management fee paid by the City to TSJ.

The Financial Statements Show an Operating Loss

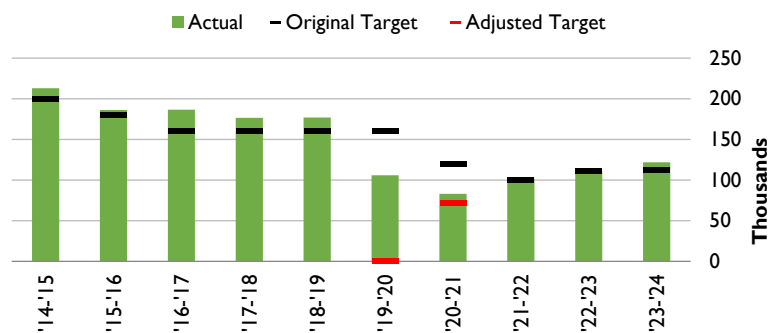
While TSJ exceeded its gross operating results measure, the audited financial statements for the Convention and Cultural Facilities show an operating loss of about \$11.1 million in FY 2023-24. Ongoing subsidies from hotel taxes and parking garage revenue cover this loss. Appendix B reconciles the audited financial statements to the Management Agreement’s definition of gross operating revenue.

Hotel Room Nights – 109% of Target

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

As shown in Exhibit 6, TSJ met its hotel night target or adjusted target in each of the last ten years. In FY 2023-24, the hotel room nights booked were above the target—121,835 hotel room nights were booked compared to a target of 112,000 nights. This was 109 percent of the target. While future hotel room nights have improved since FY 2019-20, they have not recovered to pre-COVID levels.

Exhibit 6: Future Hotel Room Nights Booked



Source: Auditor analysis of the Management Agreement and its amendment, TSJ’s hotel room night’s production report, and our prior TSJ audits.

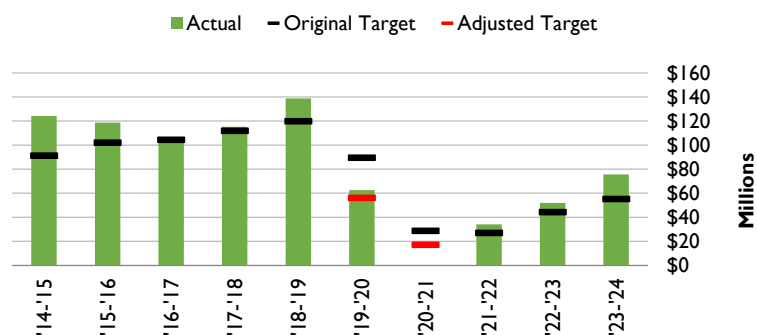
This measure is also used to determine performance of TSJ for CVB services.

Estimated Economic Impact – 137% of Target

Estimated economic impact is calculated by multiplying an agreed upon average daily spending rate by event attendance and duration. Average daily spending rates vary depending on event type (e.g., conventions, meetings, performing arts, sporting events) and attendee type (e.g., local/social visitors, out-of-town visitors, and exhibitors). Event attendance and the assumed spending rates drive this measure.

As shown in Exhibit 7, in FY 2023-24, the estimated economic impact was above the target—\$75.6 million in estimated economic impact compared to a target of \$55.1 million. This was 137 percent of the target. While TSJ’s estimated economic impact has improved since FY 2019-20, it has yet to return to pre-pandemic levels.

Exhibit 7: Estimated Economic Impact



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

This measure, also referred to as Direct Visitor Spending, is also used to determine TSJ’s performance for CVB services.

The five events with the highest estimated economic impact contributed 37 percent towards TSJ’s estimated economic impact (\$28.1 million). These events, in alphabetical order, included:

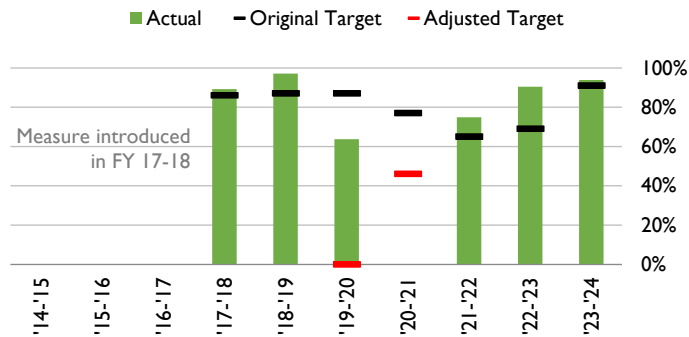
- 2023 US Gymnastics National Congress & Tradeshow
- Bruhan Maharashtra Mandal of North America 2024
- Display Week 2024
- FanimeCon 2024
- NVIDIA GTC AI Conference 2024

Theater Occupancy – 103% of Target

Theater occupancy is measured by the number of occupancy days, divided by available days at the four Cultural Facilities (San Jose Civic, Center for the Performing Arts, California Theatre, and Montgomery Theater).⁷ This includes dance productions, concerts, musicals, and comedy shows, speakers, and other performances generally available for the public.

The City’s Cultural Facilities were occupied on 545 of 581 available use days (94 percent). This was 103 percent of the target. The number of occupied and available use days has increased since FY 2019-20 and exceeded pre-COVID levels. For example, in FY 2018-19, Cultural Facilities were occupied for 540 out of 556 available days. Additionally, there were 238 event bookings in FY 2023-24, higher than the 232 bookings in FY 2018-19.

Exhibit 8: Theater Occupancy



Source: Auditor analysis of the Management Agreement and its amendment, TSJ’s theater occupancy records, and prior TSJ audits.

The California Theatre was occupied for the most days (170), followed by the City National Civic (148), the Center for Performing Arts (118), and the Montgomery Theater (109).

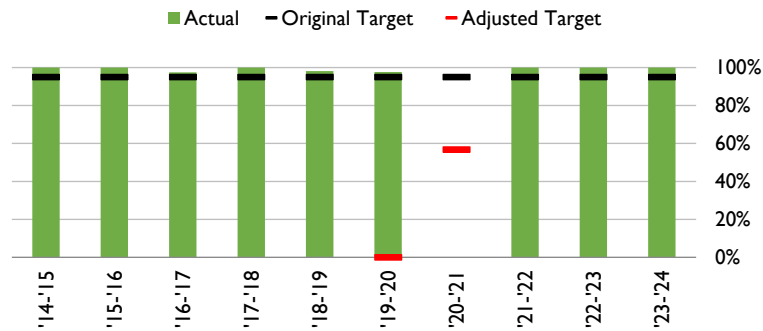
⁷ The Management Agreement defines available days as: (a) the number of Thursdays, Fridays, and Saturdays within a fiscal year, minus (b) any such days that fall within a United States holiday period, and minus any such days that are blocked-out for facility repairs.

Customer Satisfaction – 105% of Target

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

In FY 2023-24, customer satisfaction was above the target – 100 percent customer satisfaction compared to a target of 95 percent.⁸ This was 105 percent of the target.

Exhibit 9: Customer Satisfaction



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

⁸ We reviewed the accuracy of the reported survey results by matching a sample of actual customer survey responses to the reported results for FY 2023-24. There were 57 respondents for the customer satisfaction survey from a total of 204 reported non-resident partner events, or a 28 percent response rate.

Conclusion

Team San Jose (TSJ) exceeded its weighted incentive fee score as well as its CVB performance targets for FY 2023-24. In FY 2023-24, TSJ:

- Exceeded its target in gross operating results,
- Booked 121,800 hotel room nights,
- Had an estimated economic impact of nearly \$76 million,
- Held 545 days of events at its cultural facilities, and
- Received 100 percent satisfaction ratings on its customer service surveys.

Overall, Team San Jose met its weighted incentive fee targets and qualifies for the incentive fee of \$250,000.

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APPENDIX A

Audit Objective, Scope, and Methodology

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

In accordance with the City Auditor's Fiscal Year (FY) 2024-25 Audit Work Plan, we have completed an audit of Team San Jose, Inc.'s (TSJ) management of the City's Convention and Cultural Facilities and the Convention and Visitors Bureau. The objective of this audit was to determine whether Team San Jose met their incentive fee measures and performance measures specified in the *First Amendment to the Agreement for the Management of the San José Convention Center and Cultural Facilities between the City of San José and Team San Jose* and the *Agreement for Convention and Visitors Bureau Services between the City of San José and Team San Jose* for FY 2023-24.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We sought to understand the relevant internal controls over TSJ's performance reporting. We did not review internal controls over all TSJ operations. To achieve our audit objectives, we have performed the following:

- To understand agreed upon performance measures and targets, we reviewed:
 - The 2014 Management Agreement, the 2018 First Amendment to the Management Agreement, the 2019 Second Amendment to the Management Agreement, and the 2024 Third Amendment to the Management Agreement,
 - The 2014 Convention and Visitors Bureau Services Agreement, the 2019 First Amendment to the Convention and Visitors Bureau Services Agreement, and the 2024 Second Amendment to the Convention and Visitors Bureau Services Agreement,
 - Council-adopted performance targets from Manager's Budget Addendum #33, dated May 29, 2023.
- To understand TSJ's performance and activity for FY 2023-24, we reviewed:
 - TSJ's performance reports to the City Council's Community and Economic Development Committee,

- The FY 2023-24 audited financial statement for the Facilities,⁹
- Budget Office Source and Use reports for the Convention and Cultural Affairs Fund (Fund 536), the Convention and Cultural Affairs Capital Fund (Fund 560), the Transient Occupancy Tax (TOT) Fund (Fund 461), the Convention Center Facilities District Revenue Fund (Fund 791),
- Internal TSJ reports, including an income statement (unaudited) for the Convention and Cultural Facilities Division and a parking garage revenue and expense report, and
- Discussed performance measures and TSJ's accomplishments for the fiscal year with management and staff from TSJ, the City Manager's Office of Economic Development and Cultural Affairs, and the Budget Office.
- To test the accuracy and completeness of performance reports and whether TSJ met agreed upon performance targets, we:
 - Reviewed TSJ's reported activity for estimated economic impact, theater occupancy, and customer service surveys, and hotel-room night bookings.
 - On a sample basis, tested the accuracy and completeness of TSJ's recording of the number of theater occupancy days for theaters, estimated economic impact based on event attendance, customer service survey results, and hotel room nights booked during the year.
 - Assessed the accuracy of TSJ's computation of gross operating results using the audited financial statements for FY 2023-24 and the agreed upon methodology in the Amendment to the Management Agreement.

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

⁹ The financial audit of the City's Convention and Cultural Facilities, by the independent accounting firm of Macias Gini and O'Connell was completed in September 2024.

APPENDIX B

Reconciliation of Management Agreement Performance Measure of Gross Operating Results to the Audited Financial Statements

	Audited Financial Statements	Adjustments for Gross Operating Results per Management Agreement	
Operating Revenues:			
Building rental	\$ 5,882,207		
Food and beverage services	\$ 20,404,592		
Commission revenue	\$ 786,377		
Event electrical/utility services	\$ 740,772		
Networking Services	\$ 1,135,884		
Audio/visual services	\$ 454,626		
Ticketing services	\$ 1,092,750		
Telecommunications services	\$ 105,764		
Equipment rentals	\$ 140,985		
Event production labor revenues	\$ 11,690,344		
Rigging Assessment Fee	\$ 320,437		
Other	\$ 603,759		
Revenues			
Bad Debt Expense		(2,686)	A
Total Operating Revenues	\$ 43,358,497		
<i>Transient Occupancy Tax revenue to Convention and Cultural Affairs Fund</i>		\$ 11,635,004	A,B
<i>Parking garage revenue</i>		\$ 4,132,457	A
Revenues for gross operating results calculation		\$ 59,123,272	
Operating Expenses:			
Administrative and general salaries – TSJ	\$ 23,909,410		
Cost of event production labor	\$ 9,944,775		
Utilities	\$ 4,504,487		
Food and beverage costs	\$ 3,287,320		
Bad debt expense	\$ 2,686	\$ (2,686)	A
Contracted outside services	\$ 4,013,862		
Professional services	\$ 271,689		
Operating supplies	\$ 876,235		
Depreciation	\$ 13,495	\$ (13,495)	A
Repairs and maintenance	\$ 1,764,791		
Insurance	\$ 625,618		
City of San José oversight	\$ 733,374	\$ (733,374)	A
Ticketing costs	\$ 63,162		
Workers' compensation insurance premiums	\$ 653,210		
Fire insurance	\$ 450,508	\$ (450,508)	A
Management fee – Team San Jose	\$ 1,250,000	\$ (1,250,000)	A,C
Equipment rentals	\$ 97,760		
City of San José facility usage (City Free Use)	\$ 22,725	\$ (22,725)	A
Other expenses	\$ 1,992,289		
Total Operating Expenses	\$ 54,477,396		
<i>CVB expenses paid by Convention and Cultural Affairs Fund</i>		\$ 0	A
<i>Less: City Worker's Compensation</i>		\$ 0	A
<i>Parking garage expenses</i>		\$ 1,427,476	A
Expenses for gross operating results calculation		\$ 53,432,084	
Gross Operating Profit or (Loss)	\$ (11,118,899)	\$ 5,691,188	

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

Notes to Appendix B:

- A. The Management Agreement defines gross operating results to include or exclude these items.
- B. The Transient Occupancy Tax revenues of \$11,635,004 allocated to the Convention and Cultural Affairs Fund in 2023-24 reflect a transfer of \$11,706,778 from the Transient Occupant Tax Fund plus a reduction of \$71,774 to reconcile the difference between the budgeted estimate for Transient Occupancy Tax revenues and the actual revenue performance in 2023-24.
- C. The management fee shown here includes the \$1 million management fee for FY 2022-23, and the \$250,000 incentive fee paid for FY 2022-23 under the Management Agreement.