REDEVELOPMENT AGENCY AND THE CITY OF OAKLAND

AGENDA REPORT

TO: Office of the City/Agency Administrator
ATTN: Deanna J. Santana
FROM: Community and Economic Development Agency
DATE: January 24, 2012

RE: Informational Report on the Fox Theater Renovation Project Performance Audit

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SUMMARY

This report provides a status report on the implementation of the recommendations from the Fox Theater performance audit and includes the October 4, 2011 Fox Theater Renovation Project Performance Audit from the City Auditor's Office ("Fox Audit" or "Audit") and the City Administration's October 5, 2011 response to the Fox Audit ("City Administration Response").

FISCAL IMPACT

This is an informational report and does not authorize any action with a fiscal impact. As part of the close-out process for the Fox Theater project, the City Administration asked for the Audit. Staff follow-up work based upon some of the issues identified by the Audit may result in recovery of some funds to the Oakland Redevelopment Agency ("Agency"). The exact amount the Agency may recover has not been determined.

BACKGROUND

In late 2009, the City Administration requested an outside audit in order to provide a thorough, independent performance management audit on the Fox Theater Project, and to identify any outstanding issues. On January 2010, the Agency Board directed staff to request that the City Auditor perform the audit.

From the project conceptual phases to completion, staff has on no fewer than fifteen occasions sought guidance from the Agency Board and/or City Council. The full list of reports and action items is included in the Chronology of Fox Theater Council Reports in the City Administration Response.

The Fox Theatre Project was funded by redevelopment funds, private investment, and federal and state grants. The City/General Fund provided no funding for this project.

The nationally acclaimed Fox Theater renovation was a highly successful project that is serving as a centerpiece for revitahzation of an area that had fallen into serious blight and disrepair. The

Fox Theater has spurred economic development, dynamic growth and new revenues to Oakland—as it was intended when originally conceived in 2001. Earlier this year the *New York Times* named Oakland as the #5 destination on its list of the Top Places to Visit in 2012 in the entire world, between London and Tokyo on this prestigious ranking. The Fox Theater was cited as a linchpin of the revitahzation which made this acclaim possible.

As common with similar complex and historic renovation projects, the Fox renovation involved design and development stages. The Fox project required Agency staff and partners to successfully leverage public dollars with private dollars; coordinate multiple funding sources and partners; and plan for the theaters eventual tenants.

As demonstrated by the Administration's request for outside review, the Redevelopment Agency and City of Oakland acknowledge the importance of and commitment to transparency and accountability through independent verification; analysis and feedback on cost-control measures, project delivery and contracting processes; internal controls to assure accountability; and continuous evaluation and improvement of management policies and practices.

CITY AUDITOR'S AUDIT AND CITY ADMINISTRATION RESPONSE

The Audit report (***Attachment A***) contains 17 recommendations. These recommendations were summarized in four broad categories or chapters:

1) Fox Theater Project Scope And Cost Increased By 172 Percent Or $58 Million From Initial Inception To Final Construction;
2) Agency Justitied Awarding Contracts On A Sole Source Non-Competitive Basis By Requiring LBE And SLBE Subcontractor Participation Goals Be Established At Higher Than Normal Levels. However, LBE And SLBE Participation Goals Were Not Achieved;
3) Inadequate Project Organizational Structure And Contract Oversight And Administration By Agency Resulted In Payments Exceeding Contract Authorized Amounts And Overpayment Of Contractor Costs; and
4) The Financial Feasibility Analysis Performed By Agency Was Inadequate For The Scope Of The Project Resulting In Under Estimating The Financial Needs Of The Project

In those areas of the Fox Audit in which the Administration is in agreement, pro-active corrective plans are being developed. However, the Administration is not in full agreement with all the audit findings and recommendations. Specitically:

1. Final Project Cost Came in 8% Below Projections
   - The Auditor's conclusion that project costs "skyrocketed" by 172% is incorrect and misleading. When the 2001 estimated full renovation cost is adjusted for inflation, the actual cost at completion in 2008 would have been $98.3 million, 8% below actual costs, not 172% above cost as stated in the Audit.

- The Audit Report inaccurately characterizes the renovation project cost as increasing by 172 percent because it compares the cost of the initial phase of the project ($33 million) to the cost of the full historic restoration ($91 million), an "apples-to-oranges" comparison.

- The estimate of $33 million noted in the Audit was for the initial phase of the project. At the time that Council approved the initial phase, funds were not identified for the entire project. When construction began in 2006, full funding was in place for the complete historic renovation of the project as originally envisioned, for a total project cost of $91 million.

- After factoring in pre-development costs and the impact of inflation related to the costs of concrete and steel, which had skyrocketed during the national construction boom in the early-mid 2000's, tinal project costs were lower than originally estimated in 2003. Adjusted for inflation, the actual cost at completion of the project would have been $98.3 million; the tinal cost of the project, at $91 million, was 8% below projections, not 172% above projections as stated in the Audit.

2. **Hiring Goals and Competitive Bidding:** The project nearly doubled the City's Small/Local Business Enterprise participation, and met Council requirements and Federal regulations
   - Council agreed that the project should waive competitive procurement requirements in order to maintain strict project schedules and increase Small/Local Business Enterprise (S/LBE) participation levels.

   - The Fox Theater project achieved 37% S/LBE participation:
     - nearly double the City's requirement of 20%
     - much greater than the Citywide S/LBE participation rate for large projects of 29%
     - exceeded the citywide S/LBE participation rate of 36%

3. The Auditor's report fails to recognize the fact that the Fox Theater project was consistent with the comprehensive vision of Council, which was stated in 2001 and reaftirmed in 2003 and 2004, for the full historic restoration of the Fox Theater (as detined in Resolution No. 2003-82 C.M.S.).

4. The Council was informed and engaged on the status and progress of the project. From the initial planning phase through the project completion, the Council was presented with numerous reports and/or approved resolutions on more than 14 occasions, including several supplemental reports when the Council requested additional information.

5. Best practices in administration and oversight were performed on the project. The project was monitored with four different independent layers of oversight on the contracts, which included oversight by: Redevelopment Agency Staff, the project manager, the contractor, the architect, and Bank of America's construction monitor. The Audit

identified two instances of possible overpayment to two contractors that require further follow-up and analysis by the Administration.

It appears that the Audit did not acknowledge all of the documentation provided with respect to the financial feasibility study conducted. The Administration provided the Auditor with more than 2,400 pages of financial closing documents consisting of loan documents, financial projections, operafing agreements, the disposition and development agreement, and formation documents of the various entities of the Project. These documents provided the financial framework for the project and were instrumental in leveraging the Project's Redevelopment Agency funds with private funding, resulting in outside alternative financial sources that totaled over $45 million.

Status of Fox Audit Recommendations

Several of the Audit recommendations required additional research including review by outside counsel and discussions with California Capital Group ("CCG"), the fee developer for the project, and Turner Construcfion Company ("Turner"), the contractor for the project. The City Administrator sent a letter to Fox Oakland Theater, Inc. (FOT) requesting analysis of four legal and accounting issues raised in the Audit, including:

- Unsupported costs of $178,726 paid to CCG. (Audit pp. 23-4).
- Overpayment of fees to CCG totaling $178,843. (Audit pp. 24-5).
- Possible refunds from Turner due to potential costs being less than budgeted for Turner's Guaranteed Maximum Price (GMP) contract. (Audit pp. 25-6).
- The Fox Theater Landlord, LLC (FTLL) may have overpaid for some change orders. In particular, some of the labor for some change orders may have been over-priced. (Audit pp. 26-7).

FOT has completed research on one of the items and has presented this information to the Auditor and the City for confirmation. This includes documentafion for $184,661.80 in expenditures for January 2007 that cover the unsupported costs. FOT has discussed the other three items with CCG and Turner and is negotiating with outside counsel to review and advise FOT on the other three issues. FOT will complete legal and accountant review and, if warranted, send demand letters that require CCG and Turner to provide evidence that the charges were jusfified or return the questionable charges, $178,843 from CCG and $224,684 from Turner.

SUSTAINABLE OPPORTUNITIES

This is an informational report and no new sustainable opportunities have been.

DISABILITY AND SENIOR CITIZEN ACCESS

There are no American with Disabilities Act (ADA) or senior access issues applicable to this report.

ACTION REQUESTED OF THE CITY COUNCIL

Staff requests that the City Council accept the Fox Audit, City Response and status report.

Respectfully submitted,

Fred Blackwell, Assistant City Administrator
Community & Economic Development Agency

Reviewed by:
Gregory D. Hunter, Deputy Director
Economic Development and Redevelopment, CEDA

Prepared by: Patrick Lane, Redevelopment Manager

APPROVED AND FORWARDED
TO THE COMMUNITY & ECONOMIC
DEVELOPMENT COMMITTEE:

Office of the City/Agency Administrator

Attachment A - Fox Theater Renovation Project Performance Audit
Attachment B – City's Response to the Fox Audit

ATTACHMENT A
Fox Theater Renovation Project Performance Audit

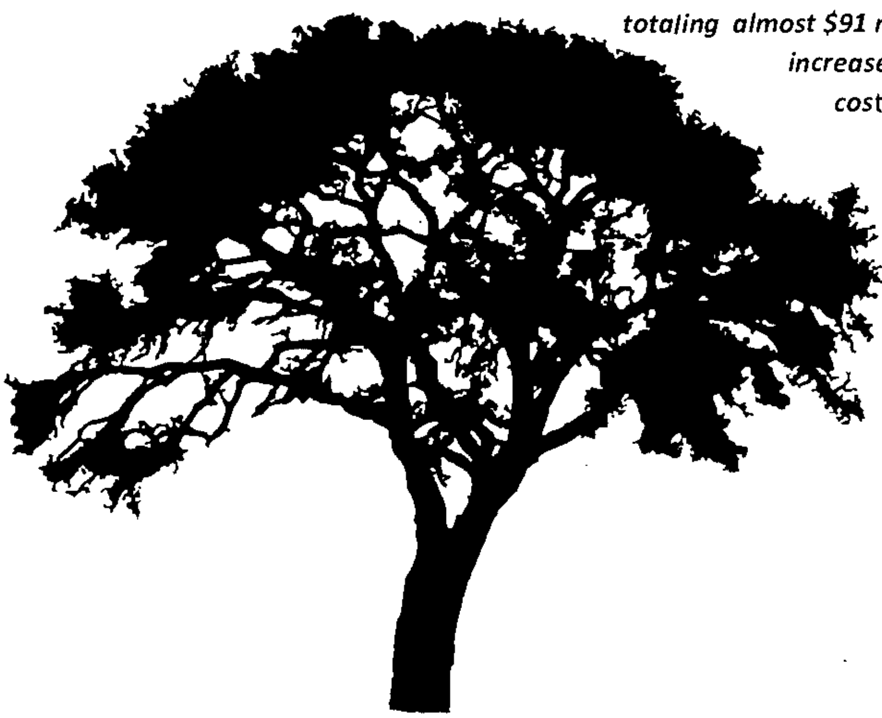
Item: _______
CED Committee
January 24, 2012

City of Oakland
Office of the City Auditor

October 4, 2011

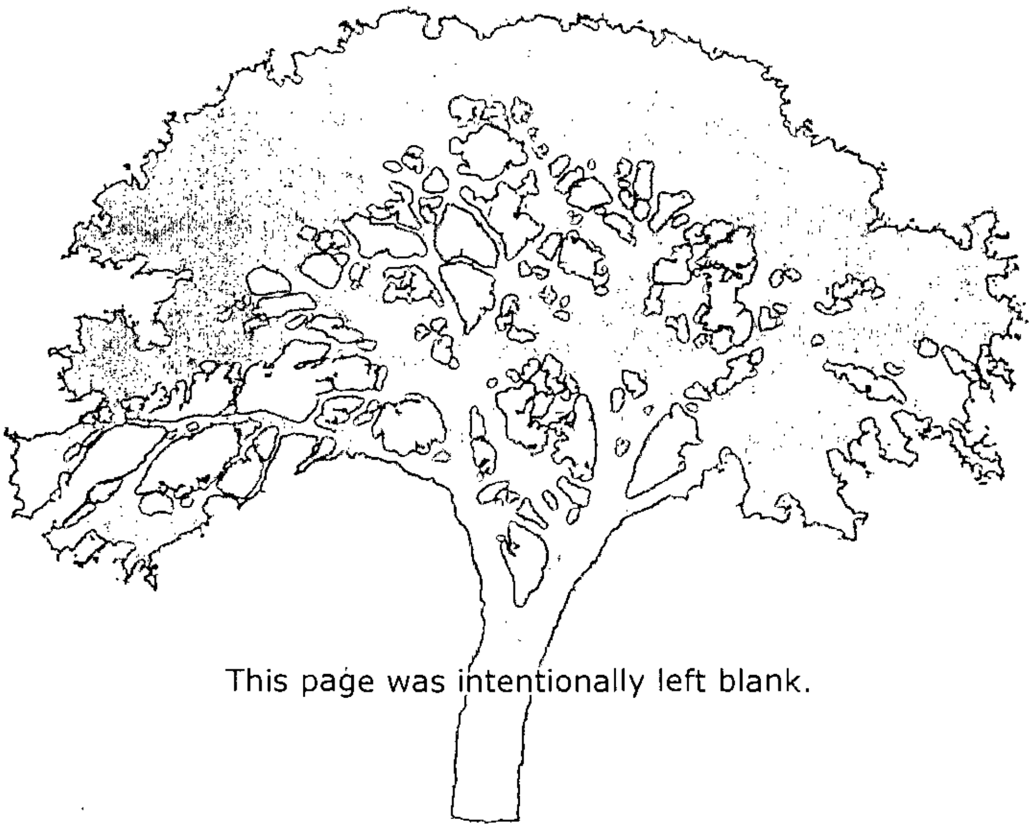
Fox Theater Renovation Project Performance Audit

A significant expansion of the project's scope, failure to conduct a comprehensive financial feasibility study, a project management structure that lacked independence, insufficient legislative oversight, and poor contract administration led to a final renovation project cost totaling almost $91 million, or a 172 percent increase from the initial project cost estimate of $33 million



City Auditor
Courtney A. Ruby, CPA, CFE

PERFORMANCE AUDIT



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CITY OF OAKLAND

CITY HALL • ONE FRANK H. OGAWA PLAZA, 4TH FLOOR • OAKLAND, CALIFORNIA 94612

Office of the City Auditor
Courtney A. Ruby, CPA, CFE
City Auditor

(510) 238-3378
FAX (510) 238-7640
TDD (510) 238-3254
www.oaklandauditor.com

October 4, 2011

OFFICE OF THE MAYOR
HONORABLE CITY COUNCIL
CITY ADMINISTRATOR
CITIZENS OF OAKLAND
OAKLAND, CALIFORNIA

RE: FOX THEATER RENOVATION PROJECT PERFORMANCE AUDIT

Dear Mayor Quan, President Reid, Members of the City Council, City Administrator Santana, and Oakland Citizens:

In 1996, the City of Oakland's Redevelopment Agency (Agency) purchased the Fox Theater to begin work on a master plan to renovate this historical performing arts center and to return downtown to the bustling entertainment and shopping district that it once was.

In December 2004, the City Council approved the "Basic Renovation" for the Fox Theater, scaled to be a 500 to 600-seat cabaret-style venue within the shell of the existing historic theater. With the identification of new potential funding sources, the project evolved into the Full "Broadway" show, including the balcony level with a fixed stadium-style seating for 1,100 patrons, a rear theater bar, restoration of the phantasmal figures, the basement, stage, and new "wing extensions". In December 2006, the construction project, the largest of its kind in the U.S., got underway and the Fox Theater reopened in February 2009 after being out of commission for 35 years.

From a purely construction renovation perspective, the project was a success as lavish architectural details were restored and state-of-the-art systems were installed to create a performance space second to none. Additionally, the theater consistently draws capacity crowds, as well as continues to spur the opening of new shops and restaurants near the theater.

However, the objective of this performance audit was to evaluate whether or not the renovation met the necessary standards in project management and contract compliance, as well as to assess the execution of a complex financing strategy. In initiating this performance audit, the intention of both the City Auditor's Office and the Community Economic and Development Agency was ultimately to use this project evaluation as a guide for future redevelopment projects. Given the current Army Base Redevelopment, the timing couldn't be better for the Agency to know where its strengths are and where the Agency must improve if it is to deliver upon its responsibility to use every tax dollar wisely and effectively on behalf of our citizens.

The final renovation project costs totaled almost $91 million, or a 172 percent increase from the initial project cost estimate of $33 million. A number of factors led to this dramatic increase, including a significant expansion of the project's scope, failure to conduct a comprehensive financial feasibility study, a project management structure that lacked independence, insufficient legislative oversight, and poor contract administration. Consequently, the Agency's contribution increased from $13 million to $52 million, or approximately $39 million, from December 2004 and comprised 57 percent of the total project costs.

The audit identified the following areas where improvements are warranted:

- Preparing a comprehensive financial feasibility analysis that includes project scope, budget, and financing structure
- Establishing a project budget with funding sources clearly identified before project specifications are defined
- Providing clear and consistent information for the City Council to make informed decisions, and such information should include project alternatives, options to reject or modify scope, and required versus proposed changes
- Establishing ways to increase LBE and SLBE participation without limiting competition
- Ensuring Federal compliance requirements will be met when accepting federal funds
- Developing project management structures that ensure independent and objective decision making
- Utilizing contracts that provide incentives for cost savings instead of cost growth
- Ensuring contract compensation provisions are clear, consistent, and adhered to by both contractors and subcontractors
- Establishing contract oversight to ensure all payments are properly authorized, supported, and do not exceed contract amounts
- Establishing a formal change order review process that includes independent cost estimates, cost analysis, and records of negotiation
- Developing a comprehensive construction project management manual to ensure all necessary project management standards are established, known, and adhered to

The audit also identifies the following areas where the Agency met or exceeded standards:

- Capital totaling $32 million from Bank of America and Bank of America Community Development Banking Group was successfully obtained in a challenging economic environment
- Established sponsorship and organizational structure was critical to attract private capital

The body of this performance audit provides, in detail, evidence to support our conclusions; however, I would like to highlight a few examples:

Project Management Structure

The audit found that the Agency established a project management structure where both the project leader and contractor were in a position to increase the project's scope, and therefore benefit financially from cost increases. For this renovation, construction costs grew from an estimated $24.5 million to $63.9 million, or a 161 percent increase.

Legislative Oversight

Agency management did not adhere to the December 2004 staff agenda report, which stated that the City Council would have, at each phase, the opportunity to review the costs and financing in order to determine whether or not to proceed. The audit found no evidence that project alternatives were provided or that City Council was provided options to reject or modify the scope changes.

While additional funding was identified and the project scope increased, the scope increases should have been addressed as either proposed or required changes. The City Council should then have had the opportunity to decide on whether to proceed, modify, or reject the proposed changes, if not required.

Competitive Bidding Requirements Waiver

To allow for "greater than usual local business participation", Agency staff requested that the City Council grant a competitive bidding requirements waiver for the Fox Theater Project's construction contracts. The contractor established participation goals at 50 percent for LBE and 20 percent for SLBE. However, these goals were not achieved (with 18 percent LBE and 19 percent SLBE) - producing L/SLBE participation far less than intended and no better than in other City contacts where the competitive bidding requirement had not been waived.

Contract Oversight and Administration

The audit report provides clear evidence of how contract oversight and administration were inadequate, which includes the Agency authorizing payments in excess of contract ceilings, payments being made for unsupported costs, and overpayments being made for developer/management fees. Additionally, the audit found clear evidence of inadequate change order review, such as no independent cost estimates, no cost detail to conduct a cost analysis, and no records of negotiation. The audit also found that the Agency and FOT may be entitled to refunds due to potential costs being less than budgeted for Turner's Guaranteed Maximum Price (GMP) contract.

Financial Feasibility Analysis

While the requisite Agency approvals for the increase in the project's scope were obtained, there was never a comprehensive financial feasibility analysis and presentation of the entire Fox Theater Project, which resulted in under-estimating the capital needs of the project. As such, a comprehensive road map for the project did not exist.

Without the comprehensive analysis, changes were viewed in isolation and not evaluated in an integrated manner that would address the impact on the entire project's feasibility or assess the financial risks. For example, while it is expected that an adaptive re-use project would likely experience cost overruns, the analysis would have determined the amount of reasonable contingencies for these unknown factors. Additionally, the absence of a forecast or projection model limited the Agency's ability to assess the Project's ability to reach its redevelopment objectives and financial goals.

Given the audit findings, it is clear no single entity, be it the Administration, City Council, project manager or contractor, can be held ultimately responsible for the successes and failures of the Fox Theater's renovation. Consequently, this lack of ultimate leadership produced a circumstance where no one was solely accountable to the citizens but everyone was partially at fault for the significant expansion of the project's scope, failure to conduct a comprehensive financial feasibility study, a project management structure that lacked independence, insufficient legislative oversight, and poor contract administration.

With a deal for the redevelopment of Oakland's former Army Base underway, it is critical that the City adopts the appropriate administrative measures and internal controls to ensure that this project estimated at more than half a billion dollars will not duplicate past mistakes.

Before the City invests its very limited resources into a larger and more complex redevelopment project, it is absolutely necessary for this audit's recommendations to be fully implemented and for the following questions to be discussed among the City Council and City Administration:

- Who is ultimately accountable to Oakland's citizens for Redevelopment's successes or failures?
- Are the requisite systems implemented to ensure a redevelopment project meets its objectives on time, within budget, and with unmitigated transparency?
- And finally, if Oakland is presented with an opportunity to increase a project's size and scale, who is responsible for initiating a cost/benefit analysis to conclude that a greater award of the City's limited resources is in Oakland's best economic interest?

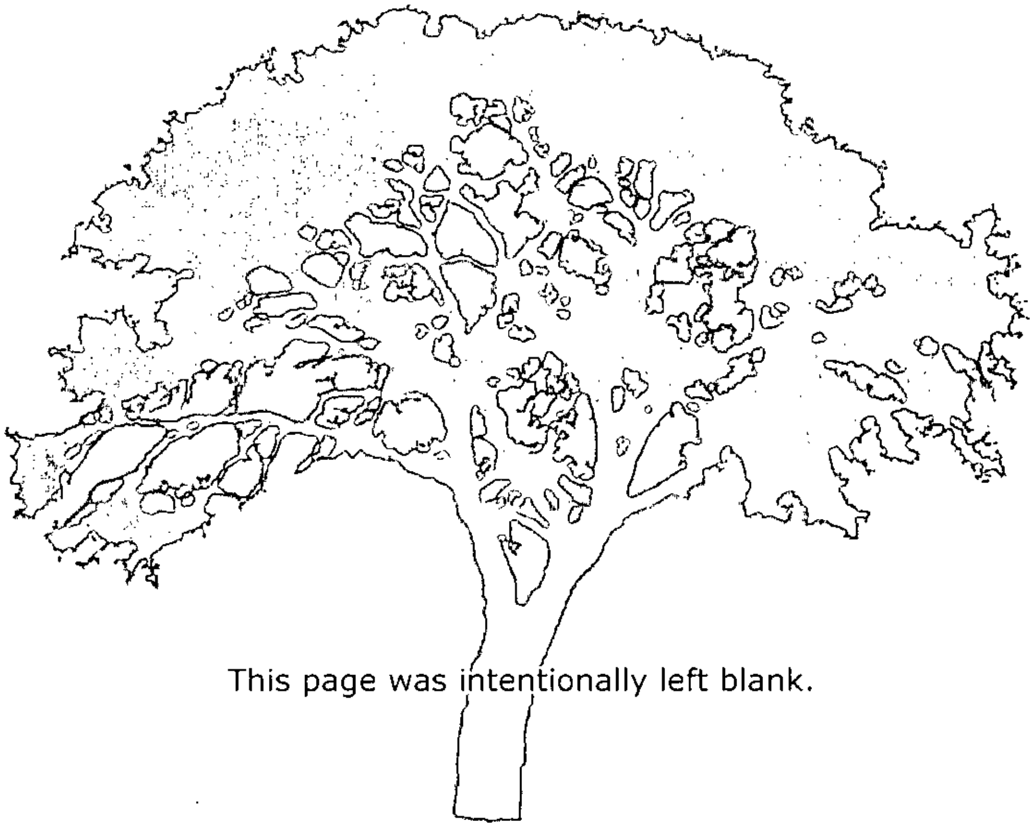
It is my hope that this report more clearly informs the City Administration, City Council, and the public of the decision making process that led to the final project cost of almost $91 million. It is now up to the City Administration and the City Council to ensure that the lessons learned from the Fox Theater's renovation are not repeated in other future redevelopment projects.

Respectfully submitted,

Courtney A. Ruby

COURTNEY A. RUBY, CPA, CFE
City Auditor

Table of Contents



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FOX THEATER RENOVATION PROJECT PERFORMANCE AUDIT
REPORT SUMMARY

OVERVIEW

The final renovation project costs totaled almost $91 million, or a 172% increase from the initial project cost estimate of $33 million. A number of factors led to this dramatic increase, including a significant expansion of the project's scope, failure to conduct a comprehensive financial feasibility study, a project management structure that lacked independence, insufficient legislative oversight, and poor contract administration.

Objective

The Office of the City Auditor conducted a comprehensive evaluation of contract compliance, project management, and the complex financing strategy utilized for the Fox Theater Renovation Project. The objectives of the audit were to evaluate:

- Contract compliance relating to the Agency's Fox Theater Renovation Project
- Project management relating to the Agency's Fox Theater Renovation Project
- Complex financing strategy relating to the Agency's Fox Theater Renovation Project

Key Findings

The following are key findings from the audit:

- Project cost growth increased by $58 million from 2004 to 2011, with the City absorbing a majority of the increased cost
- Agency staff communications to City Council regarding project cost and scope appeared to be incomplete
- Competitive procurement requirements were waived to increase LBE and SLBE participation levels, however goals were not achieved
- The award of non-competitive procurement contracts may not have complied with federal procurement requirements and may have resulted in higher costs
- Project organizational structure did not provide for adequate independence over project management decisions
- Inadequate contract oversight and administration by the Agency and FOT over CCG and Turner contracts
- The Agency and FOT did not effectively monitor contract expenditure levels, resulting in payments exceeding contract Not-to-Exceed values
- Payments to CCG exceeded Not-to-Exceed values by $1,179,437
- Unsupported costs of $178,726 were paid to CCG
- Overpayment of developer/management fees to CCG totaling $178,843
- Improved change order pricing procedures could have resulted in lower costs
- The Agency and FOT may be entitled to refunds due to potential costs being less than budgeted for Turner's Guaranteed Maximum Price (GMP) contract

Key Recommendations

To address the audit's findings, the report includes several key recommendations:

- For future capital projects, project scope should be reevaluated only when funding sources are guaranteed and secured. If funding sources are not guaranteed, a contingency plan should be in place to reduce the project scope when those funds are not received
- Develop policies and procedures and/or a policy for future capital projects that state what, when, and how information regarding project scope and costs should be communicated to the City Council/Committee by the respective City agency
- For future projects, evaluate ways to increase LBE and SLBE participation without limiting competition
- Develop procedures to ensure that waivers of competitive procurement are not in violation of federal grant requirements
- Ensure contractual decisions are made by individuals that are independent and objective and do not directly benefit from contractual decisions
- Establish procedures to ensure that adequate records are maintained on the contract amounts paid, and on the basic and amended contract value of all contracts under a project, and that cumulative payments are checked against contract balances prior to authorizing contract payments and that contract amendments are executed where appropriate
- Request supporting documentation from CCG for all unsupported costs, and if documentation is not provided, these costs should be returned to the Agency
- Seek recovery of the $178,843 in Developer/Management fees overpaid to CCG
- Establish change order pricing procedures that require:
    - The preparation of independent estimates of contract changes
    - The preparation of detailed contractor change order proposals in accordance with specific criteria on allowable costs and mark-up
    - Use labor rates at prevailing wage levels (unless justified by documentation)
    - The performance and documentation of a cost analysis of contractor proposals
    - The preparation of records of negotiation
- Develop a comprehensive construction project management policies and procedures manual detailing the significant policies and procedures for effective management, oversight, and administration of large capital improvement projects

Introduction

The City of Oakland (City) has been operating in an environment of severe budget deficits since fiscal year (FY) 2007-08. Deficits have gripped municipalities and state governments across the country since the onset of the current recession. As revenue streams shrink, project management of large capital construction projects is critical, and it is essential that cost controls, internal controls, and contractor monitoring are effective to ensure limited funds are expended appropriately and efficiently. The Office of the City Auditor (Office) commissioned Thompson, Cobb, Bazilio & Associates to conduct a performance audit of the Redevelopment Agency of the City of Oakland's (Agency) project management of the Fox Theatre Renovation Project and to evaluate the efficiency and effectiveness of project oversight and monitoring.

Background

In 1996, the Agency purchased the Fox Theater and work began on a master plan to renovate the building to house a new 2,500-seat performing arts center and home of the Oakland School for the Arts. In December 2006, the construction project, the largest of its kind in the U.S., got underway. Lavish architectural details were restored, from the colorful marquee to the exotically themed interiors, and state-of-the-art systems were installed to create a performance space second to none. Reopened in February 2009 after being out of commission for 35 years, the theater consistently draws capacity crowds. New shops, restaurants, and apartment houses are springing up, adding vibrancy to a once-struggling area.

The Fox Theater Renovation project characteristics described above required the creation of:

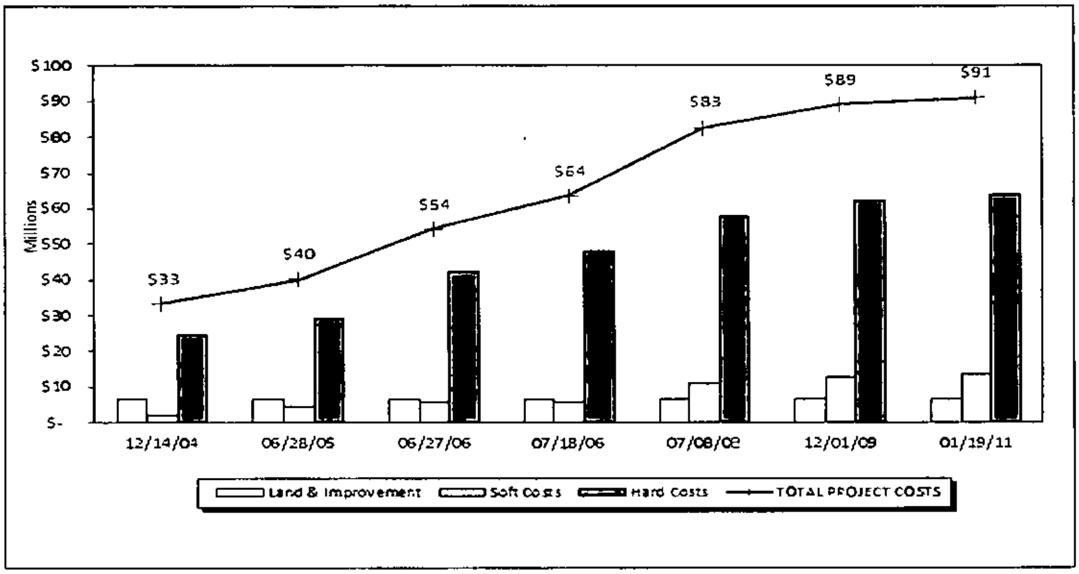
- Non-profit corporation
- For-profit corporation
- Two limited liability companies

The Agency entered into a Disposition and Development Agreement (DDA) with the parent non-profit corporation and these four entities entered into a series of ownership and financial structures and agreements to ensure that the project would receive more than $26 million in historic tax credits and new market tax credits to complete the project.

For the project scope at December 2004, project costs were estimated at $33 million. For the project scope at January 2011, the final project costs was valued at $91 million including soft costs, hard costs[1], contingencies, tenant improvements, and change orders. The project required 524 change orders[2] valued at $18.6[3] million. EXHIBIT 1 illustrates the cost growth of the project from the initial concept to final construction.

[1] Soft costs are associated with the planning, design, and coordination of a construction project. Hard costs are associated with any work or costs of the actual construction.
[2] Change orders are approved adjustments to the contract (such as amount, milestone, and time) for additional, deletion, or revision in the scope of work as originally defined in the contract.

EXHIBIT 1: Fox Theater Project Cost Growth



Source: Agenda Reports and Final Expenditure Report dated January 19, 2011

The project had both a general contractor and a project manager. The project manager acted as the "fee developer[4]" for the project. Turner Construction (Turner) served as the general contractor, and there were 34 subcontractors working under the direction of Turner. California Capital Group (CCG) served as the project manager and acted as the owner's representative for the design, construction, and financing of the project. CCG hired all professional consultants for the project, excluding the attorneys, accountants, and Turner (as the general contractor), but including all architects, engineers, security, surveying, testing consultants, etc. CCG was also the principal negotiator for the construction contract with Turner.

Under the project's complex ownership structure (see Appendix A), the Agency owns the Property and leases the Property to Fox Oakland Theater, Inc. pursuant to a DDA and a ground lease. FOT[5] (a non-profit public benefit corporation), assigned its interest in the ground lease to Fox Theater Landlord LLC (established to capture New Market Tax Credits) and FT Landlord subleased to FT Master Tenant LLC (established to capture Historic Tax Credit equity). Fox Theater (FT) Manager is the manager for both FT Landlord and FT Master Tenant. FOT and FT Manager have the same City/Agency employees as directors, officers, and unpaid staff. All of the leased interests are subject to the terms of the DDA and the ground lease.

[3] The net increase in contract value was $16.1 million after reducing the $18.6 million of change orders by $2.5 million for unused contractor contingencies and allowances.
[4] Fee Developer takes on all responsibilities of the development process and becomes the primary contact for the Owner. Services are provided on a percentage fee basis based on the project cost.
[5] Fox Oakland Theater, Inc. and its affiliated entities are collectively referred to as "FOT".

Objectives, Scope & Methodology

Audit Objectives

The objectives of the audit were to evaluate:

- Contract compliance relating to the Agency's Fox Theater Renovation Project
- Project management relating to the Agency's Fox Theater Renovation Project
- Complex financing strategy relating to the Agency's Fox Theater Renovation Project

Audit Scope

The performance audit was a comprehensive evaluation of contract compliance, project management, and the complex financing strategy utilized for the Fox Theater Renovation Project.

Audit Methodology

This section describes the methodologies used to complete the audit objectives.

To evaluate contract compliance relating to the Agency's Fox Theater Renovation Project, we:

- Evaluated the originating RFQ process to ensure it met the City's contracting requirements.
- Evaluated the original project scope and final project scope, including a detailed reconciliation of changes by identifying who authorized each change; if authorization was appropriate; if changes were necessary; and how the changes impacted project costs.
- Evaluated the project relationship with the Oakland School of the Arts, including how the relationship impacted the scope, nature, timing, and financing of the overall Fox Theater Renovation Project.
- Evaluated the project relationship with the restaurant and bar located in the ground floor of the Theater, including how the relationship impacted the scope, nature, timing, and financing of the overall Fox Theater Renovation Project.
- Evaluated compliance with all relevant laws, rules, regulations, policies, and procedures.

To evaluate project management of the City's Fox Theater Renovation Project, we:

- Evaluated project management by the Agency, CCG, Turner Construction, and any other significant subcontractors, including reviewing each parties' roles and responsibilities, effectiveness of the project's organizational structure, and if duplication of roles and responsibilities occurred.

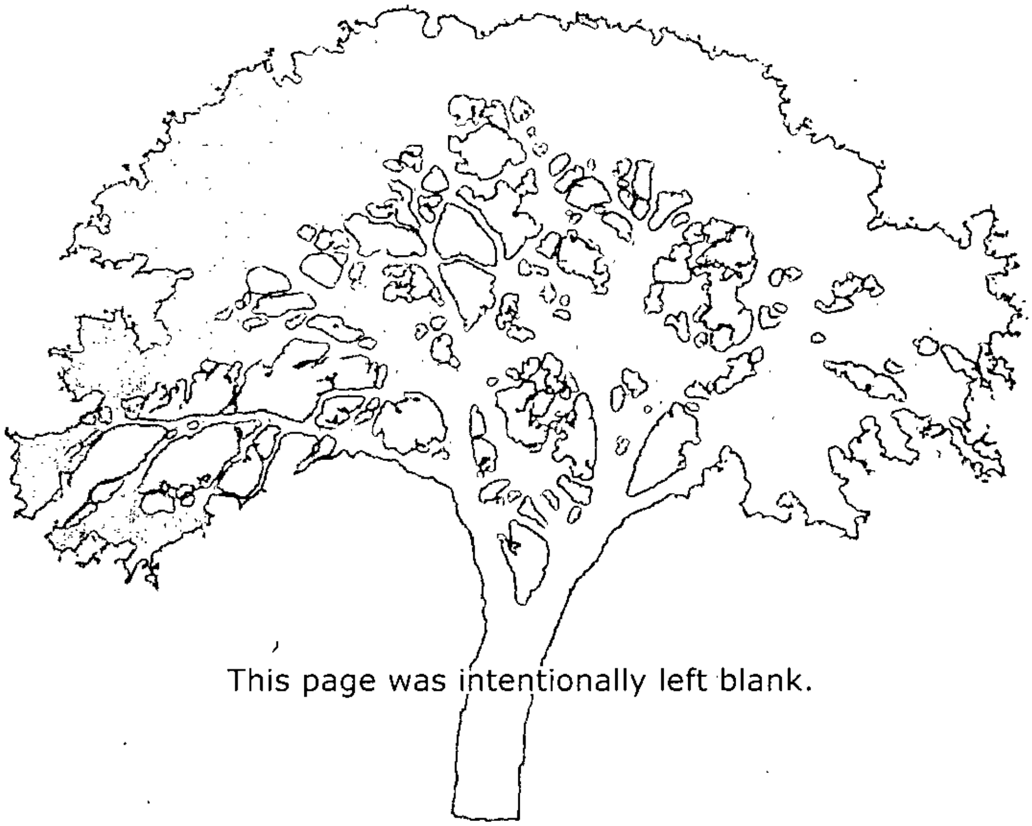
- Evaluated the adequacy of internal controls used by the Agency, project manager, general contractor, subcontractors, architects and engineers, including evaluating whether or not:
    - o Appropriate controls were in place to reduce risk and manage overall costs.
    - o Financial and budgetary reporting systems were in place.
    - o Project safety and insurance requirements were adequately monitored.
    - o Effective procedures were utilized for oversight and monitoring.
- Evaluated the process used to hire contractors and subcontractors.
- Evaluated if the City Council was appropriately informed by Agency staff of the project's progress, including all critical decisions related to changes in the project scope and cost implications from such changes.
- Examined applications for payments to ensure they were accurate and met contract terms.
- Evaluated the change order process to determine:
    - o If adequate procedures/controls existed to keep the cost of change orders to a minimum.
    - o If change orders were appropriately authorized.
    - o If change orders were split to avoid proper authorization.
    - o Why change orders occurred.
    - o The extent to which change orders could have been avoided or minimized.
- Evaluated related third-party transactions to determine their appropriateness.
- Evaluated the level and adequacy of the quality assurance and quality control measures used on the project.

To evaluate the complex financing strategy of the Agency's Fox Theater Renovation Project, we evaluated:

- The accuracy of project financing; examination of Agency and FOT finances, grants, special historic and new market tax credits, and tenant improvements.
- If the project financing strategy increased the project's scope of work and/or increased the Agency's required financial contribution.

- The Board of the Fox Theater, Inc. (a non-profit public benefit corporation) and the FT Manager, Inc. (a for-profit entity) inclusion in the ownership structure to determine the appropriateness of the same City/Agency employees serving as members of both Board of Directors.

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.



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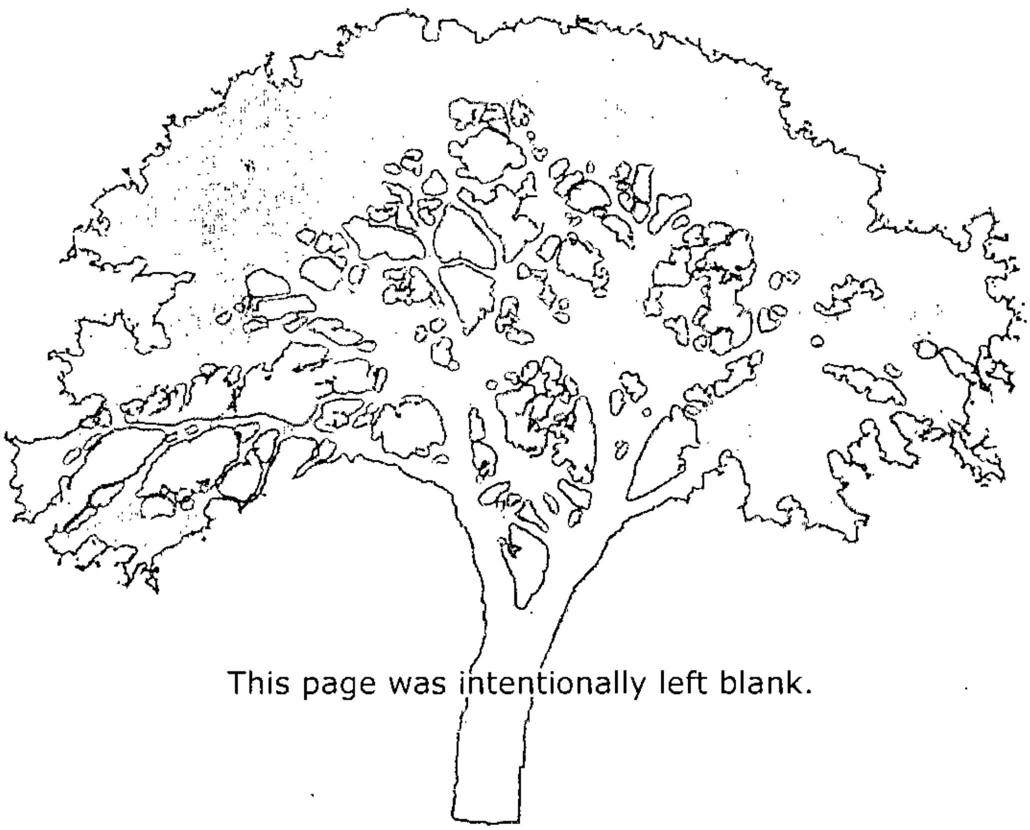
AUDIT RESULTS



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CHAPTER 1

FOX THEATER PROJECT SCOPE AND COST INCREASED BY 172 PERCENT OR $58 MILLION FROM INITIAL INCEPTION TO FINAL CONSTRUCTION

Project cost growth increased by $58 million from 2004 to 2011, with the City absorbing a majority of the increased cost

Typically, large capital projects establish a budget and the funding sources before project requirements and specifications are defined.

The Fox Theater Project budget and sources of funding changed constantly, resulting in changing construction requirements and specifications as additional funding was identified. Thus, increases in funding were the primary cause for project scope and cost increases.

The Design Development Phase was approved by the City Council in December 14, 2004. The total cost of the renovation was estimated at $33 million[6]. Five financing options were presented to the City Council, which acts as both the City Council and Agency Board, that included Agency contributions ranging from $4.15 to $13.15 million, with the remainder to be funded through grants and fundraising efforts. The Design Development and Construction Document Phases spanned December 2004 through December 2006. During the design phase, the project scope and costs increased as additional funding sources were identified. These additional funding sources included both internal and external sources, which were all approved by the City Council. Per discussions with Agency representatives, it was the additional funding sources that drove the scope of the project.

In December 2004, the Fox renovation (Basic Renovation) was for a 500 to 600-seat cabaret-style venue within the shell of the existing historic theater, which included the renovation of the theater and the wrap-around building, plus constructing second and third floor extensions.

In June 2005, the Agency and CCG identified almost $34 million in additional funding, consisting of $13 million from Agency bonds, $2.8 million in Agency insurance proceeds and funds, $2.5 million in tax credits, and the remaining from grants and fundraising. With this additional funding, the scope of the project increased to include the lower section of the balcony that could seat as many as 1,300 patrons.

In June 2006, the Agency and CCG identified an additional $47.9 million in potential funding sources. Consequently, the project evolved from the "Basic" renovation into the Full "Broadway" show and additional space was added to accommodate the activities of the Oakland School for the Arts (OSA). The potential funding sources included a $25.5 million loan from the Agency, $10.3 million in tax credits, $5 million in grants, $500,000 in private contributions, and a $6.5 million conventional loan from billboard revenues. With this additional funding, the scope of the project increased to include the balcony

[6] This includes the cost of land and improvements of $6.5 million.

level with a fixed stadium-style seating for 1,100 patrons, a bar at the rear of the theater, restoration of the phantasmal figures, the basement, stage, and new "wing extensions".

EXHIBIT 2 illustrates the identified funding sources as presented to the City Council by the Agency from December 2004 through March 2011.

EXHIBIT 2: Funding Sources

Funding Sources	12/14/04	06/28/05	06/27/06	07/18/06	Funded Amounts FINAL (3/2011)	Agency	B of A Tax Credits	Other Sources
Agency/City Contributions								
Agency Land/Improvements Loan		$ 1,500 000			$ 9,728,000	$ 9,728,000		
Agency Loan Installment #2					3,109,250	3,109,250		
Agency Loan (12/2009)					1,550,000	1,550,000		
Insurance Proceeds (Fire Insurance Settlement)		1,300,00)		1,500,000	2 226,250	2,226,250		
Senior Loan (Agency Loan) - Bond Issuances	13,150,000	13 000,000	25 500,000	25,500,000	22,390 750	21,390,750		
GASS 7I Grant (Portion for Turner 7I's)					513,986	518,986		
Redevelopment Façade Improvement Grant					75,000	75,000		
Redevelopment Tenant Improvement Grant					99 000	99 000		
Agency/City Contribution: Bridge Loan						-		
FOOF Advance ($7 45M)					350 000	350,000		
HUD Grant #2 (Advance of $7 45M)					3,000,000	3,000,000		
Prop 1C (Advance of $7 45M)					2,000,000	2,000,000		
Prop 40 (Advance of $7 45M)					-	-		
Historic Tax Credit (Advance $7 45M)					1,100,000	1,100,000		
Tax Credits								
Historic Tax Credits (HTC)	4,100,000	2,500 000	5,000,000	6,000,000	15 669,609		15,669,609	
New Market Tax Credits (NMTC)			5,500,000	8,500000	9,454 758		9,454,758	
Other Funding Sources								
Conventional Loan OSA Reserve (THE BANA LOAN)		6,000,000	6,500,000	6,500,000	6,492,098			6,492 098
Propostion 40 Grant (California Cultural & Historical Endowment-CCHE)	5,000,000	2,887,500	2,887,500	2,887,500	3,951,393			3,951,395
OSA Contribution to theater construction					1,500 000			1,500000
Cash from operations					1,343,000			1,343,000
Interest Income (From $25 S and NMTC)					662,105			662,105
HUD Funding			600,000	600 000	594 000			594,000
APE Lease Obligation					500,000			500,000
State Façade Grant (SHPO) (California Heritage Preservation Fund Grant)	750,000	750,000	375,000	375,000	375,000			375,000
CCHE Additional Grant Funding								-
OSA Reimbursement					280 787			280 787
OSA Capital				3,682,000				-
Friends of the Oakland Fox Campaign (FOOF)		1,000,000	500,000	500,000	230,000			230,000
Bank of America Grant					570,000			570,000
American Express Partners in Preservation					75 000			75,000
Ghielmetti Mitigation					68,750			68 750
Proposition 55 Grant		4,983,922						
School Construction Loan	4 000,000							
Federal Charter School Facility Grant			1,200,000	1,200,000				
TOTAL DEVELOPMENT	$27,000,000	$33,921,422	$47,862,500	$57,244,500	$87,908,736	$46,142,236	$25,124,367	$16,642,133
Tenant Improvements: Not Included in Development Budget								
OSA Tenant Improvement Loan					2,019 213	2,019,213		
Restaurant Tenant Improvement Loan					1,400,000	1,400,000		
FOOF Theater Tenant Improvement Loan					1,300,000	1,300,000		
GASS Theater Grant					1,486,014	1,486,014		
Subtotal of Tenant Improvement Assistance	-	-	-	-	6,205,227	6,205,227		
TOTAL PROJECT FUNDING	$27,000,000	$33,921,422	$47,862,500	$57,244,500	$94,113,963	$52,347,463	$25,124,367	$16,642,133

Source: Agenda Reports	Note: Funded amounts at 3/2011 include line items with zero amounts; this represents those funding sources that did not materialize.

As shown above, the Agency's contribution totaled approximately $52 million, or 57% of the total project costs.

The audit found that $7.6 million of funding sources identified were not secured. The Agency provided a $7.45 million bridge loan for several grant sources that only partially materialized. In addition, the Agency funded tenant improvements of $7 million, $5 million in loans that are to be repaid and a $2 million grant.

The Agency's contribution increased from $13 million to $52 million, or approximately $39 million[7], from December 2004[8].

The Agency proceeded with the development and design of the Fox Theater project renovation without first securing the project's full funding.

The final project costs totaled almost $91 million, of which $7 million were for tenant improvements that were not included in the project budget. However, the $7 million was funded by the Agency as loans or grants to tenants to be repaid in the future. This represents an increase of 172 percent from the original estimated cost in December 2004 of $33 million. EXHIBIT 3 illustrates the project costs in 2004 and 2006 as presented to the City Council by the Agency. The Final Costs were based on the Final Expenditure Budget as of 2011.

We recommend that for future capital projects, the project scope should be reevaluated only when funding sources are guaranteed and secured. If funding sources are not guaranteed, a contingency plan should be in place to reduce the project scope when those funds are not received.

EXHIBIT 3: Comparison of Project Costs

	2004	2006	FINAL
Hard Costs	$ 24,520,833	$47,890,000	$63,918,614
Soft Costs	$2,359,306	$5,672,500	$13,487,878
Total Development	$26,880,139	$53,562,500	$77,406,492
Land/Improvements	$6,500,000	$6,500,000	$6,500,000
Tenant Improvements		$3,682,000	$7,000,000
TOTAL PROJECT COSTS	**$33,380,189**	**$63,744,500**	**$90,906,492**
Source: Agenda Reports & Final Expenditure Budget			

[7] This includes the bridge loan of $7.45 million and the loan and grants for tenant improvements of $7 million.
[8] The Agency provided Tenant Assistance of $7 million in loans and grants for tenant improvements. Approximately $800,000 was already included in the development budget (GASS TI Grant and OSA Reimbursement).

Agency staff communications to City Council regarding project cost and scope appeared to be incomplete

Staff Agenda Report dated December 14, 2004 stated the following:

> The Council will have the opportunity to review the costs and financing at each phase and determine whether to proceed or not. At the end of this phase Agency staff will return to the Agency Board with a refined cost estimate and a preferred funding option because the outcome of various grant applications will be known. At that time, the Agency can authorize the commencement of the project and its financing, reject the project entirely, or modify the proposal to renovate the theater and wrap-around buildings. Following the authorization action, the third and final phase of drawings and cost estimation will be conducted and the project will only return to the Council if costs are not within the design development estimates last seen by the Council or for other actions necessary to implement financing.

Based on the audit's review of Board reports and observing taped City Council sessions regarding the Fox Theater Project, the audit found no evidence that the City Council was provided with the following:

- Project alternatives during the design phase
- Options to reject or modify the project
- Changes to the scope of the project identified as required changes or proposed changes

In December 2004, City Council approved the design development phase of the Fox renovation. The concept for the renovation was for a 500- to 600-seat cabaret-style venue, otherwise known as the "Basics" renovation, estimated at $33 million. The other alternative mentioned in the report was for a full restoration, or 3000-seat potential estimated at $60 million.

The design development and construction document phases spanned from December 2004 through July 2006. During this time, the project scope grew from the "Basics" renovation to the "Full" renovation. City Council was provided project updates during this time. These updates included a description and overview of the new project and scope. However, the audit found no evidence that project alternatives were provided and that City Council was provided options to reject or modify the scope changes. For example, the audit found no evidence that City Council was provided the opportunity to accept/reject balcony renovations, basements, etc. The reports provided by the Agency only provided a description of the current project that was being proposed for approval.

Based on the communications above, the audit found that changes in the scope of the project should have been more clearly communicated to City Council. That is, the scope changes should have been categorized as required changes or proposed changes, clearly communicating that City Council had the ability to accept, modify, or reject. Other alternatives to the scope changes should have been presented, thus allowing City Council to decide on whether or not to proceed.

A questionnaire was developed and sent to select[9] City Council members to solicit their views on whether or not Agency staff's communications regarding the Fox Theater Project scope and costs were clearly presented to them. Below is a summary of the two responses received:

- All communication was done through the Agenda reports
- The scope changed when other funding sources were identified
- Some alternatives were presented, but not sure if every prudent decision was presented
- Project scope changes and potential funding sources could have been presented more clearly
- New Market Tax Credits were explained, but complicated.

While project scope and costs were provided during the development phase, project alternatives were not provided. Responses from City Council members concur that as additional funding sources became available, the project scope increased; however, other project alternatives with lower costs could have been presented. In addition, funding sources and uses failed to accurately reference land and predevelopment costs, which understated total project costs.

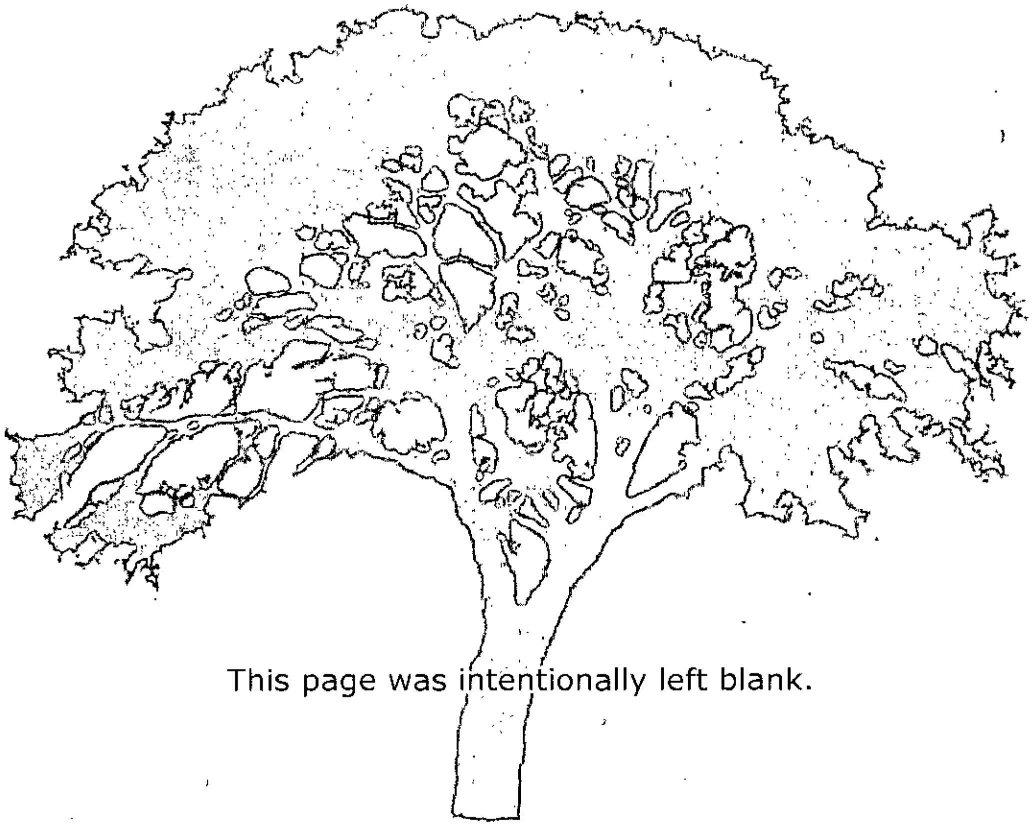
Agency management did not adhere to the December 2004 staff agenda report that stated the City Council would have the opportunity to review the costs and financing at each phase and determine whether to proceed or not.

Without providing information that was accurate, relevant, and complete, City Council did not have the opportunity to provide effective oversight and decision-making to proceed, modify, or reject the project.

We recommend that the City Administration develop policies and procedures and/or a policy for future capital projects that state what, when, and how information regarding project scope and costs should be communicated to the City Council/Committee by the respective City agency.

RECOMMENDATIONS	
We recommend that the **City Administration** and **Agency Management:**	
Recommendation #1	For future capital projects, project scope should be reevaluated only when funding sources are guaranteed and secured. If funding sources are not guaranteed, a contingency plan should be in place to reduce the project scope when those funds are not received.
We recommend that the **City Administration:**	
Recommendation #2	Develop policies and procedures and/or a policy for future capital projects that state what, when, and how information regarding project scope and costs should be communicated to the City Council/Committee by the respective City agency.

[9] Questionnaires were sent to all members of the CED Committee from FY 2003 through FY 2011, as well as other City Council members that were in attendance during City Council meetings that discussed the Fox Theater Project.



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CHAPTER 2

THE AGENCY JUSTIFIED AWARDING CONTRACTS ON A SOLE SOURCE NON-COMPETITIVE BASIS BY REQUIRING LBE AND SLBE SUBCONTRACTOR PARTICIPATION GOALS BE ESTABLISHED AT HIGHER THAN NORMAL LEVELS. HOWEVER, LBE AND SLBE PARTICIPATION GOALS WERE NOT ACHIEVED

Competitive procurement requirements were waived to increase LBE and SLBE participation levels, however goals were not achieved

California Public Contract Code 20160, Oakland Municipal Code (OMC) 2.04.050, and OMC 2.04.051 require that construction contracts for public projects be awarded through a competitive procurement process generally with award to the low qualified bidder after formal advertisement. Public Contract Code 20160 authorizes alternate procurement methods with the approval of governing boards, but these alternate methods still require competition.

The City's Local and Small Local Business Enterprise Program established Local Business Enterprise ("LBE") and Small Local Business Enterprise ("SLBE", and also counted as LBE) participation goals of 20 percent and 10 percent, respectively, on City contracts[10]. This program does not require that the City's competitive procurement procedures be waived to accomplish participation goals.

Agency staff requested that the City Council grant a waiver of Agency competitive bidding requirements for construction contracts for the Fox Theater Project to allow for "greater than usual local business participation"[11]. The City Council granted this waiver in July 2006[12].

The audit found that, due to the waiver, a competitive procurement process was not used for the Fox construction contract. Through Agency staff, CCG and Turner Construction, originated the request that the Agency's competitive bidding requirements be waived to facilitate increased SLBE and LBE participation under the construction contract. After obtaining this waiver from the Oakland City Council, Turner established participation goals for the Fox construction contract at 50 percent for LBE and 20 percent for SLBE. With this waiver, Turner issued subcontracts for the Fox Theater construction contract without using a low bid competitive procurement process.

Agency staff reported to the City Council's Community and Economic Development Committee ("CED Committee") in July 2007 that the construction phase was projected to achieve "LBE and SLBE participation

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[10] City of Oakland Local & Small Local For Profit and Not For Profit Business Enterprise Program Brochure, page 3.
[11] Agency Agenda report, June 27, 2006, page 15.
[12] Agency Resolution 80057 passed on July 18, 2006.

percentages of 51 percent and 21 percent[13]. The CED Committee has received no updates on Fox Theater Project L/SLBE participation since July 2007.

As of the close of FY 2009, Oakland's L/SLBE monitoring unit had not received final participation data on the Turner Fox Theater construction contract.

Turner did not use the competitive low bid procurement process to award subcontracts under the Fox Phase 2 construction contract in order to negotiate with subcontractors and obtain higher L/SLBE participation. However, goals were not achieved and the results of L/SLBE participation were no better than participation levels the City had achieved on contracts where the competitive selection process requirements were in place.

EXHIBIT 4 summarizes data that the Oakland L/SLBE compliance monitoring unit recently compiled and calculated on the L/SLBE participation during the two-year period ended June 30, 2009 under the Turner construction contract[14]. The table also shows the L/SLBE participation achieved under other Oakland contracts that were awarded without waiving the City's competitive bidding requirements.

EXHIBIT 4: Comparison of Fox Theater Project Construction Phase L/SLBE Participation with Overall City L/SLBE Participation[15]

	Dollars	Percentage	Participation on other City Contracts
Total Contracts	**$60,389,204**		
LBE (non-SLBE)	$10,904,724	18%	15%
SLBE	$11,720,144	19%	23%
Total L/SLBE	**$22,624,868**	**37%**	**38%**

The audit found that the waiver of competitive bidding does not appear to have increased L/SLBE participation levels under Phase 2 of the construction contract.

[13] Memo dated July 10, 2007 from Community and Economic Development Agency to Office of City Administrator/Agency Administrator RE: An Informational Report On The City's Local Contracting And Hiring Goals

[14] The LBE/SLBE Participation Reports from Oakland's L/SLBE monitoring unit was incorrectly calculated. The correct calculation should have reported 36%; however, the monitoring unit has not acknowledged this error or made any corrections. Thus, we are reporting the L/SLBE participation percentages as reported by Oakland's L/SLBE monitoring unit. The discrepancy only results in a 2% difference, and despite the 2% difference, the finding still remains as the 50% goal was not achieved.

[15] Compiled from LBE/SLBE Participation Reports on the Fox Theater Project for Phases 1, 2 and 3, as well as from the memo dated October 13, 2009 from Department of Contracting and Purchasing to Office of City Administrator - RE: Memo Informational Report on Annual Participation by Local and Small Local Business Enterprises (L/SLBE) on City Contracts for Fiscal Years 2007/2008 and 2008/2009, page 3.

The award of non-competitive procurement contracts complied with state law but may not have complied with federal procurement requirements and may have resulted in higher costs

California Public Contract Code 20160 requires that contracts for the construction or renovation of public projects be awarded on a competitive basis, which is consistent with federal and state laws. Public Contract Code 20175.2 allows cities to approve alternate procedures for bidding public projects, such as design-build; however, it still requires a formal competitive process. California Government Code 4529.12 requires that all architectural and engineering contracts be procured on a fair competitive basis.

These competitive requirements are predicated on the belief that competition saves money and eliminates favoritism in the award of contracts by state or local agencies. Under state law, Charter cities, such as Oakland, may adopt their own procurement procedures through City Ordinances. Oakland's procurement ordinances allow the City Council to waive competitive procurement requirements with a determination that such is in the best interest of the City.

On February 4, 2004, and with the approval of City Council, the Agency entered into a contract with CCG to perform pre-development activities associated with the development of the Fox Theater Project, including interviewing, negotiating and managing contracts with architects, engineers, and a general contractor "to develop schematic/design development drawings for budget estimating (not construction)" of the project. According to Agency officials, the contract was awarded to CCG without any formal competitive process. Two other proposals for development of the Fox Theater Project were received but were deemed unacceptable.

By December 2004, CCG activities under this contract included 1) preparation of conceptual drawings, 2) interior remediation of mold, asbestos and lead-based paint, 3) development of preliminary cost estimates, 4) completed grant applications, and 5) development of financing options.

In August 2005, the Agency amended the CCG contract by, among other things, authorizing CCG to negotiate a contract with Turner Construction (an existing member of CCG's Fox Theater consulting team) for the construction of the project under a Guaranteed Maximum Price contract.[16]

In July of 2006, the City Council approved an amended Disposition and Development Agreement with the Fox Oakland Theater, Inc. that included provisions authorizing CCG (the developer) to waive competitive bidding and request for proposal requirements for all professional services, procurement, and construction contracts under the project.

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[16] Guaranteed Maximum Price (GMP) contract is a cost-type contract where the contractor is compensated for actual costs incurred plus a fixed fee subject to a ceiling price. The contractor is responsible for overruns, unless the GMP has been increased through a change order. Savings resulting from cost underruns are returned to the owner. This is different from a fixed-price contract, where cost savings are typically retained by the contractor and essentially become additional profits.

In December 2006, without the benefit of competition, FOT entered into a contract with Turner Construction Company to construct the Fox Theater Project.

In addition to state and local competitive procurement requirements, the U.S. Housing and Urban Development (HUD) require that all procurement transactions under its grants be conducted in a manner that provides for full and open competition. Further, OMB Circular A-102 and Code of Federal Regulations 24 CFR 85 require procurement on a competitive basis.

The audit found that funding for the Fox Theater Project includes $600,000 of U.S. HUD grant money. City/Agency personnel associated with the award of the initial professional services contract with CCG were not aware of HUD requirements for competitive proposals and recommended to the City Council that competitive requirements be waived to increase L/SLBE participation for the Fox Theater Project. City Council was not advised of the potential adverse effects of waiving competition and approved Agency staff's recommendation to waive competition.

We recommend that the City Administration develop procedures to ensure that waivers of competitive procurement are not in violation of federal grant requirements and to evaluate more effective ways to increase L/SLBE participation without limiting competition.

RECOMMENDATIONS

We recommend that the City Administration:

Recommendation #3	Develop procedures to ensure that waivers of competitive procurement are not in violation of federal grant requirements.
Recommendation #4	For future projects, evaluate ways to increase LBE and SLBE participation without limiting competition.

CHAPTER 3

INADEQUATE PROJECT ORGANIZATIONAL STRUCTURE AND CONTRACT OVERSIGHT AND ADMINISTRATION BY THE AGENCY RESULTED IN PAYMENTS EXCEEDING CONTRACT AUTHORIZED AMOUNTS AND OVERPAYMENT OF CONTRACTOR COSTS

Project organizational structure did not provide for adequate independence over project management decisions

A fundamental contracting principle is that individuals or entities should be independent and objective and not be in a position to benefit from their contract decisions. Under public projects, project management decisions should be made by agency employees or representatives that have no personal interest in benefiting from contract cost increases.

If public agencies use alternative contractual arrangements, such as design-build[17] or construction manager at risk contracts[18], the project should be clearly defined to limit contract change orders. The contract should also be structured so that the contractor assumes significant risks and is rewarded for cost savings, rather than project cost growth.

Both CCG and Turner were in a position to direct/influence increases in project scope and cost, and benefited financially from cost increases. CCG provided development and project management services and acted as the owner representative for the Fox Theater Project. For these services, CCG was paid various fees, including a development fee based on the Fox Theater's construction cost. CCG recommended hiring Turner Construction Company for construction. Construction was performed primarily by Turner subcontractors, and Turner was the prime negotiator for any changes in work that occurred under the construction contract. Turner received a fee of 4.5 percent on the cost of all approved contract change orders.

The Turner construction contract has been described by Agency staff as a construction manager at risk contract. However, the audit found that this contract placed little risk on Turner and provided no incentive for Turner to reduce costs. The major contract risk items were placed into allowances and cost for allowance items had no contractual cap. One of the perceived advantages of a construction manager at risk contract is fewer contract changes. However, the scope of the Fox Theater Project was not defined well enough to limit contract change orders. Contract change order costs were 42 percent of the original Guaranteed Maximum Price (GMP) contract amount.

[17] A design-build contract requires a single contractor to be responsible for all design and construction work required to complete the project.
[18] The contractor assumes the risk of not being reimbursed for any cost overruns.

The audit found that the Agency established a project management structure where the project leader, CCG, could increase its revenues and profit by growing the project both in scope and costs. The Agency, FOT and CCG relied heavily on Turner construction to negotiate the cost of construction contract change orders - where the higher the cost of the change order, the higher Turner's fee.

The audit found that both CCG and Turner benefited financially from scope and cost growth experienced under the Fox Theater Project. The scope of the Fox Theater Project grew from a 600 person capacity cabaret-style venue when initially authorized in 2004 to a 3,000 person capacity full Broadway show venue at completion. Hard costs grew from an estimated $24.5 million to $63.9 million, an increase of 161 percent. CCG's Development and program management fees grew from a 2004 project estimate of $637,000 to $1.9 million, an increase of 195 percent. Turner's fees per the original contract totaled $1,779,000. Change orders under the construction contract totaled approximately $18.6[19] million. Turner's additional fee associated with these change orders amounted to more than $800,000.

We recommend that Agency management utilize contracts that provide incentives for cost savings instead of cost growth. If construction manager at risk contracts are to be used, the contract should be structured so that the construction manager assumes significant risks.

We also recommend that Agency management ensure that contractual decisions are made by individuals who are independent, objective, and do not directly benefit from contractual decisions.

Inadequate contract oversight and administration by the Agency and FOT over CCG and Turner contracts

Contract compensation provisions must clearly state the basis for payment to enable effective contract administration. Contract management personnel are responsible for reviewing and approving contractor request for payments and ensuring that payments are made within the limits and terms of the contract. To effectively perform this function, contract management personnel must clearly understand when and why payments are due, and must monitor total payments to ensure that they are within contract ceilings.

Under a GMP contract, the monitoring activity should also include an examination and verification of actual final contract GMP costs incurred, since costs incurred at less than budgeted GMP values should be returned to the owner entity. The audit found the following:

- The compensation terms of the Agency's contract with CCG and of CCG's contracts with its design subconsultants lacked clarity on the basis for payment.

[19] The net increase in contract value was $16.1 million after reducing the $18.6 million of change orders by $2.5 million for unused contractor contingencies and allowances.

- The Agency and FOT did not effectively monitor contract expenditure levels, resulting in payments exceeding contract Not-to-Exceed values.
- Unsupported costs of $178,726 were paid to CCG.
- Overpayment of developer/management fees to CCG totaling $178,843.
- The Agency and FOT may be entitled to refunds due to potential costs being less than budgeted for Turner's GMP contract .

The compensation terms of the Agency and FOT contract with CCG and of CCG's contracts with its design subconsultants lacked clarity on the basis for payment

CCG's basic contract states that CCG will be paid for performance, based on actual costs with a not-to-exceed cap, based on the scope of services and the budget by deliverable task and billing rates. This contract language lacks clarity and is contradictory. Based on the contract language, it is difficult to determine if CCG will be paid based on actual costs only or paid in accordance with the budgeted amount, or at a billing rate. This same language is used in CCG subconsultant contracts. These payment terms changed under some of CCG's contract amendments, but the language was still unclear. For example, for Amendment 1 to CCG's contract, it states that payments will be based on actual cost, but payments were made to CCG based on a monthly payment schedule.

While the meaning of these payment terms is unclear, it was agreed to by both the Agency and CCG that CCG's development and program management fees were fixed and that CCG's subconsultant fees and expenses and CCG expenses were to be reimbursed to CCG at cost without mark-up.

The audit found the following:

- Agency payments to CCG for the basic contract and Amendment 1 were made in accordance with a time schedule without regard to costs incurred. Thus, the Agency reimbursed CCG for expenses that were either unsupported or not incurred by CCG.
- The Agency and FOT did not clearly define contract payment provisions with CCG nor did it provide CCG with appropriate guidance on contract payment language for its subconsultants.
- The Agency and FOT did not establish procedures for monitoring CCG contract costs until the beginning of construction and did not have procedures to effectively ensure that payments were held with contract ceilings.

As a result of unclear payment provisions and the lack of contract monitoring procedures, the Agency authorized payments for CCG in excess of contract ceilings and in excess of costs incurred and/or documented CCG expenses.

We recommend that Agency management ensure that contract compensation provisions for future Agency contracts be tailored to each category of payment under the contract. For example, if a fixed amount is to be paid for a service, the compensation provision should identify the service and state that payment for that service is based on a "fixed fee". If there are costs that are to be reimbursed, the contract should identify those costs and state that those costs will be reimbursed at cost without mark-up.

The Agency/FOT did not effectively monitor contract expenditure levels, resulting in payments exceeding contract Not-to-Exceed values

Contract Not-To-Exceed values are generally established to limit an agency's financial exposure.

The audit found the following:

- The Agency and FOT did not effectively monitor contract expenditure levels, and as a result, payments made to CCG and its major design subconsultants exceeded contract Not-to-Exceed ceilings.
- Project subconsultants and subcontractors did experience periods where they were unable to obtain payment for work performed, and we know that the Agency and FOT occasionally withheld payment requests because it was unsure of whether or not consultants had exceeded contract authorizations.

As a result of unclear payment provisions and lack of contract monitoring procedures, the Agency and FOT authorized payments for CCG in excess of contract ceilings. EXHIBIT 5 details the payments made to CCG for its services and various pass through costs that exceeded its Not-To-Exceed ceiling.

EXHIBIT 5: Payments Made to CCG that Exceeded Not-to-Exceed Values

	CCG
Total Paid[20]	$12,674,471
Contract NTE	$11,495,034
Amount Over NTE	**$1,179,437**

The audit also found that payments to CCG's major design subconsultants: Architectural Dimensions and Associates (AD), KPA Group (KPA), ELS, and Starkweather Bondy Architecture LLP (SBA) exceeded contract Not-To-Exceed values as detailed in EXHIBIT 6.

[20] The total amount paid to CCG includes the amounts paid to the four architects listed in EXHIBIT 6.

EXHIBIT 6: Payments Made to Major Design Subconsultants that Exceeded Not-to-Exceed Values					
	AD	**KPA**	**ELS**	**SBA**	**TOTAL**
Total Paid	$1,569,154	$1,584,010	$685,169	$837,720	$4,676,053
Contract NTE	$1,077,960	$1,288,470	$465,794	$770,000	$3,602,224
Amount Over NTE	**$491,194**	**$295,540**	**$219,375**	**$67,720**	**$1,073,829**

According to Agency and FOT officials, payments made to the subconsultants for services provided were valid and consistent with work requirements, thus the audit is not questioning these costs. However, contracts should have been amended increasing the contract Not-to-Exceed values.

We recommend that Agency management establish procedures to ensure:

- Adequate records are maintained on the contract amounts paid and on the basic and amended contract value of all contracts under a project;
- Cumulative payments are checked against contract balances prior to authorizing contract payments; and
- Contract amendments are executed where appropriate.

Unsupported costs of $178,726 were paid to CCG

The contract between the Agency and CCG states that the "Contractor will be paid for performance of the scope of services an amount that will be based upon actual costs but will be "Capped" so as not to exceed..."

Amendment 1-4 of the CCG contract states that, "the Contractor will be paid for performance of the Scope of Services, Schedule A2 required under this Amendment... an amount that will be based upon actual costs..."

The audit found the following:

- Agency payments to CCG for the basic contract and Amendment 1 were made in accordance with the payment schedule (EXHIBIT B of Amendment 1) without regard to actual costs incurred.
- CCG costs incurred under the basic contract and Amendment 1 showed that CCG had received a payment of $22,421 for expenses that it had not incurred.
- Payment files indicated that the Agency and FOT staff reviewing CCG pay applications at the beginning of the construction contract requested documentation for $156,305 of CCG claims for expenses previously incurred under contract Amendments 2 through 4. However, the Agency

and/or FOT eventually reimbursed CCG for these expenses without obtaining the requested documentation.

Beginning with the award of the construction contract and under Amendment 5 of CCG's contract, the Agency and FOT began requiring documentation for CCG costs incurred under its contract. At this time, the Agency/FOT attempted to retroactively obtain documentation on CCG costs incurred but was not completely successful. The audit found that:

- The Agency and FOT did not establish procedures for monitoring CCG contract costs until the beginning of construction phase.
- The Agency and FOT made payments based on the payment schedule included in the contract; however, payment was to be limited to cost plus specified fees.
- The Agency and FOT reimbursed CCG $178,726 for expenses that were either unsupported or not incurred by CCG. EXHIBIT 7 details the unsupported costs.

EXHIBIT 7: Unsupported CCG Costs

Payments Made Under	**Unsupported**
Basic Contract/Amendment 1	$22,421
Amendment 2-4	$156,305
Total Unsupported	**$178,726**

We recommend that the Agency and FOT management request supporting documentation from CCG for all unsupported costs, and if documentation is not provided, these costs should be returned to the Agency and FOT.

Overpayment of developer/management fees to CCG totaling $178,843

Under CCG's contract with the Agency and FOT, including Amendments 1 through 7, CCG was authorized Fixed Developer/Management fees totaling $1,883,001, paid in increments over the period of the contract.

The audit found the following:

- The Agency and FOT did not maintain complete and accurate records on the nature and amount of fees authorized and paid to CCG over the life of the project, particularly during the period before the beginning of construction in December 2006.
- The Agency and FOT did not begin comparing CCG payment requests to fees authorized under the contract and its amendments until Phase 2 of

construction began. Consequently, the Agency and FOT did not have complete information on the nature and amount of fees paid under the entire CCG contract.

- The Agency and FOT did not have procedures that required complete and accurate accounting of fees authorized and paid under the CCG contract.

Developer/Management fees that the Agency/FOT paid CCG for the Fox Theater Project exceeded fees authorized by the CCG contract and amendments as illustrated in EXHIBIT 8.

EXHIBIT 8: Overpayment of Developer/Management Fees

Payments Made Under	Paid Developer & Program Management Fee
Basic Contract	$103,000
Amendment 1	$211,700
Amendment 2	$574,000
Amendment 3	$166,250
Amendment 4	$50,893
Draws 1-26	$956,001
Total Paid	**$2,061,844**
Authorized Fee	$1,883,001
Fee Overpayment	**$178,843**

We recommend that the Agency and FOT management seek recovery of the $178,843 in developer/management fees overpaid to CCG.

The Agency and FOT may be entitled to refunds due to potential costs being less than budgeted for Turner's Guaranteed Maximum Price (GMP) contract

Under a GMP contract, the monitoring activity should include an examination and verification of actual final contract costs. Costs incurred at less than budgeted GMP values are to be returned to the owner entity.

The audit found that neither CCG nor the Agency and FOT had performed any procedures to verify actual costs incurred by Turner Construction under the GMP contract. Additionally, the Agency and FOT did not perform or require that CCG perform an examination of the final GMP cost under the Turner construction contract.

If actual costs incurred under the GMP contract with Turner are less than the GMP, the final contract value should be adjusted and the amount paid in excess of actual costs should be returned to the Agency and FOT.

Based on the audit's review of the AIA Document G703 included in Turner's final payment application, the audit noted that $321,000 were for items that appear to represent uncommitted GMP budget balances that should result in a reduction in the GMP contract final price. This refund may be greater since the Agency and FOT has not verified Turner's actual costs to date. Approximately $39 million of the $43 million of the Phase 2 construction contract initial values with Turner was subject to GMP provisions, which means that at the completion of the contract, the contract value would be adjusted to the extent that actual costs were less than the $39 million value. The audit found no review has been performed yet to identify or validate Turner's actual costs that were incurred under the contract. Thus, the amount paid to Turner may be greater than warranted under the contract.

We recommend that Agency management perform a thorough examination of actual costs incurred by Turner under the Phase 2 construction contract to determine if an adjustment in contract price is warranted.

Improved Change Order pricing procedures could have resulted in lower costs

Contract change orders are negotiated without the benefit of competition, therefore, public agencies need to document the appropriate steps taken to ensure fair and reasonable prices were negotiated. At a minimum, the following documentation should be maintained:

- Preparation of a change order cost estimate independent from the contractor's proposal
- The contractor's detailed price proposal broken out by labor, material, and equipment costs and with sufficient detail as to allow a cost analysis (an analysis of the proposed costs)
- Preparation of a record of negotiation showing how the final price was established

These procedures not only provide a public record on the reasonableness of negotiated prices, but also could reduce change order costs.

The audit found that the project required 524 change orders totaling $18.6 million. The net increase in the contract value resulting from the change orders totaled $16.1 million after reductions for allowances and contingencies.

Based on the audit's review of four change orders valued at $2.1 million, the audit found the following:

- Independent estimates of change order costs were not prepared
- Labor rates included in change order proposed prices were excessive

- Records of negotiation were not prepared to show how the reasonableness of change order proposed prices were determined
- No written procedures on steps to be followed to establish fair and reasonable change order prices existed
- No specific instruction existed on the format and details that contractors/subcontractors should use in proposing change order prices
- No guidance had been provided to contractors/subcontractors on allowable costs and mark-up

While the audit cannot estimate total potential savings of change order costs that may have been achieved through improved change order pricing procedures, the audit found that significant cost savings could have been achieved had procedures been established for the preparation of independent estimates, on allowable costs and mark-ups, and on cost analysis of contractor change order proposals. For example, rates used in three of the four change orders that were reviewed exceeded California prevailing wage rates plus applicable benefits and payroll taxes by 40 percent, 41 percent and 60 percent, respectively.

We recommend that Agency management establish change order pricing procedures that require:

- The preparation of independent estimates of contract changes
- The preparation of detailed contractor change order proposals in accordance with specific criteria on allowable costs and mark-up
- Use labor rates at prevailing wage levels (unless justified by documentation)
- The performance and documentation of a cost analysis of contractor proposals
- The preparation of records of negotiation

Controls to limit potential conflicts of interest could have been improved for the Fox Theater Project

California Government Code Section 1090 prohibits a public official from being financially interested in a contract in both the official's public and private capacities. The purpose of California Government Code Section 1090, as stated by the California Supreme Court, is to make certain that "every public officer be guided solely by the public interest, rather than by personal interest, when dealing with contracts in an official capacity."

In addition, because Federal U.S. HUD grant monies were used on the Fox Theater Project, relevant Federal regulations apply. 24 CFR 85 applies to awards from the United States Department of Housing and Urban Development. These regulations apply to all entities, including subgrantees, involved in expenditures of Federal awards. Thus, these regulations apply to the City, Fox Oakland Theater, Inc., CCG, Architectural Designers and Turner.

24 CFR 85.36 states, in part: "Grantees and subgrantees will maintain a written code of standards of conduct governing the performance of their employees engaged in the award and administration of contracts. No employee, officer or agent of the grantee or subgrantee shall participate in selection, or in the award or administration of a contract supported by Federal funds if a conflict of interest, real or apparent, would be involved."

While Oakland Municipal Code (OMC) 3.16.010 incorporates state regulations for annual employee reporting of economic interests in certain business entities, the Agency has no procedures for disclosing conflicts of interest by specific project. City employees involved in selecting the CCG team and other vendors (including consultants and subcontractors) were not required to sign any conflict of interest disclosure statements for the selection of contractors for the Fox Theater Project. CCG team members involved in selecting other vendors received no formal guidance on conflicts of interest and were not required to sign conflict of interest disclosure statements for any of their procurement decisions.

City conflict of interest procedures require employees to disqualify themselves from decisions on matters concerning entities in which they have an economic interest. However, these procedures do not prescribe actions that should be taken to avoid conflicts of interest by those involved in procurement decisions. City Administrative Instruction ("AI") 595, effective July 1, 2007, provides basic guidelines on conflicts of interest, but it does not include specific guidance on the disclosure of conflicts of interest by employees making procurement decisions and on requirements for the completion of conflicts of interest disclosure statements for specific procurement actions.

While the audit found a need for additional conflict of interest safeguards, no conflicts of interest of city employees or CCG officials were revealed.

We recommend that the City Administration update AI 595 to make clear that those involved in selecting vendors be guided by the requirements of California Government Code Section 1090.

We also recommend that the City Administration implement a process that requires all individuals involved in selecting vendors (including non-City employees) on City-sponsored projects (including projects sponsored by non-City entities established by the City) to sign conflict of interest disclosure statements identifying any potential direct or indirect financial interests associated with any vendors under evaluation.

We also recommend that the City Administration and Agency Management develop a comprehensive construction project management policies and procedures manual detailing the significant policies and procedures for effective management, oversight, and administration of large capital improvement projects.

RECOMMENDATIONS	
We recommend **that Agency M**anagement:	
Recommendation #5	Utilize contracts that provide incentives for cost savings instead of cost growth. If construction manager at risk contracts are to be used, the contract should be structured so that the construction manager assumes significant risks.
Recommendation #6	Ensure contractual decisions are made by individuals that are independent and objective and do not directly benefit from contractual decisions.
Recommendation #7	Ensure that contract compensation provisions for future Agency contracts be tailored to each category of payment under the contract. For example, if a fixed amount is to be paid for a service, then the compensation provision should identify the service and state that payment for that service is based on a "fixed fee". If there are costs that are to be reimbursed, then the contract should identify those costs and state that those costs will be reimbursed at cost without mark-up.
Recommendation #8	Establish procedures to ensure that adequate records are maintained on the contract amounts paid, and on the basic and amended contract value of all contracts under a project, and that cumulative payments are checked against contract balances prior to authorizing contract payments and that contract amendments are executed where appropriate.
Recommendation #9	Request supporting documentation from CCG for all unsupported costs, and if documentation is not provided, these costs should be returned to the Agency.
Recommendation #10	Seek recovery of the $178,843 in Developer/Management fees overpaid to CCG.
Recommendation #11	Perform a thorough examination of actual costs incurred by Turner under the Phase 2 construction contract to determine if an adjustment in contract price is warranted.
Recommendation #12	Establish change order pricing procedures that require: • The preparation of independent estimates of contract changes • The preparation of detailed contractor change order proposals in accordance with specific criteria on allowable costs and mark-up • Use labor rates at prevailing wage levels (unless justified by documentation) • The performance and documentation of a cost analysis of contractor proposals • The preparation of records of negotiation

We recommend **that the City Administration:**	
Recommendation #13	Update AI 595 to make clear that those involved in selecting vendors be guided by the requirements of California Government Code Section 1090.
Recommendation #14	Implement a process that requires all individuals involved in selecting vendors (including non-City employees) on City-sponsored projects (including projects sponsored by non-City entities established by the City) to sign conflict of interest disclosure statements identifying any potential direct or indirect financial interests associated with any vendors under evaluation.
We recommend **that** the **City Administration and Agency Management:**	
Recommendation #15	Develop a comprehensive construction project management policies and procedures manual detailing the significant policies and procedures for effective management, oversight, and administration of large capital improvement projects.

CHAPTER 4

THE FINANCIAL FEASIBILITY ANALYSIS PERFORMED BY THE AGENCY WAS INADEQUATE FOR THE SCOPE OF THE PROJECT RESULTING IN UNDER ESTIMATING THE FINANCIAL NEEDS OF THE PROJECT

Financial feasibility analysis was inadequate for the scope of the project

The early financial feasibility analysis by the Agency did not clearly define the project's scope, budget, and financing structure. While the requisite Agency approvals were obtained, there was never a comprehensive financial feasibility analysis and presentation of the entire Fox Theater Project, which resulted in under-estimating the capital needs of project.

A comprehensive financial feasibility analysis was critical for the Fox Theater Project. The Fox Theater Project is a large-scale adaptive reuse project, which includes the renovation of a historical structure. The ability to determine the appropriate uses that produce an economically viable property will have an impact on the ability of the project to sustain its ongoing operations. As such, a comprehensive financial feasibility analysis[21] should have been completed to provide a road map for the project. A comprehensive financial feasibility analysis should include, but not be limited to, the following:

- Project Scope/Description
- Organizational Structure
- Resumes of Principals
- Operators and/or Developers
- Statement of Sources and Uses
- Project Budget and Financial Projections
- Financial Statements
- Site Control and Plan
- Building Floor Plan
- Appraisal/Valuations "As-Is", "As-Completed", at "Stabilized Operation"
- Environmental Assessment
- Financing Commitments
- Equity Requirement
- Tenant Leases or Letters of Interest
- Job Creation Projections

The Agency feasibility analysis included many (or variations) of the above requisite elements; however, given the progressive and complex nature of the Fox Theater Project, there were shortcomings associated with the following five major elements:

[21] Document is progressive and allows consistent checks and balances to measure project development against the stated Scope of the Project. Consequently, substantial deviations may deem a project infeasible.

- Project Scope/Description
- Statement of Sources and Uses
- Project Budget and Financial Projections
- Financial Statements
- Real Estate Appraisal or Valuation

As the scope of the project changed and the costs increased from $33 million (including land and predevelopment) to $91 million (as of 2011), so should have other assumptions in the comprehensive project financial feasibility analysis. Without a comprehensive financial feasibility analysis, changes were viewed in isolation and not evaluated in an integrated manner that would address the impact on the entire project feasibility or assess the financial risks.

Specifically, the audit found that the following five major elements of the Agency's project financial feasibility analysis needed improvement:

<u>Project Scope/Description</u>
The original project scope/description included the "Ruins Concept" at $33 million. It was similar to the "Basic Concept" at $70 million described in an earlier 2001 Fox Master Plan. Though the two concepts were similar, it was not clear what contributed to the significant cost differences, especially given the resulting $91 million final project cost. It is expected that an adaptive re-use project would likely experience cost overruns as unknown conditions are uncovered; however, the conduct of appropriate due diligence and preparation of a comprehensive financial feasibility analysis during the predevelopment phase would have determined the amount of reasonable contingencies for these unknown factors.

<u>Statement of Sources and Uses</u>
Well managed sources and uses statements (timely updates, clarity, footnotes, etc.) provide an ongoing view of a much needed development financing equation, cost + equity = financing need. Changes in any one of these components would alert the Agency to the escalating costs. The audit found that sources and uses statements (dated 12/14/04, 06/28/05, 06/27/06, and 07/18/06) omitted or failed to accurately reference land and predevelopment costs. In addition, $7 million in tenant improvement costs did not appear on the statements until 07/08/08, at which time the Agency provided interim loans to pay for tenant improvement costs. Thus, total project costs were either understated or were not projected at various stages of project development.

<u>Project Budget and Financial Projections</u>
These are income and balance sheet assumptions extended into the future. These projections aid in presenting an effective "operating plan" for the project. The Fox Theater Project's original plan did not project the effect of rising development costs on cash flow. Unabated, deviations in these elements may result in substantially unfavorable effects in other elements of the feasibility analysis. Specifically, when a commercial

development is undertaken, the financial analysis should evaluate the operating assumptions for the project, the likelihood of reaching stabilization (rental income and other income in excess of operating costs and debt service and operating reserves) and the resultant net cash flow. The failure to realize these projected operating results will diminish the project's ability to sustain itself. When there is an inability to produce a consistent net operating income (NOI), the project will be at risk of default on its financial obligations, and the sponsor/developer (Agency) must determine its capacity or desire to provide ongoing financial support to the project or repay any financial obligations of the project.

Financial Statements
Development projects of this magnitude, with a non-profit sponsorship, should have audited financial statements. The Fox Theater Project has a layered organizational structure, which was required to facilitate attracting New Market Tax Credits and Historic Tax Credits financing. Each organization in the project has audited financial statements except FOT, Inc., – the primary organization through which substantially all funds passed. While FOT, Inc. financial statements were unaudited, this did not adversely affect the project's ability to be awarded tax credit contributions. However, should the Agency desire to monetize or attract additional capital, it is likely that capital providers will place limited reliance on unaudited financial statements.

Real Estate Appraisal or Valuation
While the "as-is" appraisal commissioned by the Agency valued the pre-development cost, an "as-completed" appraisal would have provided a value for the entire Fox Theater Project and provided a basis to evaluate the project cost to project value. A review of the estimated value at stabilized operations would provide the Agency with the ability to assess its potential return on investment and potential return of capital. This "as-completed" appraisal would have allowed the Agency staff to disclose to the Agency Board whether it was prudent or not to complete the project at a given cost.

The Fox Theater Project has cost much more than anticipated and many of the prospective financing sources never materialized. The failure to develop a comprehensive financial feasibility analysis with clearly identified benchmarks to manage toward did not allow consistent checks and balances to measure project development against the stated scope of the project. The absence of a forecast or projection model to manage actual results limited the Agency's ability to assess the project's capability to reach its development objectives and/or produce the desired net operating income (NOI) to service debt and minimize default on its financial obligations.

We recommend that the City Administration and Agency management adopt policies and procedures to conduct a comprehensive financial feasibility analysis of future Agency project's scope and adjust the relevant components/elements of the financial feasibility model as changes are proposed. The financial feasibility model for projects should list, but not be limited, to the following elements:

- Project Scope/Description
- Organizational Structure
- Resumes of Principals
- Operators and/or Developers
- Statement of Sources and Uses
- Project Budget and Financial Projections
- Financial Statements
- Site Control and Plan
- Building Floor Plan
- Appraisal/Valuations "As-Is", "As-Completed", at "Stabilized Operatior
- Environmental Assessment
- Financing Commitments
- Equity Requirement
- Tenant Leases or Letters of Interest
- Job Creation Projections

Further, the model must be structured around project specific features.

We also recommend that the City Administration and Agency management consider hiring competent third party assistance with relative experience in the area of financial feasibility modeling and implementation to the extent that the Agency lacks the time, staff or competency.

Capital totaling $32 million from private alternative financing sources was successfully obtained to fund the Fox Theater Project

CCG was required to seek alternative funding sources, which included tax credit financing and a construction loan from the private sector. The utilization of tax credit financing for community and economic development projects can make revitalization and rehabilitation projects a reality. These tax credit financing tools are very complex instruments and require a significant amount of professional financial, legal, and tax expertise.

CCG and FOT successfully obtained private sector financing, which was provided solely by Bank of America (BOA) and Bank of America Community Development Banking Group. The BOA financing structure offered the Fox Theater Project both conventional construction financing, Historic Tax Credits, and New Markets Tax Credits, which totaled $32 million in aggregate with maturities of less than 10 years and a weighted below market interest rates.

The Fox Theater Project was a major development, which required a substantial amount of equity capital based on conventional commercial real estate underwriting standards. With a total project cost of $91 million, additional funding sources were needed to limit the amount of capital contribution required by the Agency to fund the project.

Obtaining $32 million of private sector funding offset the amount of capital contribution required by the Agency to fund the project. The financing was successfully finalized and closed during a period of great uncertainty in the financial markets.

The governance structure created to attract private sector capital for the Fox Theater Project was necessary and adequate

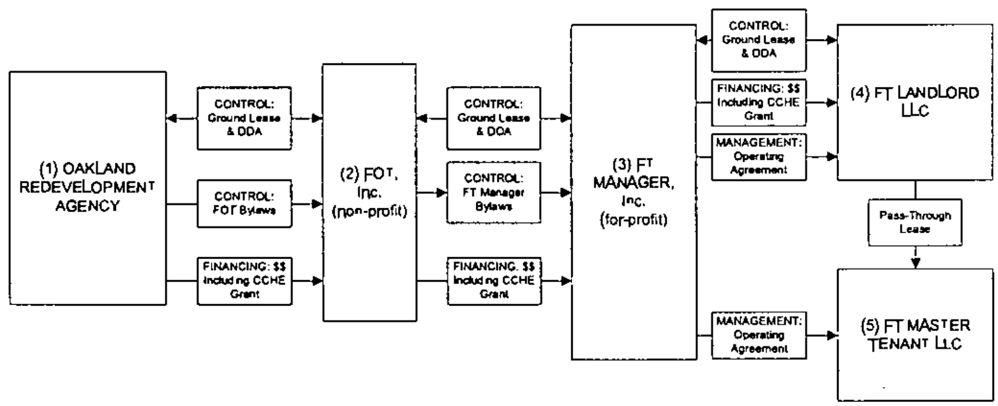
With a stated requirement to maximize the use of alternative financing and minimize the Agency's capital contribution, the sponsorship and organizational structure of the borrowing entity(s) was critical to attract private capital and/or investment.

The Fox Theater Project is a structured finance transaction with Tax Credit investors arranged by Bank of America and several related Community Development Entities (CDE). The capital structure included Historic Rehabilitation Tax Credits (HRTC) and New Markets Tax Credits (NMTC). The investors in tax credit programs require the use of pass through entities (limited liability companies ("LLC") or limited liability partnerships (LLP), which allow for the exchange of tax credits for capital from the investors; additionally, the Fox Theater Project investors utilized borrowed capital (Leverage Investment) to increase the financial returns on their investments in the project. This resulted in the use of pass through entities to raise the equity capital for the project. This method of structure finance is very complex and carries a higher expense load for professional fees and reserves.

The structure of the development entity, FOT, Inc., a California Non-Profit Corporation added another degree of legal and operational complexity. It was prudent to segregate the development and project activities into a separate legal entity. The use of a non-profit public benefit corporation was an acceptable vehicle to use. Due to the non-profit status of the development entity, it would ensure that the public's interests were the priority and the normal developer's profit motive was removed. Additionally, it provided the vehicle to allow the Agency to transfer assets, grants and capital into FOT, and FOT's subsidiaries and Fox Theatre Manager. This structure provides the Agency with a governance structure to control the entire development and provide tort protection to the Agency. The lower tier limited liability companies (FT Landlord and FT Master Tenant) that capital flows through were necessary to meet the investor requirements.

RECOMMENDATIONS	
We recommend that the City Administration and Agency Management:	
Recommendation #16	Adopt policies and procedures to conduct a comprehensive financial feasibility analysis of future Agency project's scope and adjust the relevant components/elements of the financial feasibility model. The financial feasibility model for projects should list, but not be limited to the following elements. Further, the model must be structured around project specific features. • Project Scope/Description • Organizational Structure • Resumes of Principals • Operators and/or Developers • Statement of Sources and Uses • Project Budget and Financial Projections • Financial Statements • Site Control and Plan • Building Floor Plan • Appraisal/Valuations "As-Is", "As-Completed", at "Stabilized Operation" • Environmental Assessment • Financing Commitments • Equity Requirement • Tenant Leases or Letters of Interest • Job Creation Projections
Recommendation #17	Consider hiring competent third party assistance with relative experience in the area of financial feasibility modeling and implementation to the extent that the Agency lacks the time, staff or competency.

FOX THEATER OWNERSHIP STRUCTURE



NOTES:

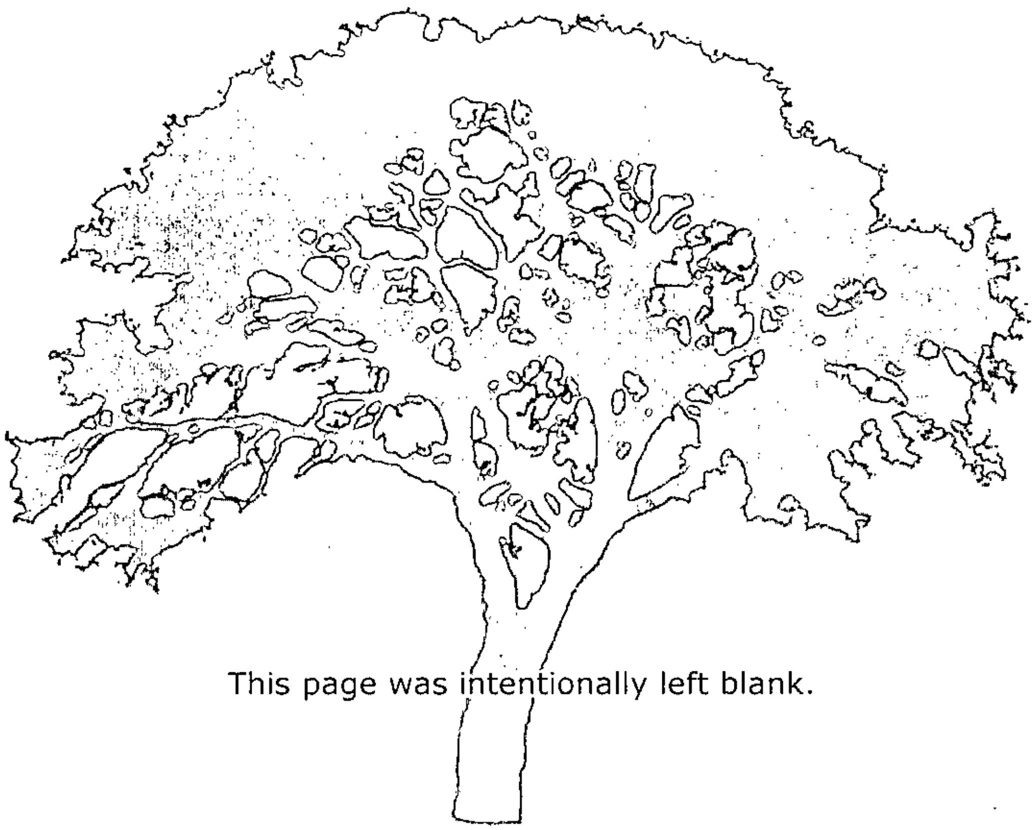
(1) ORA is the CCHE grant recipient and will control the project via the Ground Lease and DDA Agreement. The Agency will maintain further control via the FOT Bylaws. The Board of FOT is comprised of ORA/ City of Oakland employees. The ORA Agency Administrator will appoint all successors to the Board.

(2) FOT, Inc. is a non-profit entity controlled by ORA and will control the project via the Ground Lease and DDA Agreement, which will assign to FT MANAGER. FOT will maintain 100% ownership/ management of FT MANAGER via the FT MANAGER Bylaws.

(3) FT MANAGER, Inc. is a for-profit entity controlled by FOT and will control the project via the Ground Lease and DDA Agreement, which it will assign to FT LANDLORD. FT MANAGER will manage both FT LANDLORD and FT MASTER TENANT via separate Operating Agreements. FT MANAAGER exists to implement the tax credit structure.

(4) FT LANDLORD LLC exists to capture New Market Tax Credit equity financing and will rehabilitate the Theater. FT LANDLORD is the entity that will enter into a construction contract with the prime contractor and will be the borrower on the construction loan.

(5) FT MASTER TENANT LLC exists as a vehicle to obtain Historic Tax Credit equity funding for the rehabilitation. FT MASTER TENANT will have an investor, but all management authority will be FT MANAGER (as indicated in Note #3 above).



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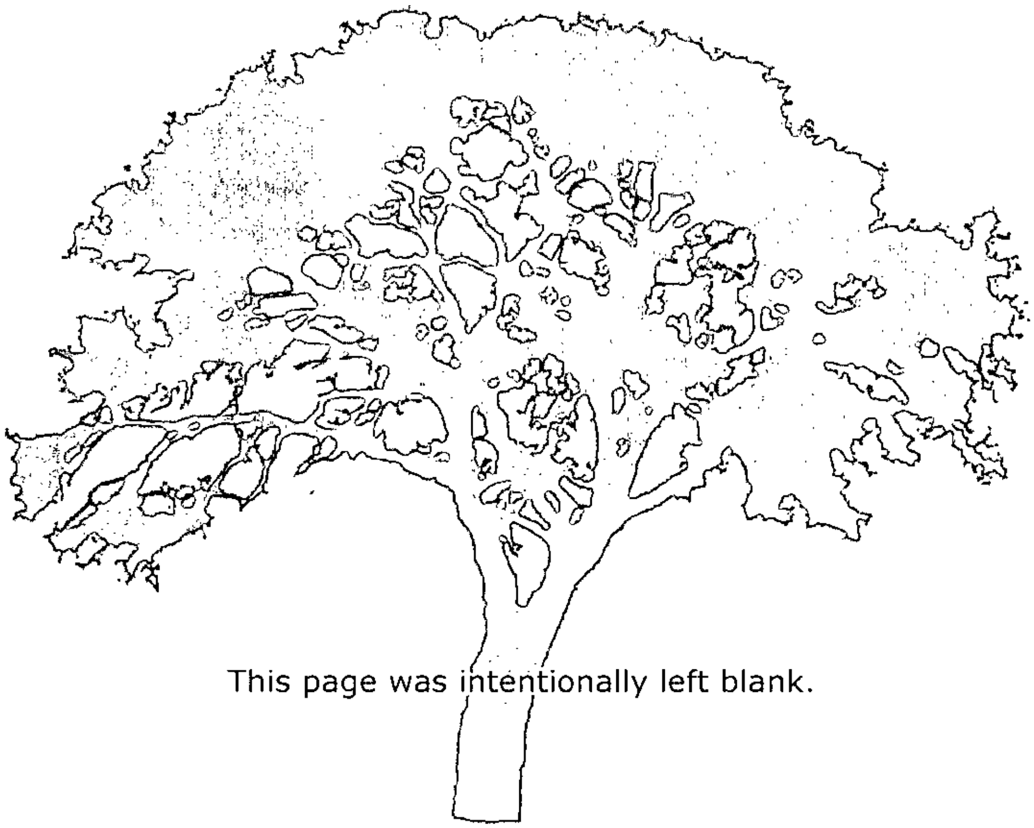
ADMINISTRATION RESPONSE



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Fox Theater Renovation Project
Performance Audit Timeline

Performance audits are most effective when the there is collaboration between the auditor and auditee. In order to maximize this collaborative process and to ensure public trust in the integrity of our audits, my Office offers the Administration multiple opportunities throughout the audit to provide all the relevant documentation and materials to support their position.

However, it is my responsibility to the public to ensure that they are provided with timely oversight of their tax dollars and that the findings and recommendations from our audits are presented in a responsive and appropriate timeframe.

After accommodating multiple extension requests from the Administration that spanned June through September, City Administrator Santana and I have agreed that it is most appropriate to move forward with the publishing of this report at this time. An initial response was provided to my Office on August 12th, and we agreed that any additional response from the Administration along with my Office's response to this response would be published in the future.

In an effort to supply a clear, accurate, and unambiguous view into this audit's process, a timeline has been provided below.

COURTNEY A. RUBY, CPA, CFE
City Auditor

Audit Step	Date
Executed Audit Contract	September 30, 2010
Entrance Conference	November 16, 2011
Preliminary Findings Meeting held between Auditee and City Auditor's Office • Opportunity to discuss preliminary findings and agree on additional documentation still to be submitted by the Auditee	April 14, 2011
Preliminary Draft Report provided to Auditee • First time Auditee sees findings in report format with audit recommendations	May 31, 2011
Exit Conference held with Auditee • Opportunity to discuss again audit findings, as well as recommendations, report tone, and any last documentation or input from the Auditee	June 10, 2011
City Auditor's Office granted Auditee additional time to provide documentation	June – July, 2011

Final Confidential Draft Report provided to Auditee • Draft reflected additional information submitted by the Auditee that merited edits to the preliminary draft • Detailed, point by point response provided by City Auditor's Office to Auditee's written comments regarding the preliminary draft • Requested Auditee to provide detailed Administration Response to each recommendation to indicate level of agreement and steps already taken or plans to implement the recommendations	July 11, 2011
Received Auditee's Administration Response to Final Confidential Draft Report • City Auditor's Office granted extension of two weeks to Auditee to provide Administration Response • Administration Response did not provide recommendation level review • Administration Response introduced new information not previously provided to the City Auditor's Office	August 12, 2011
City Auditor's Office provided Detailed, Point by Point Response to Auditee and Revised Final Confidential Draft Report • Highlighted edits to the report where Auditee and City Auditor's Office agreed to changes of certain dollar amounts based on additional documentation submitted by the Auditee: 1. Final project cost of $91 million rather than $95 million 2. Actual Land/Improvement costs of $6.5 million listed in an exhibit rather than the appraised value of $9.7 million 3. $1M from the Agency Bridge Loan was removed as it is already included in the Prop 40 grant amount • Highlighted information not previously provided to the City Auditor's Office by the Auditee that resulted in minimal changes to the revised final draft report • Highlighted Auditee statements/positions on issues that were previously unexpressed and/or shifted without providing supporting documentation that did not result in any changes to the revised final draft report • Provided Auditee three additional weeks to revise the previous Administration Response by September 16th	August 26, 2011
Auditee communicated a request for at least two additional weeks to review the revised Final Confidential Draft Report • City Administrator's Office notified City Auditor's Office on September 15 that due to the City Administration's current constraints, it would not be able to provide the revised Administration Response • City Auditor and City Administrator agreed that given the minimal changes to the revised final draft report, the August 12th Administration Response would be used and when the revised Administration Response was ready, it would be issued under separate cover	September 16, 2011

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CITY HALL • 1 FRANK H. OGAWA PLAZA • OAKLAND, CALIFORNIA 94612

Office of the City Administrator
Deanna J. Santana
City Administrator

(510) 238-3301

August 12, 2011

Courtney Ruby
City Auditor
City of Oakland
1 Frank H. Ogawa Plaza, 4th Floor
Oakland, CA 94612

Re: Fox Theater Project Performance Audit

Dear City Auditor Ruby:

I am pleased to provide you with the Agency Administration's Response to the Fox Theater Project Performance Audit. Staff Reviewed the July 11, 2011 Final Confidential Draft Report of the Fox Theater Project Performance Audit.

This project was one of the most complex endeavors this, or any other redevelopment agency, has completed. The Fox Theater was a ten year project that was planned and developed during several administrations. While I have taken time to review and comment on the audit and responses from Redevelopment staff, the management of this project was considerably before my time and I have not had the opportunity to validate the information provided by either staff or the Auditor. Through this cover letter I am forwarding the responses prepared by staff involved in the project. If there are any factual errors, I am interested in hearing about them.

The Fox Theater project is the crown jewel of Oakland's redevelopment efforts.
It is a nationally-recognized success story and has transformed the surrounding area. The Fox Theater is an achievement not merely for the rehabilitation of an historic structure, but also because it is the linchpin in the Oakland Uptown area's economic revitalization. It has achieved success beyond its projections. Not only does the Fox Theater bring thousands to its performances each week, but the surrounding businesses have benefited from this activity and the removal of the blight of the formerly dilapidated building. Further, new restaurants, entertainment venues, and bars are sprouting up in the area as well as other businesses moving in.

The Fox Theater's success does not mean that we camot use our experience with this project to improve how the City handles similar undertakings in the future. To that end we appreciate the City Council's request that your office undertake this performance audit. We wish to thank the City Auditor's Office for the effort in analyzing a complex project and working with Agency staff in preparing the final audit. We have carefully considered the recommendations in the audit, and while do not agree with many of the audit's findings, we believe the reconimendations that the audit makes will help improve our procedures for future projects. Many of the areas where there is an absence of agreement stems from the need to provide greater context or additional information to establish our perspective and provide clearer information.

Although I am new to the position of the Oakland Redevelopment Agency's Administrator, I can see that Agency staff and the City Attorney's Office spent considerable time working on this audit, assembling the facts, reviewing the issues, and the audits recommendations. I also understand that this staff immersed itself in the Fox Theater project and was in many ways responsible for the success of this project.

I look forward to working with your office to target key issues from the audit to improve management of future City and Agency projects.

Sincerely yours,

Deanna J. Santana
Agency Administrator

Attachments

- Memorandum from Patrick Lane, Redevelopment Manager
- Point by Point Response to the Fox Performance Audit

August 12, 2011

To: Deanna Santana, City Administrator

From: Patrick Lane, Redevelopment Manager

Cc: Dan Lindheim, Margaretta Lin, Walter Cohen, Gregory Hunter

Re: Response to City Auditor's Audit of Fox Performance Audit

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I reviewed the July 11, 2011 final draft of the City Auditor's Fox Theater Project performance audit. I summarize my response below. A more detailed response to the audit's findings and recommendations is provided in Attachment A, Point by Point Response to the Fox Performance Audit.

1. The Fox Theater Project Was Always Envisioned as a Full Renovation Project And Costs Were In Line With Council Information and Approvals

Contrary to the audit report findings, the Fox Theater project since 2001 was envisioned as a full renovation project. One of the concepts, the "Ruins/Basics" concept, contemplated different phases to be completed as time and funds were available. All significant aspects of the project were presented to City Council and at numerous public meetings; the Chronology of Fox Theater Council Actions is included with Attachment A.

In 2001, the Council was supplied with a report from a nationally recognized theater consultant summarizing the Fox Theater Master Plan, with details of 5 concepts or options for development, including: Alternative 1 - "The Basics" ($43.7 million); Altemative 2 - "The Roadhouse" ($66.9 million); Alternative 3 - "The Arts Center" ($69.0 million); Alternative 4 - "Existing Storefront" ($19.0 million); and Altemative 5 - "New Storefront"($36.4 million). In 2003, the Coimcil envisioned a full renovation of the Fox Theater that would start with the Basics approach because of limited financing. The full renovation was plarmed to be done in future phases when additional funding was obtainable. When the additional funding from tax credits and government grants was available in 2006, the project proceeded as a full renovation.

Futher changes in project costs occurred due to the change in the concept and scope of the project, as well as due to the availability of new outside funds for the project. Another Planet Entertainment, Inc. was selected to operate the theater and had new requirements for the project. Oakland School for the Arts also expanded from a 400 to 600 students. The Council was presented with costs for various options and the final costs were essentially the same as costs estimated by the theater consultants who evaluated the renovation options. The final development costs for the Fox Theater, including acquisition, pre-development, soft and hard construction costs, was approximately $91.5 million. These actual costs were in line with the development costs presented to the Council in 2001 and mentioned again in 2003 and 2004 for the complete restoration of the theater. The final development costs were close to the estimated cost for the "Roadhouse", $66.9 million in 2001, when adjusted for inflation and the land costs, approximately $90.0 million in 2006 when the project began construction or $98.3 million in 2008 when the project was completed. Even when adding all the grants and loans for upgrades requested and partially paid by APE and OSA, and the additional improvements for the "Restaurant Space", the development cost of the theater only increased a nominal amount. It is our understanding, through Council's discussions and actions [Attachment A quotes the Reso which shows it was the intent of the Council], that the Council always intended a full renovation of the Fox Theater as ultimately occurred. This is not a project that suffered from "scope creep."

We are concerned that the audit analysis incorporated items that are not actual costs and/or sources and made other questionable assumptions, including:

a. The audit's Funding Sources and Costs used the estimated value of the land in the Final Project ($9.7 million), which was $3.2 million more than the cost ($6.5 million), but used the actual cost or left it out of the 2004, 2005 and 2006 comparisons, thereby inflating the increase over time.

b. The audit compared Funding Sources from the June 27, 2006 staff report with Project Costs from July 18, 2006 supplemental staff report. The July 18, 2006 supplemental staff report updated and replaced the sources and uses information from the earlier report and should have been used in both the audit's Funding Sources and Project Costs comparisons. Not doing so resulted in the audit showing a seemingly unbalanced budget in 2006.

c. The sources and uses repeated an item, Prop 40 and Proposition 40 Grant, and included reserves, a non-development cost that could be used for repayment of the Agency loans and/or the eventual buyout of the tax credit investors. Together these resulted in inflated costs for the Final project.

These actions inflated the project costs to $95.6 million. The audit also overlooked the fact that the "Ruins Concept" required both operating subsidies and future improvements.

The audit also found that "Staff communications to City Council regarding project cost and scope appeared to be incomplete"; but, in fact, the Council was provided complete information, especially significant changes in project concept and scope. All project funding was explicitly addressed on more than 14 occasions in Council reports, resolutions and Committee and Council discussions, see Exhibit A, Chronology of Fox Theater Council Actions, in Attachment A - Point by Point Response to the Fox Performance Audit. These reports and various documents referenced in them, including: the Fox Theater Master Plan Report; the Initial Study/Mitigated Negative Declaration; and the report required under Section 33433 of the California Health and Safety Code ("33433 Report"), must be considered collectively. The reports all reference the earlier activities and incorporate them into the material presented to Council, including dates of previous reports. When the Council needed more information, it requested it as it did in requesting a supplement report for the July 18, 2006 meeting and other meetings. More information and details were presented to Council than perhaps any project other than the Army Base; nevertheless, the Agency Administrator has requested that we conduct a brief review to identify any "lessons learned" regarding whether there was an absence of required policy action on the part of Council for the purpose of analyzing areas where the legislative process could have been more clear or transparent..

2. The City Did Not Pay for Any Project Costs

Contrary to the audit finding, the City did not absorb any increased project costs or fund any project costs at all. First, the City (General Fund and other City fimds) did not fund the project at all. This was a Redevelopment Agency project and only Redevelopment funds were involved. Second, much of the increased costs were financed through tax credits, conventional loans, and outside grants. The Agency did make additional loans to support the project after construction began. Many of those loans are on repayment schedules and/or will be reimbmrsed from grants. OSA is expected to have repaid over $2.7 million by the end of the year, of which $1.0 million has been received by the Agency. The other Agency loans (approximately $39.8M) may be partially repaid but the remaining loan balances caii be converted to Agency equity ownership of the Fox at the end of the financing process. The percentage of the project to be funded by the Agency actually fell from 59% to 53% from 2004 to 2009. In fact, the City budget benefits fiom increases in tax revenues direct fiom the theater, restaurant, and bar operations in the project and indirectiy from the additional economic activity the theater generated for bars, restaurants and other retail and entertainment businesses in the Uptown Area and throughout the Downtown.

3. The Fox Theater Nearly Doubled the City's LBE and SLBE Participation and Met Council Requirements and Federal Regulations

The Fox Theater achieved 37% Local Business Enterprise (LBE) and Small Local Business Enterprise (SLBE) participation. The project's LBE/SLBE participation was nearly double the City's requirements (20%), and was greater than the FY 2007-09 Citywide LBE/SLBE participation (35.92%) and much greater than the FY 2007-09 Citywide LBE/SLBE participation for Large Projects (28.84%). Although the audit states the developer's waiver of the competitive bidding was to increase LBE/SLBE participation, the City Council resolution approving waiver for competitive bidding by the developer was for the purpose enabhng the developer to "maintain strict project schedules" indicating concern that a bid process could slow the project, particularly if a bid contest resulted in addition to "fiexibility to increase local and small business participation and attempt to attain the goal of fifty percent (50%) Local Business Enterprise (LBE) and twenty percent (20%) Small Local Business Enterprise (SLBE) participation" [Agency Resolution No. 2006-0057 C.M.S. (July 18, 2006)]. The project fully met the Council requirements and S/LBE Program goals.

Page 7 of the draft audit questioned compliance with federal regulations was a $600,000 HUD grant (less than 1% of project cost), but that grant was awarded long after most contracts had been let. Under federal guidelines, in general, projects with federal funding are to be competitively bid, but waivers are permitted. The applicable federal regulations permit awarding of contracts, such as design-build or construction manager contracts, on a non-low bid basis (price being one of the factors), 24 CFR § 85.36(3). Moreover, the federal procurement regulations allow for modification of award procedures when exigencies will not permit a delay. As stated above the primary reasons for modifying the contract award process was to avoid costiy project delays. The Agency could not undo all of the previously awarded contracts long after the fact just because the federal grant was awarded. The grant was for two specific purposes: (i) electrical; and (ii) painting of the historic ceiling. The painting work competitively bid and awarded and the electrical contract was design/build.

4. Project Change Orders are Common Industry Practice and Contracting Procedures and Internal Controls were Appropriate Including Monitoring of Turner and CCG's Contracts and Payments

The project had industry standard procedures in place for the development of the Fox Theater. Turner submitted documents (payment requests, requests for information, change orders, etc.) to the rest of the development team for processing and/or approvals. The development documents were reviewed by architects (Architectural Dimensions, but also at times KPA Group, ELS and Starkweather Bondy Architecture LLP), the fee developer CCG (development staff and construction experts), Redevelopment/FOT representatives (two architecture and renovation construction experts) and Bank of America's representatives. FOT and the Agency also had professional staff dedicated to reviewing payment requests, draws, invoices and budget changes before they were submitted to Bank of America for review and approval in a standard construction loan draw process. The audit had several findings regarding project fiscal management, which are covered by the following three factual areas:

a. The audit does not acknowledge that change orders are common in construction projects. While the number of change orders and combined increase were large, 34% or $16,124,637 over the initial contracts of $47,793,563, this is typical of historic renovations. This is particularly true for a building that was vacant for 35 years and when federal and state historic standards are required for the construction. Many of the change orders were the result of meeting historic renovation standards or were requested by the tenants. Staff constantly negotiated change order requests to lower prices or refused them outright. Included in the final 28 change orders processed at the end of the project were nine that were rejected ($533,682), 13 that were reduced an average of 35% (from $781,460 to $505,026) and only six that were accepted as proposed($100,543). From initial proposed change orders to final approved change orders these 28 items were reduced from $1.4 million to $610,358 or 57%.

b. The audit's finding of $178,726 in unsupported expenditures to CCG was a clerical mistake. The auditors missed one month's worth of invoices in their calculations because it was missing from two spreadsheets covering the periods just before and just after the missing month, January 2007 when the project transitioned from predevelopment to construction. The Auditor was supplied documentation verifying these legitimate expenses, yet the report has not been corrected.

c. CCG was reimbursed for $178,843 in work not authorized in the contract. There are two issue related to the developer fee payments: 1) payments to CCG for six months not covered in the contract and amendments, but justifiable for work performed during this period; and 2) over-payments to CCG that might not be justifiable and should be recovered. There is a period between completion of 90% construction documents, Amendment 2 of the CCG contract which ended March 31, 2006, and closing on the financing/start of construction, Amendment 3 of the CCG contract which began August 21, 2006. This was a critical period during which FOT and the various development entities were created and CCG contract was being transferred to this new entities, the construction work was being bid, the tax credit investor was being selected, the deal was being structured and the project was being approved by the Council. In order to keep the project moving and on schedule, CCG performed work for six months while it was out of contract, April through September 2006. Therefore the additional fees of $142,500 paid for this six month period were justifiable. The FOT board previously authorized sufficient authority to amend CCG's contract to cover the missing period. The audit also identified two additional overpayments that do not seem justifiable. Staff is reviewing $38,343 in payments identified by the auditors to determine whether the payments were appropriate and has requested justification from CCG.

5. The Project Was Successful at Raising Outside Funds And the Feasibility Analysis Provided was Comprehensive

We concur with the audit findings that the project was successful at raising alternative funding, including private funds. There were two clear points in the audit:

a. CCG, FOT and the Agency were successful in creating and sustaining a complex governance structure to generate Historic and New Markets Tax Credit equity. Syndicating the tax credits required the Agency to create a non-profit corporation (FOT), a for profit corporation (Fox Theater Manager) and two limited liability companies (Fox Theater Landlord LLC and Fox Theater Master Tenant LLC). This structure required a team of attorneys, accountants and four community development entities ("CDEs") with New Markets Tax Credit allocations - Bank of America, National Trust for Historic Preservation, Charter School Development Corporation and Local Initiatives Support Corporation. CCG, FOT and the Agency have been able to manage the development and operations of this very complicated project.

b. CCG, FOT and the Agency were successful in obtaining $32.0 million in capital and debt from Bank of America to fund the Fox Theater Project. Bank of America even continued to increase its investment in the Fox Theater as the national economy declined and the value of the tax credits was reduced. Bank of America provided all of the debt ($6.5 million) and equity ($26.0 million) for the project and the governance structure was set up to the bank's requirements. The initial equity offer from Bank of America was $15.0 million in June 2006, but by December 2010 this had grown 73%. CCG was instrumental in attracting Bank of America and negotiating the deal. Bank of America had worked with CCG on the Rotunda Building and based on this experience invested in the Fox Project.

The project prepared comprehensive feasibility analysis. Although the audit found that "the financial feasibility analysis was inadequate for the scope of the project", this is inaccurate. The project scope was detailed as far back as 2001 in the Fox Theater Master Plan. A project budget or sources and uses of funds was provided to the Council on several occasions and a much more detailed spreadsheet was prepared and updated monthly as part of the construction draws starting in early 2007. Detailed analysis or projections were used to meet the requirements of Bank of America and the CDEs. Although these 37 page detailed projections were never shown to Council, they were prepared several times in 2006 and again in 2009. Financial statements are prepared for all of the four entities but audit financials are not available for FOT because they are not needed and are expensive, approximately $12,000 per year. These documents would only be useful if the Agency was planning to use FOT on another project. FOT is a single purpose entity and another entity would be created for any future project.

6. The Project Has Been Instrumental in Downtown's Economic Revitalization.

The Fox Theater was not developed as a stand alone project. The project was seen as both filling a major hole in the Uptown Area and as catalyst for other economic revitalization in the surrounding areas. The project took a rundown, decrepit blight and turned it into a major asset. The area now has two beautifully restored theaters that are the heart of an emerging entertainment district. The Theater attracted over 160,000 paying customers its first year, over 180,000 its second year and is projected to reach 200,000 in this, its third year. This is almost double the initial projection of 100,000 paying customers per year for the first three years. These visitors have enlivened the whole area and created a demand for new bars, restaurants, cafes, and entertainment venues, which continue to open—all of which contribute to Oakland's economy and tax base. The project has been a major artistic and economic success. In addition, the Fox Theater has received numerous awards celebrating its historic restoration see Exhibit B - List of Awards and $pecial Events, in Attachment A - Point by Point Response to the Fox Performance Audit.

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ATTACHMENT A

Point by Point Response to the Fox Performance Audit

1. **RESPONSE TO CHAPTER 1** – Fox Theater Project Scope and Costs. The Fox Theater Project Was Always Envisioned as a Full Renovation Project And Costs Were In Line With Council Information and Approvals

Contrary to the audit report findings, the Fox Theater project since 2001 was envisioned as the full renovation project that was ultimately completed and the project scope and costs did not increase significantly. One of the concepts, the "Ruins/Basics" concept, contemplated completing the full renovation phases as funds became available. Other concepts included full renovation of the theater. All significant aspects of the project were presented to City Coımcil at numerous public meetings; see Exhibit A, Chronology of Fox Theater Council Actions.

A. Final Project costs were in line with those presented to the Council at initial conception when the Council was presented the various options from the Fox Theater Master Plan on April 24, 2001. On April 24, 2001 Council was presented with an informational report outlining various options for rehabilitating the Fox Theater and the estimated costs for each. The report was based on analysis by Hardy, Holztman, Pfieffer - nationally recognized theater consultants. In 2003, after considering several proposal for the Fox renovation, selected California Capital Group to proceed with developing plans and costs estimates for the first phase, based on the ruins concept, of an ultimate completed renovation. The resolution approving CCG funding clearly intended the ruins concept to be a temporary first step in the theater renovation.

> **WHEREAS**, the CCG development team has prepared concept drawings and detailed cost estimates for revitalizing the Fox Theater into a cabaret-style performing arts venue that would activate the Fox for an unspecified time period before future funding could be obtained for a full theater restoration [Agency Resolution 2003-83 (December 2, 2003)];

In 2006, when substantial additional sources of funds became available primarily through federal tax credits and state grants, the project could be accelerated, skip over the limited "ruins" phase, and move directiy to the full renovation. What's more, the growth in costs was not as great as presented by the audit and even with the growth in Agency funding, other sources grew even faster and the Agency's share of the costs declined. The audit finding regarding the increase in costs is distorted and misleading. The starting point for the audit cost analysis was the ruins concept that was never intended to be the final project and never started nor funded. The figures used in Exhibit 2 Funding Sources and Exhibit 3 Comparison of Project Costs were from diverse sources and the auditor was unable match the line items for an accurate comparison. Some of the discrepancies include:

1) The fiill project was presented in 2004 as an alternate and the final project costs were very close to the estimate by the theater consultants when adjusted for inflation. The

final development cost of the theater, including the purchase price and improvements previously paid by the Agency, was $91.5 million. The Fox Master Plan in 2001 estimated the full theater renovation "Roadhouse" concept at $66.9 million. Inflation in construction costs between 2001 and 2006 was approximately 24.8% or 4.5% per year based on Engineering News Record San Francisco City Cost Index/Building Cost Index. By adjusting the 2001 estimated full renovation cost for inflation, that cost at actual completion would have been $90.0 million or $98.3 million in 2008 when the project was completed. Even when adding all the grants and loans for upgrades requested and partially paid by Another Planet Entertainment ("APE") and Oakland School for the Arts ("OSA"), and the additional improvements for the "Restaurant Space", the development cost of the theater only increased a nominal amount or were actually less than the first estimates.

2) The comparison is between different projects – the ruins concept for a 500 seat cabaret venue and renovation of wrap around building for OSA versus the full theater restoration of a 3,000 person performance venue and renovation and the addition to the wrap-around building for the OSA, a restaurant and bar.

3) Both major tenants of the Fox required additional improvements. When the project was being analyzed in 2004 and 2005 under the original contract with California Capital Group ("CCG") no operator had been found for the theater and OSA was still fund raising and programming its needs. The budget prepared at the end of this analysis was much different than what was built. Both tenants provided capital funds and demanded scope revisions, including:

   a. APE provided $500,000 for tenant improvements in its lease, but required substantial changes to the theater that were over and above its contribution. APE essentially requested the fully restored theater minus the fixed seating on the main floor to allow the theater to operate with either a 3,000 person capacity with general admission or approximately 2,500 person capacities with movable seating.

   b. OSA obtained the CBS billboard revenue and used this for lease payments which then leveraged a $6.5 million conventional loan. OSA also pledged to provide a $1.5 million Charter School Facility Incentive Grant, which OSA was unable to secure; instead OSA provided cash through a fund raising campaign. With these funding sources provided by OSA, came an expanded scope including providing arts spaces in the new 2nd and 3rd floor additions to the two one-story wrap buildings. OSA also pledged to build out the $3.7 million in tenant improvements for these additions. The project scope and funding sources were substantially motivated by the tenant driven changes.

4) The "Ruins Concept" anticipated Agency on-going operating subsidies and major renovations in the future, with additional Agency expenditures. Comparing the final renovation cost of the theater to the estimated costs of the "ruins concept" (first phase only), over estimates the overall increase in actual project costs substantially. In the ruins concept presented to the Council, the Paramount Theater of the Arts would have been the operator, and would have required a $500,000 per year

operating subsidy from the Agency. The Theater would have initially operated at a reduced capacity, no balcony and only 500 to 600 seats on the first floor, meaning limited ticket revenue. It would have also required major additional improvements in the future to increase capacity and ticket sales and reduce the operating subsidy, but with additional Agency development subsidies required. This would be more expensive than what was actually built because it is more expensive to do work in multiple phases and it would interrupt operations at the theater.

5) The budgets presented to the City Council in 2004 and 2006 excluded the cost to complete, although the reports describe the previous costs - \$6.5 million spent by the Agency on purchase of the property, improvements and predevelopment planning. The audit compared these sources and uses with a Final development budget that for tax credit purposes included appraised value of the FOT lease with the Agency \$9.7 million. Thus the Audit's use of the \$9.7 million figure exaggerates costs in the final cost figure; to be accurate either the cost to the Agency of \$6.5 million should be included in all sources and costs columns or the \$9.7 million should be used in all of the previous budgets for the comparisons.

6) The land cost used for the Final sources and costs in the audit is the appraised value of the lease and does not reflect actual costs. This is compared to the actual costs in 2004 and 2006, thus inflating the audit figure used for costs increases. For tax credit purposes the appraised value of the FOT lease with the Agency \$9.7 million was used in the final development budget as part of FOT's equity contribution. In addition, the land costs are not included in the 2004 and 2006 sources, even though these sources had already been provided by the Agency.

7) The audit compared Funding Sources from the June 27, 2006 staff report with Project Costs from July 18, 2006 supplemental staff report. The July 18, 2006 supplemental staff report updated and replaced the sources and uses information from the earlier report and should have been used in both the audit's Funding Sources and Project Costs comparisons. The July 18, 2006 supplemental staff report was provided at the meeting Council approved the DDA. This report included: 1) new bid information from Turner Construction; and 2) additional information from the Bank of America -- the tax credit investor and construction/permanent lender -- and other fimding sources, which substantially increased the sources and uses. Using the two different reports resulted in the audit showing a seemingly unbalanced budget in 2006.

8) The audit comparisons double count sources in the Final column; the Agency Bridge Loan for Prop 40 is the same as the Other Funding Sources Proposition 40 Grant. The audit also counts reserves and other non-expenses in Final Project Costs. Both of these duphcations overstate the increases.

9) The use of Historic Tax Credits in the project required additional improvements in order to comply with the historic preservation requirements and receive any historic tax credits. The National Parks Service required revisions to the Phase II application for certification of the project for historic tax credits before the start of construction, including reconfigured the new building to set back from the historic building farther

and other smaller changes. The Phase III required further revisions to the building after the receipt of the temporary certificate of occupancy, including building out the restaurant space and minor finish revisions such as painting the natural wood window frames brown. Not making these changes would have prevented the project from receiving approximately $15.7 million in enhanced tax credit equity.

B. The City Did Not Pay for Any Project Costs. Contrary to the audit finding, the City did not absorb any increased project costs or fund any project costs at all. First, the City (General Fund and other City funds) did not fund the project at all. This was a Redevelopment Agency project and only Redevelopment funds were involved. Second, much of the increased costs were financed through tax credits, conventional loans, and outside grants. The Agency did make additional loans to support the project after construction began. Many of those loans are on repayment schedules and/or will be reimbursed from grants. The other Agency loans (approximately $39.8M) may be partially repaid but the remaining loan balances can be converted to Agency equity ownership of the Fox at the end of the financing process. The percentage of the project to be funded by the Agency actually fell from 59% to 53% from 2004 to 2009 as the following table shows:

The important comparison should be between Agency and non-Agency sources, which fell as a percentage as the development team was able to secure additional funding sources. Although several grant sources were not secured, the project continued to secure additional grant and other equity and loan sources. In particular, Bank of America invested additional equity because of increased tax credits and also brought in a new source of New Market Tax Credit enhanced debt through the Local Initiatives Support Corporation. This change funding sources for the Fox Theater can be seen in the following table:

Changes in Funding Sources

	2004	2005	2006	2009	Increasse
Agency ($Million)	19.65	20.95	33.30	50.13	30.48
Other ($Million)	13.85	17.95	30.40	44.07	30.22
Total Sources ($Million)	33.50	38.90	63.70	94.20	60.70
Agency Percentage	59%	54%	52%	53%	-5%
Other Percentage	41%	46%	48%	47%	5%

While the City did not pay for any of the costs, it benefits from increases in tax revenues direct from the theater, restaurant, and bar operations in the project and indirectly from the additional economic activity the theater generated for bars, restaurants and other retail and entertainment businesses in the Uptown Area and throughout the Downtown.

C. The project was unable to secure approximately $5.6 million in grant funds, $9.4 million less than stated in the Audit. In addition OSA has repaid $1.0 million of the funds it borrowed from the Agency a will repay the remaining $1.7 million by the end of the year reducing the unsecured funds to approximately $2.9 million. Furthermore, the Council was never told all of these grants would be available at the same time and the amounts mentioned in most of the reports was the maximum allowable not the amount the project was likely to receive. In addition, some of the grants replaced other grants and some of the grants were additional funds to earlier grants where the project had not received the full amount the project was eligible for and applied again in later rounds of applications. The Agency provided a $7. 5 million bridge loan for several grant sources that only partially materialized. This finding is based on the following sources:

Performance Audit - Funding Sources that was not secured	
$1,200,000	Federal Charter School Facility Grant
3,682,000	OSA Capital
60,000	Bank of America Grant (only received $190,000 not full $250,000)
4,983,922	Proposition 55 Grant
1,048,607	Proposition 40 Grant (only received $4.0 million not full $5.0 million)
375,000	State Façade Grant (only received $375,000 not full $750,000)
770,000	FOOF (Embarked on $1.0 million - but only raised $230,000)
3,006,000	HUD Funding (only received $594,00 not full $3.6 million)
$15,125,529	Total for unsecured funding

There seem to be several misunderstandings related to the list of funding sources that were not secured above, including:

1) Federal Charter School Facility Grant ($1,200,000) - The grant was with OSA and OSA's providing it was requhed of OSA under its lease with FOT. When this source was not received, OSA made payments in lieu of the grant. A portion of the Bank of America grant mentioned below was also credited to OSA's obligation, per Bank of America's direction. The total received for this obligation was $1.5 million as required in the lease, $300,000 more than expected in the report to Council. This obligation was fully secured by OSA, therefore the unsecured amount was $0.

2) OSA Capital ($3,682,000) - The cost for OSA's tenant improvements was higher dian estimated, $4.5M instead of $3.7M. OSA paid for a portion directly, at least $2.2M, and borrowed $2.3M from the Agency. OSA is making regular payments and is expected to pay off the Agency loan at the end of this year. OSA's shortfall from the original capital estimate was only $1.5M. OSA has paid almost $1.0M and is expected to repay the remaining $1.7M by the end of the year. At that time the unsecured amount will be $0, until then it is $1.5M. It should also be noted that this was the additional amoumt that OSA had to raise to replace the Federal Charter School Facility Grant. In addition, this capital requirement came after project determined that the Proposition 55 Grant was eliminated as a funding source.

3) Bank of America Grant ($60,000) - The grant was received through Friends of Oakland Fox, Inc. ("FOOF") and was never part of the sources presented to the Council. It was paid in 3 installments, only the 1st of which was during the development phase. Two additional payments of $190,000 were received on 1/4/2010 and 1/21/2011. The 1st of these payments was part of tiie funds used to make the fmal payoff to Turner and the sub-contractors. FOOF received additional funds that were used for the grand opening gala and other fund raising events. These

payments should also be credited to the FOOF fundraising because they came through FOOF. The unsecured amount was <u>$0</u>.

4) Proposition 55 Grant ($4,983,922) - The grant was eliminated in the predevelopment phase when it was realized that the grant's requirements and process would not work with the proposed project. In discussion with the state, the Federal Charter School Facility Grant, which is also awarded through the state, was offered as a replacement for Prop 55. These 2 grants were therefore never expected together and have never been shown in the same budget to the Council. If the OSA payment is included in lieu of the Federal Charter School Facility Grant, and the Federal Charter School Facility Grant as a partial replacement for the Proposition 55 Grant, then the unsecured Proposition 55 Grant was <u>$3.5 million</u>. If the OSA Capital is considered a replacement for the Proposition 55 Grant, then the unsecured amount was <u>$0</u>.

5) Proposition 40 Grant ($1,048,607) – The project was awarded funds in three different application rounds and in the end was only $548,607 short of the maximum allowable grant. The Agency received an additional $500,000, but the funds could only be used for activities after the grant award and so have been used to fund the tenant improvements for the "Restaurant" and "VIP Space" on the corner of 18th Street and Telegraph Avenue. This area was left vacant until leases were signed. The tenant improvements have and will be completed in 2011 and processing of this grant continues. The portion not secured was only <u>$548,607</u>.

6) FOOF Fund Raising ($770,000) - If the Bank of America Grant is added to the other FOOF payments, $800,000 was raised. The unsecured portion would only be <u>$200,000</u>. What's more, the $1.0M estimate for FOOF fund raising was made in the predevelopment phase before any fundraising had begun. The fund raising was actually higher than estimated when the project was approved for development in 2006 and FOOF is continuing to fund raise to repay the $1.3 million Agency loan.

<u>Actual - Funding Sources that was not secured</u>

$0	Federal Charter School Facility Grant – OSA replaced funding
1,482,000	OSA Capital – OSA paid $2.2M and borrowed $2.3M from Agency
0	Bank of America – See FOOF
0	Proposition 55 Grant – This was replaced partially by Charter School Grant
548,607	Proposition 40 Grant (only received $4.5 million not full $5.0 million)
375,000	State Façade Grant (only received $375,000 not full $750,000)
200,000	FOOF ($230,000 plus 3 - $190,000 Bank of America Grant payments)
3,006,000	HUD Funding (only received $594,00 not full $3,600,000)
$5,611,607	Total for unsecured funding
($2,700,000)	OSA Repayments
$2,911,607	Funding Shortfall

If all of these issues are considered, the unsecured funds are only $5.6 million; which is offset by the approximately $1.0 million that has already been repaid by OSA and another $1.7 million that is expected before the end of the year. The Agency has had to make up for about $2.9 million in unsecured funds.

D. Council was provided complete information regarding Fox project costs and options. Based on review of Board reports and observing taped City Council sessions regarding the Fox Theater Project, the audit erroneously found no evidence that the City Council was provided with the following: 1) Project alternatives during the design phase; 2) Options to reject or modify the project; and 3) Changes to the scope of the project identified as required changes or proposed changes.

These conclusions are based on considering each report and Council action separately. Council reports often reference and discusses previous activities. The former reports are considered part of the current report. The reports and resolutions reference the earlier reports and other documents such as the Initial Study/Mitigated Negative Declaration and the report required under Section 33433 of the California Health and Safety Code ("33433 Report"). The 33433 Report includes: the estimated fair market value of the property at the highest and best use and the value of the interest conveyed under the disposition and development agreement also referred to as a reuse appraisal. The Council was provided reports and/or approved resolutions on 14 occasions, at least three of which included multiple meetings and reports, see Exhibit A, Chronology of Fox Theater Council Actions. The July 18, 2006 report when the Council approved proceeding with the project, was extensively detailed. The Council has always indicated when it needs additional information as it did for the 2006 report. The Council sought additional information on the subcontracts and it was provided in a supplemental report. If the Council needed additional information at any stage, it would have requested it. Several times the Council approvals were delayed for one or more supplemental reports (June 27 and July 18, 2006 for the DDA with FOT or December 1, 2009, December 15, 2009 and January 5, 2010 for the additional $2.0 million Agency loan).

More information and details were presented to Council than perhaps any project other than the Army Base. Nevertheless, the Agency Administrator has requested that we conduct a brief review to identify any "lessons learned" regarding whether there was an absence of required policy action on the part of Council for the purpose of analyzing areas where the legislative process could have been more clear or transparent..

2. **RESPONSE TO CHAPTER 2** - The Fox Theater Nearly Doubled the City's LBE and SLBE Participation and Fully Met Council Requirements and Met Federal Regulations

E. The S/LBE participation was higher than program requirements, the Citywide average and similar projects. The Agency, as a grantor and lender for the Fox Theater project, approved FOT's intent to modify contract award procedures. What the Audit failed to mention was that the approval of modified award procedures was done primarily to ensure the project moved forward in a timely manner, to lower costs, in addition to better enable the project to achieve higher LBE and SLBE participation goals. The resolution approving the waiver states the following as the rational:

> WHEREAS, in order to better enable the Developer to maintain strict project schedules with respect to project deadlines and flexibility to increase local and small business participation and attempt to attain the goal of fifty percent (50%) Local Business Enterprise (LBE) and twenty percent (20%) Small Local Busimess Enterprise (SLBE) participation that the Agency desires, it is recommended that the Agency authorize the Developer to waive competitive bidding and request for proposal requirements for all professional services, procurement and construction contracts needed to complete construction of the Fox Theater Project, and to employ non-competitive means for selection of contractors and award of such contracts; [Agency Resolution 2006-0057, p. 4 emphasis added].

The staff report discussed the need the need to modify competitive bidding requirements in order not only to achieve higher LBE and SLBE participation, but more importantiy to permit negotiating with contractors and subcontractors to lower costs, and to avoid the potential for bid disputes that might delay the project. [Agency Report, July 15, 2006, p. 16]. The project had two major concerns that required the project to move rapidly: 1) Fox Court needed to start construction or the Agency was liable for a fee for delaying the project and OSA was required to relocate and temporarily occupying space on San Pablo Avenue for its portable classrooms; and 2) these classrooms were restricting access to businesses in the area. The Agency was therefore motivated to complete the project as rapidly as possible. The report also noted at the outset that time was of the essence to proceed quickly because: subcontractor bids had been received, but were only valid for a limited time, and delays could cause the materials and labor to increase if the project had to be rebid; In addition, and most important, OSA had to move from its temporary site behind the Fox to make way for a housing project (which the Agency had already approved for that site) to avoid being in violation of an existing development agreement and a $400,000 increase in an agency loan to the developer. Thus, the use of modified contract award procedures was concerned with moving the project expeditiously forward to avoid cost increases and project delays.

Moreover, the supplement report dated July 18, 2006, showed that subcontracts for the project were competitively bid and the resuhs of that bidding for the subcontractor selection process to date. Staff noted that despite significant outreach efforts negotiating with bidders was necessary to increase particularly the SLBE representation in the project.

Although it is true that the project did not meet the LBE/SLBE goals set by the Agency Board in the July 18, 2006 resolution. But, as the resolution states, the effort was only to "attempt to attain the goal of fifty percent (50%) Local Business Enterprise (LBE) and twenty percent (20%) Small Local Business Enterprise (SLBE) participation". [Agency Resolution 2006-0052, p. 4.]. The report also discussed the difficulty the project would have meeting this goal:

> The pre-bid goal for this project is to attain 50% LBE and 20% SLBE for contracts for the project. A summary of the bids shows that out of the 113 bids received, 39% were from LBE firms and 27% from SLBE firms.

> Acceptance of only the low bidders will result in 43% LBE and 12% SLBE participation. This exceeds the City of Oakland's S/LBE requirements by over 100%, but is lower than the 50% goal. [Report July 18, 2006 page 7].

When all of the project phases were bid, the LBE participation fell, but the SLBE participation increased. It is the SLBE participation that is hardest to increase in large projects. The larger the project, the more you need to break the project up in order for the elements to be small enough for small contractors to bid.[1] The audit compared the participation in the Fox Project with the participation in citywide projects in FY2007-09. This is an invalid comparison, because it does not take into account the fact that many small projects are 100% SLBE and other projects are 100% S/LBE.

A more valid comparison than the one referenced in the audit report, would be to compare the Fox Theater Project to the eight large affordable housing projects completed in FY 2007-09 (14th Street Apartments, Coliseum Gardens Phase III, Mandela Townhomes, The Orchards on Foothill, Jack London Gateway Senior Housing, Tassafaronga Village, St. Andrews Manor and 10800 Edes Avenue Homes Phase B). These represent 41.10% of the projects in this period; and the results is very different. These projects are also building projects with multiple disciplines, similar to the Fox Project. The total S/LBE participation projected by early bids was 43%, the Fox actual S/LBE participation was 37.47%, the FY 2007-09 Citywide S/LBE participation was 35.92% and the FY 2007-09 Citywide Large Project S/LBE participation was 28.84%. Thus the Fox bettered participation in similar size projects.

	SLBE	LBE	Total
Fox Predevelopment (Lowest Bids)	12.00%	31.00%	43.00%
Fox Actual	19.41%	18.06%	37.47%
Citywide 2007-2009	20.11%	15.80%	35.92%
Large Projects Citywide 2007-2009	15.53%	13.31%	28.84%

From this analysis, it is still correct to conclude that the higher goals were not met, but the Council was apprised that the goals might not be achievable when the Council was asked to approve the project and the bidding method. What is more important is that the project was able to achieve substantially higher S/LBE participation than other large building projects by waving the competitive bidding requirement, 37.47% versus 28.84%.

We also note that the Agency transferred the Fox property to FOT as a non-profit corporation and its for-profit subsidiaries as entities separate from the Agency and City to be developed under a 60 year lease and a disposition and development agreement. FOT and its subsidiaries are not public entities and not subject to statutory restrictions on contractor hiring procedures unless required in the DDA or funding agreements. . However, However, where the Agency is acting as a lender or dealing with a less experienced developer, the

[1] Along this line, federal regulations suggest breaking up larger projects into smaller components to encourage participation by smaller and minority businesses.

Agency may include DDA terms that would permit Agency approval of construction contracts, contractor, and tenants in a commercial project—just as a commercial lender. to better assure the Agency that project will be successful and in the event the Agency has to take back an uncompleted project, the Agency would have a construction contract and contractor it can live with. Because the Fox project included substantial Agency fimds and the Agency had reversion rights in the project, Agency staff wanted to include the Council in more of the decisions than would be typical in an Agency assisted development and sought Council approval for modified contracting procedures.

F. The project met federal regulations. The City received a grant of $600,000 as part of an earmark for a small portion of the Fox construction costs as part of an earmark. The grant agreement was executed on March 13, 2008; by then construction had been underway for some time and subcontractors selected. The grant agreement specified that it applied to two specific items of work: restorative painting and electrical work. The restorative painting was competitively bid and the electrical work was performed on a design-build basis. The applicable federal regulations permit awarding of contracts, such as design-build or construction manager contracts, on a non-low bid basis (price being one of the factors). 24 CFR § 85.36(3). Moreover, the federal procurement regulations allow for modification of award procedures when exigencies will not permit a delay. As discussed in section 2C above, one of the primary reasons for modifying the contract award process was to avoid costly or fatal project delays. Thus, federal bidding processes were complied with for the portions of the project the grant applied to. Further, to have the $600,000 grant control how the entire $91.5 nüllion project proceeded would be a case of the tip of the tail wagging the dog; more finds would arguably have been spent complying in all aspects of the project than the amount of the grant was worth. But, as stated above, the project complied.

There is no evidence that not using a fully competitive process increased costs; it may have reduced costs. The audit suggests that non-competitive procurement process may have resulted in higher costs. This is pure speculation and not borne out by any facts. The City and Agency permit waivers on their projects in part because fill competitive bidding is not necessarily the best way to achieve the lowest price or the best overall results. Bidding can increase project costs in several ways: preparing full bid packages and responding to inquiries increase the costs for design professionals, bidders may build in more profit and risk into bids; bidders may include additional amounts in the bid in order to cover the fact that they win some bids and lose others; a bid contest can delay projects by many months increasing carrying costs; and if a prime contractor delays or fails to complete a project, the costs can be catastrophic to a project. These problems are minimized when a construction manager is used and the subcontracts bid or negotiated. Construction managers take less profit because there is less risk. It is easier to readily replace a subcontractor who fails to complete than the entire contractor. Given the risks of litigation if the housing project failed to start on time or the delay that could risk losing millions of dollars in tax credits, the manner in which FOT and the Agency proceeded was the most prudent.

The construction management contract was awarded to Turner on a percentage industry standard basis. The contract was based on a standard American Institute of Architects construction manager at risk contract form. Turner did not use its crews to perform any actual construction work on the project, but supervised the work of the subcontractors through its percentage allowance. All the subcontracts were bid or utilized design-build. The Agency Supplemental Report dated July 18, 2006 set out the significant efforts undertaken by project managers to solicit bids and to obtain bids from LBE and SLBE firms. Part of those efforts provided LBE and SLBE with technical assistance to put them on a more competitive basis in bidding on the Fox project. The waiver was intended permit negotiation so that the costs could be lowered or LBE and SBLE firms could participate in the project. If the entire construction contract were competitively bid, not only would this have resulted in more time being lost, but because all the subcontracts were bid, would most likely not have resulted in any cost savings over fully competitively bidding all of the subcontracts.

3. RESPONSE TO CHAPTER 3 - Project Change Orders are Common Industry Practice and Contracting Procedures and Internal Controls were Appropriate Including Monitoring of Turner and CCG's Contracts and Payments

G. The Project organizational structure provided sufficient independence over project management decisions. The Audit concludes the arrangements with Turner and CCG present a conflict because their compensation increased when change orders were approved. This arrangement is no different than the typical construction contract and fee developer arrangements.

At a very early stage in the project Agency staff informed the Council that the general contract would not be bid. In a report to Council in 2005, Agency staff stated its intent to hire a construction manager and bid the subcontracts in lieu of bidding the entire contract. [Report June 28, 2005 p. 9.] In such an arrangement, a construction manager has no risk in the construction. In negotiating the construction management contract, FOT decided to move some of the construction risk onto the construction manager in the project by modifying this approach and moving from a straight construction manager contract to a construction manager-at-risk arrangement. The construction manager at risk contract form was a standard AIA form contract modified for the Fox project. The contract was negotiated using outside counsel expert in construction law matters

Further, the audit is mistaken when it concluded that CCG increased its income based on increased change orders. Although in the beginning FOT's contact with CCG was loosely based on two percent of the construction costs, less than standard for such agreements, subsequent amendment were not based on increased costs, but rather on the basis of actual work performed and CCG's costs over time. Although final CCG payments may have approximated two percent of the actual development costs--that is coincidental and not by design.

Of course the Fox construction had change orders. The rehabilitation of a structure that has been abandon for 35 years was a high-risk venture; the addition of historic renovation standards made it riskier and more likely that changes orders would be required. Moreover, bidding the construction contract would not have affected the number of change orders. Bidding by general contractors would not have changed the bid documents from those that the subcontractors originally bid on. The Fox projects treatment of change orders was no different than in other construction jobs. In any typical construction contract, change orders additive change orders include profit, risk and overhead. Additionally, the costs for architect and engineering services increase because these services are needed to assist in evaluating change orders and preparing documentation. Further, Fox project management worked throughout the project to reduce construction costs through negotiating change orders, rejecting many, value engineering, and deductive change orders.

But the audit does not find that any one of the change orders was not warranted by changed conditions, changes in plans and specifications, additional requirements from inspectors or the state and federal historical preservation inspectors, or the needs of the tenants. The only individual change orders the Audit criticized were three in which the Auditor calculated the labor costs exceeded prevailing wages (the Audit failing to note that prevailing wages are the minimum that must be paid as standard wages and that actual and union wages may exceed prevailing wages).

H. There was sufficient contract oversight and administration by Agency/FOT over CCG and Turner contracts. Change orders and payment requests in the construction phase had substantial review requh ements. Tumer prepared "Potential Change Orders", which often went through several revisions before they became final "Change Orders". The "Potential Change Orders" would be reviewed in weekly construction meetings, which included Turner, Architectural Dimensions, CCG (development staff and construction experts), and Redevelopment/FOT representatives (two architecture and renovation construction experts). After the Change orders were negotiated and everyone agreed to the scope and cost, the minor change orders could be executed without Redevelopment/FOT approval but the major change orders required everyone's approval - Tumer, Architectural Dimensions, CCG and Redevelopment/FOT. In addition, Bank of America had a construction manager at the construction site who made weekly reports from the field, worked closely with the constmction management team and who reviewed change orders. Bank of America also approved any budget amendments required by increased construction and soft costs with the monthly payment draws.

Payment requests followed the same procedures, preparation by Tumer, and review by Architectural Dhnensions, CCG and Redevelopment, except that two FOT officers/board members were also required to review the requests before the were sent to Bank of America Construction Lending for final review and release of fimds held in the project account. These procedures seemed more than adequate for Bank of America

I. The contracts were clear on how CCG and the sub-consultants were to be paid. But CCG was allowed to receive fimds to cover the costs and provide invoices, cancelled checks, bank statements and general ledger accounts after the payments. The audit in fact reviewed all of the payments, relying mostiy on spreadsheets supplied by FOT and CCG, and only found $178,726 in unsupported expenditures. These were later found to be missing invoices from January 2007 that were later supplied to them, see K. below. The Agency and FOT's contract with CCG and CCG's contracts with its design sub-consultants was based on a monthly fee to CCG, which was adjusted in each phase based on the tasks required in the period, and reimbursement without markup for any of the sub-consultants. The typical compensation term in each contract or amendment with CCG read as follows: "Compensation and Method of Payment: Contractor will be paid for performance of the scope of services an amount based upon actual costs but that will be "Capped" so as not to exceed $amount based upon the Scope of Service in Schedule A ..." The Scope of Service includes three exhibits: 1) Task List; 2) Schedule; and 3) Budget, with tasks and sub-consuhants listed. Use of the phrase "based upon actual costs but shall not exceed" does imply that costs/compensation could vary, depending upon what the actual costs were, so long as there was a ceiling to the costs. The type of services and the costs for them would change during the contract and amendments and CCG was allowed to amend the sub-consultant budgets with FOT approval but changes to CCG's developer fee required a formal amendment of the contract. Understandably, this may have provided grounds for confusion, as CCG always requested payment for the maximum amount permitted under each contract. However, this was permitted per the stated compensation term in each contract.

J. The Agency and FOT effectively monitored contract expenditure levels. Staff prepared extensive spreadsheets of revenue and expenditures, with detailed sources and uses of funds that were tracked by the consultant based on monthly draws. Most of the discrepancies found in the audit were made from review of these documents. Staff was aware of several contracts, mostly architectural and engineering, going over their budget. For the construction phase it is typical to contract on a time and materials basis since it is difficult to determine the scope for unknown conditions. Most of the work in the constmction phase is responding to requests for information from the contractors or design modifications for unanticipated condition. The design contracts with the four firms - Architectural Dimensions and Associates ("AD"), KPA Group ("KPA"), ELS and Starkweather Bondy Architecture LLP ("SBA") – should have all become time and materials contracts in the final phase. CCG did prepare one contract, with ELS, that was open ended as related to time and materials and therefore the audit finding that this contract was over the not to exceed amount by $219,375 is inaccurate. The other contracts were not amended, but FOT and Agency staff was aware of the rising costs and even negotiated to reduce the fees due. In particular, the AD contract which was almost half of the increase, was negotiated as a direct payment from FTLL hi installments - as part of construction contract close out and the final equity payment. The payments were part of a settiement agreement approved by Fox Theater Manager's board and executed March 4, 2010. The agreement reduced the amount due by $68,175 and eliminated over $42,714 in requested interest for delays in payment. Finally, it should be noted that FOT never approved contract amendments with CCG, or its sub-consultants, until the funds were approved and available, which for the final project costs was after the $2.0 million loan from the Agency was approved on January 5, 2010.

K. The $178,726 in expenditures to CCG are fully supported. The audit stated that: "Unsupported costs of $178,726 were paid to CCG," and made the following recommendation: "We recommend that Agency management request supporting documentation from CCG for all unsupported costs and if documentation is not provided, these costs should be returned to Agency and FOT." The audit was correct in showing that there was $178,726 in unsupported costs between the December 18, 2006 spreadsheet of expenditures for Amendment 2, 3 and a portion of 4 (Fox Accounting Amendments 2-3-4 Dec-18-06.xls) and the January 19, 2010 spreadsheets of constmction draws, which start with Amendment 4 (Fox Budget FINAL Jan-19-11.xls and FOX EXPENDITURES Jan-31-11.xls). But there were additional documents that had not been recorded in these spreadsheets. Review of the records during the audit found the missing costs were for a one-month period between the predevelopment and constmction phases in January 2007. CCG presented documentation for $184,661.80 in expenditures for this period. This amount includes expenditures from interest that CCG earned on the Fox Project funds on deposit in a project account, which is why they were able to document payments that were greater than the amount of unsupported costs in the audit.

L. CCG was reimbursed for work outside of the contract. There are two issue related to the developer fee payments: 1) payments to CCG for periods not covered in the contract and amendments, but still justifiable; and 2) over-payments to CCG that might not be justifiable and should be recovered.

There is a period between completion of 90% constmction documents, Amendment 2 of the CCG contract which ended March 31, 2006, and closing on the financing/start of constmction, Amendment 3 of the CCG contract which began August 21, 2006. This was the period in which FOT and the various development entities were created and CCG contract was being transferred to this new entities. This was one of the busiest times for the development during which the construction work was being bid, the tax credit investor was being selected, the deal was being stmctured and the project was being approved by the Council. On August 8, 2006 at its first meeting the FOT board approved a $1,050,000 contract with CCG. But because of a limit in funds, Amendment 3 of the CCG contract was for only $900,000. Instead of covering the period from April 1 to November 30, 2006, Amendment 3 only covered October and November 2006. When the project received full funding and Amendment 4 was executed in December 2006, the 6-month period from April through September was not included but the fees for this period were paid out of the first Amendment 4 payment. The fees paid for this six month period was $142,500 ($23,750 per month the same as October and November in Amendment 3). Since CCG performed many services during this period and these fees seem reasonable, FOT should use the prior board approval to execute an additional amendment to CCG's contract to cover the missing period and increase the fee $142,500.

There seem to be two over payments as well - $27,143 and $9,200. During staff s review of documents during the audit it was determined that here were two payments for December 2006, one for $31,381 the monthly rate for Amendment 4, and one for $27,143. Amendment 4 was signed November 27, 2006, it should have covered December. It seems that $9,200 was paid to CCG over the course of Amendments 4 and 5. It is hard to determine why these payments were over by this amount since there were numerous monthly payments, but it seems to be an over payment. If the fees are increased by $142,500 and the $27,143 and $9,200 over payments are recovered or justified by CCG, the developer fees payments would be correct. Staff is in discussion with CCG about these over payments and has requested a repayment of $36,343.

M. FOT is not entitled to refunds for Turner's Guaranteed Maximum Price (GMP) contract. The Audit argues that Turner was under a GMP contract, where the price is fixed and saving automatically go to the contractor, and yet FOT is due any saving from costs being less than budgeted. The Turner contract provided a maximum price for the work (including Turner's fee) pursuant to the listed plans and specifications, but subject to additive and deductive change orders. If a particular item actually cost less than the original pricing, Turner would be the beneficiary; if it cost more, FOT would be the beneficiary. Only in the case of items with allowances, where the price is only estimated until the scope is worked out, is FOT due any savings from the final cost being reduced and these were generally negotiated as constmction proceeded and incorporated within the change order process.

N. The project followed proper Change Order pricing procedures. The Fox project's treatment of change orders was no different than in other constmction jobs. In any typical constmction contract, change orders additive change orders include profit, risk and overhead. Additionally, the costs for architect and engineering services increase because these services are needed to assist in evaluating change orders and preparing documentation. Further, Fox project management worked throughout the project to reduce constmction costs through negotiating change orders, rejecting many, value engineering, and deductive change orders.

The audit does not acknowledge that change orders are common in constmction projects. While the number of change orders and combined increase were large, 34% or $16,124,637 over the initial contracts of $47,793,563, this is typical of historic renovations. This is particularly tme for a building that was vacant for 35 years and when federal and state historic standards are required for the construction. Many of the change orders were the result of meeting historic renovation standards or were requested by the tenants. Staff constantly negotiated change order requests to lower prices or refused them outright. Included in the final 28 change orders processed at the end of the project were nine ($533,682) that were rejected, 13 ($781,460) that were reduced an average of 35% and only six ($100,543) that were accepted as proposed. From initial proposed change orders to final approved change orders these 28 items were reduced from $1.4 million to $610,358 or 57%.

The Audit criticized change order labor pricing for three change orders for exceeding prevailing wage rates and states that labor rates should be priced at prevailing wage. However, prevailing wages are the minimum that must be paid as standard wages on a project where they are required by law and that actual or union wages and benefits may exceed prevailing wages.

O. The Project met the City's Administrative Instructions for conflict of interest as well as California State requirements on conflicts. At the outset we note that the Audit did not find any conflicts of interest in the Fox Project. Nonetheless, the Audit failed to discuss the conflict of interest provisions that were in place in the project, some of which exceeded standard City/Agency requirements. As with all City/Agency professional service contracts, there is standard language regarding conflict of interest, including prohibitions on donations to City elected officials. But FOT went firther with the CCG contract by amending to the contract to include non-standard language regarding Government Code 1090. Further, in discussing staff conflicts the Audit failed to note that all City/Agency must annually file Political Reform Act public disclosures of theh financial interests (Form 700) and comply with the City's two Administrative Instructions ("AI") on conflict of interest – AI 21 and AI 595 Employee Conflicts of Interest / Incompatible Employment. During tiie course of this project, the City Attorney's Office acted as lead counsel for FOT and was in a position to analyze any potential conflicts of interest. Together, these steps represent more conflict safeguards than are typically present on City or Agency or private Agency fimded development projects.

4. RESPONSE TO CHAPTER 4 - The Project Was Successful at Raising Outside Funds And the Feasibility Analysis Provided was Comprehensive

P. The project prepared comprehensive financial feasibility analysis including: 1. Project scope/description; 2. Statement of sources and uses; 3. Project budget and financial projections; 4. Financial statements; and 5. Real estate appraisal or valuation.

The audit found that "the financial feasibility analysis was inadequate for the scope of the project". In particular that: "there were shortcomings associated with the following five major elements: 1. Project scope/description; 2. Statement of sources and uses; 3. Project budget and financial projections; 4. Financial statements; and 5. Real estate appraisal or valuation." But this is inaccurate. The project scope was detailed as far back as 2001 in the Fox Theater Master Plan. A project budget or sources and uses was provided to the Council on several occasions and a much more detailed spreadsheet was prepared and updated monthly as part of the construction draws starting in early 2007. A detailed analysis or projections used to meet the requirements of Bank of America and the CDEs were prepared several times in 2006 and again in 2009, although these long (37 page) and detailed projections were never shown to Council, they were available. Financial statements are prepared for all of the four entities but audit financials are not available for FOT because they are not needed and expensive--approximately $12,000 per year. These documents would only be useful if the Agency was planning to use FOT on another project. FOT is a single purpose entity and another entity would be created for any future project.

It is hard to determine from the audit what level of information was expected for these items, but much of the information was in fact presented. The question that should be asked is whether any additional information would have improved the Council's ability to make decisions; too much information might have the effect of burying the key information. Moreover, when the Council believes it needs additional information, it does not hesitate to request it. The project is described in the reports to Council, which included reduced graphics. In the section regarding the project scope/description the audit stated that "the "Ruins Concept" at $27.0 million (excluding land and predevelopment cost) ... was similar to the "Basic Concept" at $70.0 million described in an eariier 2001 Fox Master Plan. This is not tme. In the 2001 Fox Master Plan, the "Basic Concept" was estimated at $43.7 million and the "Arts Center" concept was estimated at $69.0 million and the "Roadhouse" concept was estimated at $66.9 million. The final project combined elements of the "Arts Center" concept and the "Roadhouse" concept. The total cost of the project was amazingly close to the Hardy Holzman Pfeiffer report prepared in 2001. As stated earlier in this response, if the "Roadhouse" project concept was adjusted for inflation (see response to Chapter1) the total cost of the project would have been $83.4 million. This is close to the final cost of the theater if the already expended purchase price and improvements are eliminated - $85.0 million.

In the section regarding the statement of sources and uses the audit stated that "sources and uses statements (dated 12/14/04, 06/28/05, 06/27/06, and 07/18/06) omitted or failed to accurately reference land and predevelopment costs." While the sources and uses did exclude these costs, the sources and uses were only illustrating the cost to complete the project and more ìnportantiy the Fox Theater Master Plan also only considered the costs to complete the projects. The reports also discussed the Agency's expenditures to date in other sections. More importantly, the audit did not consistentiy incorporate the same historic costs in the Funding Sources and Project Costs comparisons, which both understated the initial costs and inflated the growth in costs.

In the section regarding the project budget and financial projections the audit stated that "The Fox Theater Project's original plan did not project the effect of rising development costs on cash flow. Unabated, deviations in these elements may result in substantially unfavorable effects in other elements of the feasibility analysis. Specifically, when a commercial development is undertaken, the financial analysis should evaluate the operating assumptions for the project, the liketihood of reaching stabilization (rental income and other income in excess of operating costs and debt service and operating reserves) and the resultant net cash flow. The failure to realize these projected operating results will diminish the project's ability to sustain itself When there is an inability to produce a consistent net operating income (NOI), the project will be at risk of default on its financial obligations, and the sponsor/developer (Agency) must determine its capacity or desire to provide ongoing financial support to the project or repay any financial obligations of the project." While this is typical for a normal project, and would be tme of the Fox Project if the additional funds used to complete the project included conventional financing. But the one additional loan used to finance the project, a Local Initiatives Support Corporation/Bank of America New Markets Tax Credit enhanced loan where funds were set aside for all debt service payments from the loan principal. The project received $800,000 and $700,000 was set aside for all of the fees and hiterest payments. There was no additional risk assumed during the changes to the budget from 2006 to 2010. What is more, the tax credit stmcture included several "projections" which included income and expense analysis for the various entities. They were prepared in 2006 and again in 2009 for the Local Initiatives Support Corporation financing. These 38 page projections were very detailed and were required to confirm that the project would operate successfully.

In the section regarding the financial statements the audit stated "Development projects of this magnitude, with a non-profit sponsorship, should have audited financial statements. The Fox Theater Project has a layered organizational stmcture, which was required to facilitate attracting New Market Tax Credits and Historic Tax Credits financing. Each organization in the project has audited financial statements except FOT, Inc., which is the primary organization through which substantially all fimds pass through. While FOT, Inc. financial statements were unaudited, this did not adversely affect the project's ability to be awarded tax credit contributions. However, should Agency desire to monetize or attract additional capital, it is likely that capital providers will place limited reliance on unaudited financial statements." This seems contradictory, FOT should be audited but not being audited did not adversely affect the project's ability to be awarded tax credit contributions. FOT was a pass through entity. Funds came in and went out. The only fiinds needed by the entity were for accountant fees for the tax returns, bank fees and a few small expenses. All of the other funds fiow through to the entities which were audited, primarily Fox Theater Landlord LLC and Fox Theater Master Tenarit LLC. Staff felt that auditing FOT would be an unnecessary expense that the Agency would have ultimately paid.

In the section regarding the real estate appraisal or valuation the audit stated " While the "as-is" appraisal commissioned by Agency valued the pre-development cost, an "as-completed" appraisal would have provided a value for the entire Fox Theater Project and provided a basis to evaluate the project cost to project value. A review of the estimated value at stabilized operations would provide Agency with the ability to assess its potential return on investment and potential return of capital." The Agency did prepare a 33433 Report, including review of the project and DDA by an outside economic consultant (Keyser Marston Associates, Inc.) who prepared a fair reuse value or the Fox Theater, July 6, 2005. This type of report is required under redevelopment law to show that the project requires the proposed Agency financing/subsidy. Further, it should be noted that the value to the Agency or to the City, is not in the market value of the completed project, but rather in the value to the community in renovating an historic resources and in the catalytic economic effect of the renovated and operating Fox Theater to the surrounding community.

Q. The Agency, FOT and CCG were successfully in obtaining $32.0 million in capital and debt from Bank Of America to fund the Fox Theater Project. The project successfully attracted Bank of America to invest and continue to increase its investment in the Fox Theater as the national economy declined and the value of the tax credits was reduced. Bank of America provided all of the debt ($6.5 million) and equity ($26.0 million) for the project and the governance stmcture was set up to the bank's requirements. The initial equity offer from Bank of America was $15.0 million in June 2006, but by December 2010 this had grown 73%. CCG was instrumental in attracting Bank of America and negotiating the deal. Bank of America had worked with CCG on the Rotunda Building and based on this experience invested in the Fox Project.

R. The Agency, FOT and CCG were successfully in creating a complicated governance structure to generate Historic and New Markets Tax Credit equity. Syndicating the tax credits required the Agency to create a non-profit corporation (FOT), a for profit corporation (Fox Theater Manager) and two limited liability companies (Fox Theater Landlord LLC and Fox Theater Master Tenant LLC). This structure required a team of attorneys, accountants and four community development entities ("CDEs") with New Markets Tax Credit allocations - Bank of America, National Trust for Historic Preservation, Charter School Development Corporation and Local Initiatives Support Corporation. CCG, FOT and the Agency have been able to manage the development and operations of this very complicated project.

5. CONCLUSIONS - The Project Has Been Instrumental in Downtown's Economic Revitalization.

We concur with the audit findings that the project was successful at raising alternative funding, including private funds. An Agency owned theater would have save several million dollars at least, if only the legal, accounting and New Market Tax Credit fees. But the Agency would have needed to provide at least $20.0 million more in subsidies and still would have needed to seek $6.5 million in traditional debt for the project.

There is one final point to add, the Fox Theater was not developed as a stand alone project. The project was seen as both filling a major hole in the Uptown Area and as catalyst for other economic revitalization in the surrounding areas. The project took a rundown, decrepit blight and turned it into a major asset. The area now has two beautifully restored theaters that are the heart of an emerging entertainment district. The Theater attracted over 160,000 paying customers its first year, over 180,000 its second year and is projected to reach 200,000 in this, its third year. This is almost double the initial projection of 100,000 paying customers per year for the first three years. These visitors have enlivened the whole area and created a demand for new bars, restaurants, cafes, and entertainment venues, which continue to open—all of which contribute to Oakland's economy and tax base. The project has been a major artistic and economic success. In addition, the Fox Theater has received numerous awards celebrating its historic restoration and has hosted special events and tours, see Exhibit B List of Awards and Special Events.

Since the lighting of the historic marquee in 2001, investors and businesses have been flocking to the Uptown with over twenty new restaurants and nighttime entertainment venues have opened in close proximity to the Fox. On any given night restaurants like Flora, Pecan, Ozumo, Plum, Hibiscus and the recently open Rudy's Can't Fail Café as well as bars and clubs like the Uptown, Somar, Era Art Bar and the Dogwood are crowded with patrons from the Fox and its nearby twin sister, the Paramount. On any given evening these two theaters attract as many as 6000 patrons to the Uptown area, providing a huge customer base for the nearby bars and restaurants and giving the street a sense of vitality and safety that has been missing for over forty years.

But the Fox Theater is much more than just a theater, it is also houses the Oakland School for the Arts a performing arts middle/high school. The Fox provides OSA with a new first class facility for almost 600 full- time students from all over the Eastbay. Many of these students are from disadvantaged families. With a college placement rate of over 95%, the Fox project is providing them with an opportunity to advance their education, attend college and become productive artists and members of the community. During the day, they populate the street and surrounding neighborhood with a message of education and learning.

From a purely economic standpoint, all of this has meant new sales tax revenue to the city, an increase in business license taxes, an increased property tax base and additional tax increment for future projects in the neighborhood. In addition, new jobs have been generated by the new restaurants and bars and over 150 people now find employment at the Fox Theater. But just as important as the jobs and increased revenues, the Fox has brought people back to a once unstable and unsafe neighborhood. It has changed this once blighted backwater of Oakland into the most important entertainment area in the Bay Area. It has brought new life to Oakland and provided hope for the students of the OSA.

EXHIBIT A

Chronology of Fox Theater Council Actions

7/18/2000	1. Authorization for a professional services contract with Hardy, Holzman Pfeiffer Associates for the Fox Theater Master Plan
4/24/2001	2. Reports and discussions of the Fox Theater Master Plan
10/14/2003 12/2/2003	3. Authorization for an Exclusive Negotiating Agreement with Fox Theater I Corporation (proposed entity combining Oakland School for the Arts and Paramount Theater) and a $432,500 professional services contract with CCG as fee developer
9/21/2004	4. Authorization to apply for, accept, and appropriate Proposition 40 grant funds ($5.0 million) for the historic renovation of the Fox Theater
12/21/2004	5. Report on the schematic design phase an authorization for a $746,000 amendment to the professional services agreement with CCG
6/28/2005 7/19/2005	6. Authorization for a DDA with Oakland Renaissance New Markets Tax Credits, Inc. including $22.5 million from the Agency
6/27/2006 7/18/2006	7. Authorization for a DDA with Fox Oakland Theater, Inc. ("FOT") including $32.0 million loan and $5.4 million in grants and other sources from the Agency
10/31/2006	8. Authorization for guarantees by Agency in favor of the lender and tax credit investment entities
12/15/2006	Closed on financing and started construction
2/13/2007	9. Authorization to apply for, accept, and appropriate Proposition 40 grant funds ($3.0 million) for the historic renovation of the Fox Theater
7/10/2007	10. Report on the City's local contracting and hiring goals for the Fox Theater
7/15/2008	11. Authorization for an amendment to the DDA with FOT including $7.5 million bridge loan and $7.0 million in grants and loans from the Agency
12/19/2008	Temporary Certificate of Occupancy on theater and school
5/12/2009	12. Authorization for an amendment to one of the 7/15/2008 loans to authorize $1.3 million of the $2.7 million tenant improvement loan to be with Friends of Oakland Fox ("FOOF")

6/21/2009	Closed on additional New Markets Tax Credit enhanced loan through Local Initiatives Support Corporation
12/1/2009 12/15/2009 1/5/2010	13. Authorization for a $2.0 loan to FOT to complete the renovation of the Fox Theater
2/2/2010	14. Authorization to apply for, accept, and appropriate Proposition 40 grant funds ($1.0 million) for the historic renovation of the Fox Theater
10/??/2010	Signed Lease with Rudy's Can't Fail Cafe
6/1/2011	Rudy Can't Fail Cafe

EXHIBIT B
List of Awards and Special Events

The Fox Theater has won a number of awards; hosted other special events; been the subject and site of tours and talks for over 125 groups including local non-profit groups, docents from the Pardee Home, seniors, city planners, and community; and hosted "free" community events for which the local non-profit organizations including OSA are not charged rent.

Awards

2009 Resolution California State Legislature, recognizing the "Grand Opening of the Fox Oakland Theater...it's unique status as one of the oldest and most important historic buildings in California...helping generate both approval and funding for the current restoration project."

2009 National Preservation Award of the National Trust for Historic Preservation

2009 Certificate of Recognition California State Legislature, In Honor of Dedication to the Sustainable Future of Your Community"

2009 Certificate of Recognition California State Legislature, "**2009** Green Heroes, In Honor of Collaboration on Green Jobs and a Green Economy for Oakland"

2009 Certificate of Recognition City of Oakland, "**2009** Green Heroes Award Winner, for dedication and commitment to making Oakland a model city"

2009 Secretary of Interior Conservation Award

2009 Platinum Award, Building Design and Construction, Reconstruction Award

2009 Award of Merit, Excellence in Structural Engineering, Structural Engineers Association of California

2010 California Redevelopment Association Award of Excellence, Mixed-Use Development

2010 Excellence in Engineering, National Council of Structural Engineers Associations

SPECIAL EVENTS

The City of Oakland has "free" access to the theater on 5 occasions per year. For these events the City pays no rent, but it has to pay for any set up, security, stage hands or other operating expenses directly related to the event. The event must meet four criteria:

1. Organization: The event must be sponsored by an eligible organization, which may include school districts, community organizations or non-profit organizations which are located in the City of Oakland and serving Alameda County and the Bay Area.
2. Purpose: The event must be of community, educational and cultural interests to the people of Oakland.

3. Accessibility: The event must be free to the general public or raise funds for causes that serve the community, educational and cultural interests of the people of Oakland.
4. Use of Space: The event must attract sufficient interest from the community to maximize the use of the auditorium.

In addition to the 2011 Mayor's Inauguration, City sponsored events at the Fox have included the following organizations: International Council Of Shopping Center/Urban Land Institute; Children Hospital Oaldand; Oakland Chamber of Commerce; and Friends of Oakland Fox, which sponsored the grand opening gala. The Fox Theater was also highlighted in June 2009 at Uptown Unveiled! - A City of Oakland Cultural Arts & Marketing special event that attracted over 9,000 people to tour the theater one evening.

Oaldand School for the Arts also has "free" access to the theater on 5 occasions per year. The school uses this access for graduation with artistic presentations, major school productions and fund raising events.

TOURS and FOX TALKS

Tours and Talks for over 125 groups have been made presenting the Fox to local non-profit groups, docents from the Pardee Home, seniors, city planners, and community. Some of these presentations include:

October 2009 National Trust for Historic Preservation; the Old U.S. Mint San Francisco, Participating Presenter with Architectural Dimensions

April 2009 City of Oakland Rotary Brown Bag Lunch Presentation

July 2009 Walking Tours Oakland Heritage Alliance

November 2009 Presentation, San Francisco City Hall Fellows Program

November 2009 Young Preservationists, Tour and Talk

February 2010 American Planning Association of Northern California (Fox Talks with Architect Jim Heilbronner and Jeffrey Chew)

Oakland Tours Program with Amalee Allen

April 2010 History Channel Segment

May 2010 Tours for Oakland Unified School District Children learning about Oakland Historic Places.

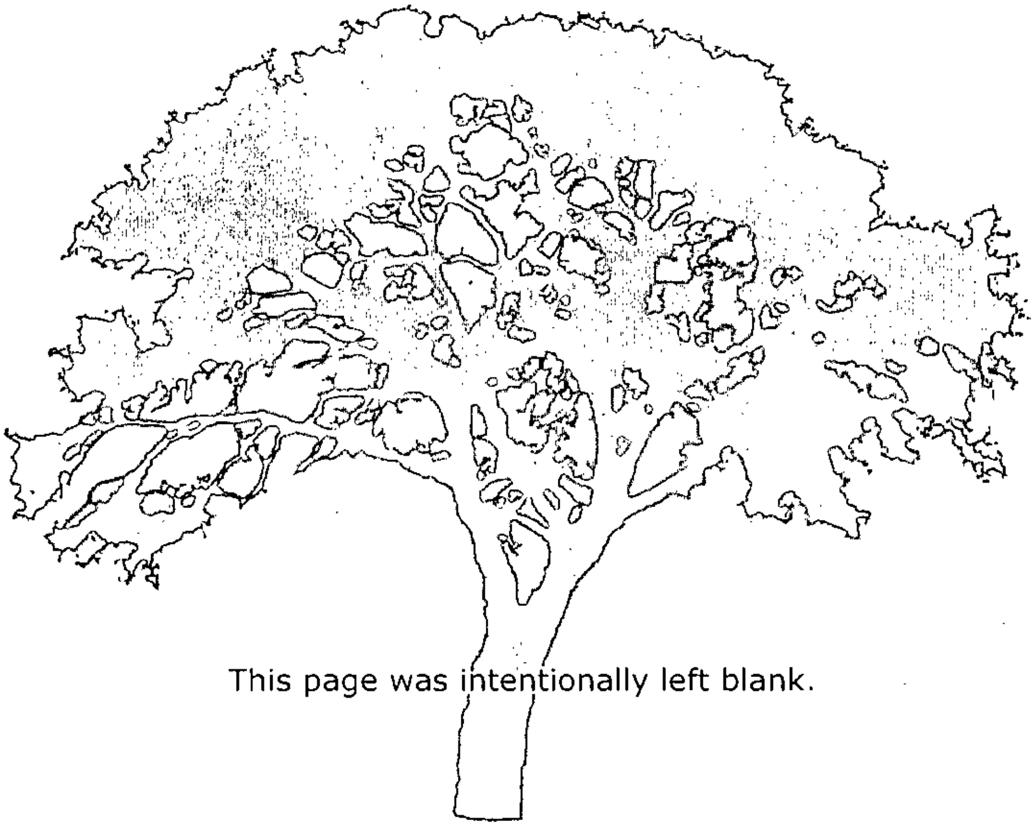
October 2009 Uptown Masquerade Bash Benefit

December 2009 Volunteer support Oakland School for the Arts, 3 day Visual Arts Show

January 2010 Norton Buffalo Benefit Concert Sponsor

February 2010 Open House Tours for 1 Year re-opening Anniversary

RESPONSE TO ADMINISTRATION RESPONSE



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RESPONSE TO ADMINISTRATION RESPONSE

(Point by Point Administration Response, Attachment A, Page 51, Dated 8/12/2011)*

Comment	Page	Ref	Administration Response	TCBA Response
CHAPTER 1				
1	1	1.A	The Fox Theater Project Scope and Costs. The Fox Theater was always envisioned as a Full Renovation Project and costs were in line with Council information and approvals.	The audit does not dispute that the project grew from the ruins concept to the full theater restoration. The report acknowledged that the project scope grew from the "Basic Renovation" to the "Full Broadway Show" and stated that the project scope and costs grew as additional funding was identified. The purpose of Exhibit 2 is to summarize the funding sources identified through the life of the project as presented to City Council, and the final funded amounts as provided to us by Agency staff. The Agency's response provides new information in regards to the Agency Resolution dated December 2, 2003 that indicates the intention was for a full renovation of the Fox. However, this information does not change the report's findings or recommendations.
2	1	1.A.1	Final projects costs were in line with those presented to the Council.	See Comment 1.
3	2	1.A.2	Comparison of two different projects.	See Comment 1.
4	2	1.A.3	Tenant driven changes	As described on page 8, the report acknowledged that the project included scope revisions required by the tenant.
5	2	1.A.4	Comparison from the "Ruins" Concept	See Comment 1. The report compares the project costs at 2004 and the final costs of the project, with discussion of the project scope changes. The fact is that the cost of the project began with a $33 million budget (as presented to the Board) and the final project costs totaled $91 million. However, the report was edited to reflect the new project costs by using the actual costs of the Land/Improvements rather than the appraised value. Exhibit 1 was revised as well as areas in the body of the report to reflect the revised project costs from $95 million to $91 million, based on the information provided.

* Indicates report areas that were changed due to new information provided by the Agency subsequent to the Administration's August 12th Administration Response.

Comment	Page	Ref	Administration Response	TCBA Response
6	3	1.A.5	Land cost at appraised value	Exhibit 3 was changed to reflect the costs of Land/Improvements at $6.5 million. However, the added footnote states that the Final Expenditure Budget listed Land/Improvement Costs at the appraised value of $9.7 million for tax credit purposes.
7	3	1.A.6	Land costs at appraised value	See Comment 6.
8	3	1.A.7	Staff Report dated July 18, 2006	Exhibit 2 has been changed to include the July 18, 2006 Supplemental Staff Report.
9	3	1.A.8	Prop 40 and other funding sources	The Prop 40 Grant amount in Exhibit 2 was corrected and the $1M from the Agency Bridge Loan was removed as it is already included in the other funding sources. The potential funding sources as of July 18, 2006 were added to Exhibit 2. This Exhibit represents potential funding sources at various points during the project timeline. The final project costs were revised to exclude reserve amounts and other non-expenses.
10	3	1.A.9	Historic Tax Credits	The audit does not dispute that the project required additional improvements in order to comply with the historic preservation requirements to receive historic tax credits. The audit report describes the growth in scope in costs throughout the life of the project.
11	4	1.B	The City did not pay for any project costs.	The Finding Heading was changed from City to Agency. While the Agency states that the percentage of the project to be funded by the Agency fell from 59% to 53% from 2004 to 2009. The audit's calculation shows that the amount funded by the Agency fell from 59% to 57%. The actual Agency funding increased from $13 million to $52 million, which is a 300% increase from the initial estimated Agency funding contribution.
12	4	1.C	The project was unable to secure approximately $5.6 million in grant funds, $9.4 million less than stated in the Audit.	The unsecured funding amount was corrected from $15.1M to $7.6M based on the additional information and documentation provided.

Comment	Page	Ref	Administration Response	TCBA Response
				will establish that ORNMTC[1] has authority to contract for the Agency. It is further recommended that the Agency establish clear authorization for ORNMTC to waive competitive bidding. This will forestall any future disputes concerning non-standard bidding or negotiation that could delay the Project. It is clear from this paragraph that the concern for delay was not due to the use of competitive bid procedures, but rather from the use of non-standard bidding procedures without a waiver of City competitive bidding requirements.
15	10	2.F	The project met federal regulations.	The Agency's response provides no basis or other factual information for altering the report's recommendation. The Agency states that the City received a grant of $600,000 and specified that it applied the funds to restorative painting and electrical work, and that restorative painting was competitively bid and electrical work was performed on a design-build basis that is allowed under federal contracting procedures. Information reviewed by the audit team showed that while more than one subcontractor was considered for some of the contract's work categories, the selection of subcontractors to perform the work of those work categories was not based on a sealed, low-bid process. In regard to federal design-build contracting procedures, the use of those procedures still require competition.
CHAPTER 3				
16	11	3.G	The Project organization structure provided sufficient independence over project management decisions.	The Agency's response provides no basis or other factual information for altering the report's recommendation. The Agency states that the audit concludes that the arrangements with Turner and CCG present a conflict of interest because their compensation increased when change orders were approved, and that this arrangement is no different than typical construction contract and fee developer arrangements. The Agency misstates the audit's concern. The audit disclosed that both CCG and Turner made or had primary influence over contractual or project decisions from which they received financial benefit. Such an arrangement is not typical for a well-managed construction project and should be avoided as it presents a potential conflict of interest.

[1] ORNMTC – Oakland Renaissance NMTC, inc. (non-profit entity)

Comment	Page	Ref	Administration Response	TCBA Response
17	12	3.H	There was sufficient contract oversight and administration by Agency/FOT over CCG and Turner contracts.	The Agency states that change orders and payment requests had substantial review requirements. As discussed in the report, adequate contract oversight and administration includes and is not limited to clear payment provisions and contract monitoring procedures. The audit report provides clear evidence of how contract oversight and administration were inadequate (i.e., the Agency authorized payments in excess of contract ceilings, payments were made for unsupported costs, and overpayments were made for developer/ management fees). As for change orders, the audit report provides clear evidence of inadequate change order review (i.e., no independent cost estimates, no cost detail to conduct cost analysis, and no records of negotiation).
18	12	3.1	The contracts were clear on how CCG and the sub-consultants were to be paid.	The Agency's response provides no basis or other factual information for altering the report's recommendation. The Agency stated that staff was aware of several contracts, mostly engineering and architectural contracts, going over their budget. The audit's review disclosed that payments to CCG and to several subcontractors had exceeded contract ceilings. These observations were based on a comparison of original and amended contract values and our summary of payments made by the Agency for these contracts. During the course of the audit and at the initial exit meeting, no one at the Agency was able to address whether or not the audit's comparison was accurate or inaccurate apparently because the Agency did not maintain such a record. The Agency implies that because Architectural and Engineering contracts carried over from the design phase to the construction phase, the work performed after construction should have been on a Time and Material basis; and as such, the contract would be open ended and have no contract ceiling. However, the Agency acknowledges that only one of the four Architectural and Engineering contracts included an amendment for work on a Time and Material basis. The audit noted that the use of Time and Material compensation provisions do not eliminate contract ceilings already established under the contract nor do they eliminate the need to establish contract ceilings. Instead, the use of Time and Material compensation provisions increase the need to control expenditures through the establishment of contract ceilings in order to limit the contractor's authorization to funds that may be available for the contract. The Agency stated that the audit finding that payments to ELS exceeded the authorized contract amount by $219,375 was inaccurate because the last amendment to this contract provided for payment on a Time and Material basis.

Comment	Page	Ref	Administration Response	TCBA Response
				The audit also noted that the Agency failed to adjust the contract ceiling when the final amendment to the ELS contract was issued, and the audit found this oversight not as an elimination of the contract ceilings established by prior amendments and the original contract, but as a failure of the Agency to exercise proper control over contract expenditures for the scope of work authorized by that amendment. The audit also noted that this contract was over the contract ceiling at the time the Time and Material amendment was executed.
19	12	3.J	The contracts were clear on how CCG and the sub-consultants were to be paid.	The Agency's response provides no basis or other factual information for altering the audit's recommendation. The Agency states that the compensation provisions of CCG and subcontractor contracts were clear and then cites as the typical subcontractor language the very language that is cited in the report, which are subject to many and varied interpretations. It then proceeds to interpret those provisions by referring to the Scope of Services, Schedules, Budgets and Task List. At the end of their explanation the Agency states the terms may provide grounds for confusion, and the audit agrees.
20	14	3.K	The $178,726 in expenditures to CCG is fully supported.	The Agency has responded positively to the report's recommendation by obtaining documentation to support the unsupported costs. At the time of the audit, the unsupported costs totaled $178,726. The audit's review of the additional documentation provided still indicates that costs are unsupported. Thus, the report's finding and recommendation remains unchanged. The Agency should continue to obtain the supporting documentation and review those documents to determine whether costs should be returned to the Agency.
21	14	3.L	CCG was reimbursed for work outside of the contract.	The Agency's response indicates agreement with the report's finding that CCG was overpaid fees as authorized under the contract in the amount of $178,483. However, the Agency believes that additional payments should have been authorized under the contract and plans to seek recovery of only $36,343. The Agency indicated that it will seek Board approval to amend CCG's contract to authorize additional fees for the balance of $142,500 in overpaid fees. The Agency believes that CCG earned those fees for services provided during the six month period extending from April 2006 through September 2006. The report recommends that the Agency consider whether CCG's fee is an earned monthly fee or a lump sum fee to be paid for the project as a whole before it makes a request to the Board for additional fees under the CCG contract. The audit team was told by Agency and CCG representatives during the audit that CCG charged a Developer fee for this project at about 2% of the construction contract

Comment	Page	Ref	Administration Response	TCBA Response
				value. The audit notes, however, that the Developer Fee authorized by the contract is currently at 2.8% of the final construction contract value.
22	15	3.M	FOT is not entitled to refunds for Turner's Guaranteed Maximum Price (GMP).	The Agency's response provides no basis or other factual information for altering the report's recommendation. The Agency states that the contract with Turner provided a maximum price and that no savings was due to FOT should actual costs incurred under the contract be less than the Guaranteed Maximum Price (GMP). The audit disagrees. The contract with Turner does allow for sharing of any savings under the GMP. Article 12.2.3.1 "Shared Savings" requires that final cost less than the GMP be shared with 70% going to FOT and 30% to Turner.
23	15	3.N	The project followed proper Change Order pricing procedures.	The Agency's response provides no basis or other factual information for altering the report's recommendation. The Agency did not question the report's findings that ▪ Independent estimates of change order costs were not prepared. ▪ Records of negotiation were not prepared to show how the reasonableness of change order proposed prices were determined. ▪ No written procedures on steps to be followed to establish fair and reasonable change order prices existed. ▪ No specific instruction existed on the format and details that contractors/subcontractors should use in proposing change order prices, and ▪ No guidance had been provided to contractors/subcontractors on allowable cost and mark-up. The Agency questioned the report's recommendation to use prevailing labor wages as a standard for assessing the reasonableness of proposed change order costs claiming that prevailing wages are the minimum that must be paid under the contract, and that actual wages paid by contractors may exceed that minimum. The audit notes that the report's recommendation was to use prevailing wages for pricing change orders unless higher wages can otherwise be justified. Also, according to Article 7 of the Turner contract, any rates paid under the contract should be paid at rates no higher than the standard paid in the area.

Comment	Page	Ref	Administration Response	TCBA Response
24	16	2.0	The Project met the City's Administrative Instructions for conflict of interest as well as California State requirements on conflicts.	The Agency's response provides no basis or other factual information for altering the report's recommendation. The Agency discussed the state requirement for public employees to disclose their financial interest and with City instructions for completing such forms under AI 21 and AI595 and that our report had failed to recognize its compliance. Our report did not question the Agency's compliance with those requirements, but rather found the need for additional conflict of interest safeguards.
CHAPTER 4				
25	16	4.P	The project prepared comprehensive financial feasibility analysis.	The Agency's response provides no basis or other factual information for altering our finding and recommendation. <u>Project Scope/Description</u> The Agency states that a detailed analysis or projections were prepared to meet the requirements of Bank of America and the Community Development Entities. However, the audit's position is that detailed projections while satisfactory to obtain Bank of America financing (supported by guarantees), may be scaled down allowing approving authorities to constantly ascertain levels beyond which they may want to use scarce public funds to support on-going costs. The Agency poses the question whether additional information would have improved the Council's ability to make a decision or bury key information. The City Council's decisions and approvals were based solely on information that was presented to them. The issue is that key data (i.e., cost of land) that was not presented may have swayed the decisions of the City Council. <u>Statement of Sources and Uses</u> The Agency stated that the sources and uses were only illustrating the costs to complete the project. A Project's Statement of Sources and Uses should include all resources needed to complete a project and should "consistently" include all costs, to properly and timely inform approving authorities and provide full disclosure to mitigate public protest. The Agency appears to misunderstand the purpose of Exhibit 2 as it also states that the audit did not consistently incorporate these costs in the report. As previously discussed, the Funding Sources (Exhibit 2) details the funding sources as presented to the Board, which omitted or failed to accurately reference land and predevelopment costs.

Comment	Page	Ref	Administration Response	TCBA Response
				<u>Project Budget and Financial Projections</u> The Agency states that the project budget and financial projections are typical for a normal project and would be true if the additional funds used to complete the project included conventional financing. The Agency appears to misunderstand the report's finding. The costs to "complete" vs. the costs in "sustaining" the project are different, but both important. The report's finding relates to the sustainability of the project (costs after completion), and at what cost to the Agency was the primary concern. <u>Financial Statements</u> The Agency contends that audited financial statements for FOT were unnecessary because FOT was a pass through entity to pay for smaller expenses. The level of funds "used" by FOT to cover expenses vs. those "passed through" should not dictate the importance of using audited financial statements. <u>Real Estate Appraisal or Valuation</u> The Agency states that it prepared a 33433 Report, as required under redevelopment law, which shows that the project requires the proposed Agency financing/subsidy. While the 33433 report showed that a subsidy was needed to build a project, absent Agency subsidy, this report should not serve as a comprehensive feasibility analysis. The purpose of the valuation is to assist in evaluating the project cost to project value and assess the project's potential return. The Agency contends that the importance of the project is placed on the value to the community. However, whenever public funds are utilized, affected citizens rarely discount the dollar value of public investment to derive catalytic economic effects to the surrounding community. The audit notes that this finding was first presented to the Agency in April 2011, at which point the Agency did not have any disagreements or issues regarding this finding. In fact, at both the Preliminary Findings meeting and the Exit conference, the Agency agreed with the finding. After numerous reviews over the course of 4 months, the Agency is now bringing forth comments regarding the finding.
26	18	4.Q	The Agency, COT, and CCG were successful in obtaining $32 million in capital and debt from Bank of America to fund the Fox Theater Project	The Agency's response indicates agreement with the report's finding.

Comment	Page	Ref	Administration Response	TCBA Response
27	19	4.R	The Agency, FOT and CCG were successful in creating a complicated governance structure to generate Historic and New Markets Tax Credit equity.	The Agency's response indicates agreement with the report's finding.
28	21	Exhibit A	Exhibit A	Not all of the Council Actions listed in Exhibit A were provided to the audit team, however, the audit agrees with the content and finds no reason to disagree with the content that is now being presented. The Council Actions presented in Exhibit A does not change the report's findings.

ATTACHMENT B
City's Response to the Fox Audit

CITY OF OAKLAND

CITY HALL • 1 FRANK H. OGAWA PLAZA • OAKLAND, CALIFORNIA 94612

Office of the City Administrator
Deanna J. Santana
City Administrator

(510) 238-3302
FAX (510) 238-2223
TDD (510) 238-2007

October 5, 2011

Courtney Ruby
City Auditor
City of Oakland

VIA Hand Delivery

Re: Revised Response to Fox Theater Project Performance Audit

Dear City Auditor Ruby:

I am submitting the Administration's Revised Response to the Fox Theater Project Performance Audit which addresses the Revised Draft Audit Report you provided to me on September 8th. Included in our revised response are the revised staff memorandum and point by point response.

As referenced in my letter to you dated September 16, 2011, the City Administration has been working closely with your office to review draft findings and recommendations and to complete the factual record. The Administration responded to a number of drafts and continued to clarify facts and provide supporting documentation during the audit process. While the Administration was in the process of completing a final response to the revised draft audit, your office released it to the press and the public.

The significant expenditure of taxpayer dollars involved in a project of this magnitude is a subject of great public importance, so it is unfortunate that the final audit was released without the Administration's final comments and documentation. I am requesting that you provide this Revised Response as part of the final Audit report.

I am concerned that the Audit did not achieve the intended goal nor did it include the Administration's final comments, clarifying facts and supporting documentation provided during the audit process. Further, we were not informed that you were providing advance review of the Audit Report to the press, which would have allowed us to issue a timely public response, absent being afforded the opportunity to have the Administration's final written response included in the Auditor's final report.

In addition, the management of this Project was considerably before my time and I have not had sufficient opportunity to personally validate the information provided in the Audit. Without the time afforded to me, I am relying on the diligent staff who have worked on both this Audit and the Project. As staff has shared with me, the Redevelopment Agency requested an audit of the project due to its complexity and the significant commitment of public fimds to this transformative project. Staff offers a compelling position that disputes many findings in the Audit report, and that deserves public review.

The nationally acclaimed Fox Theater renovation was a highly successfiil project that is serving as a centerpiece for revitalization of an area that had fallen iuto serious blight and disrepair. The Fox Theater has spurred economic development, dynamic growth and new revenues to Oakland—as was intended when originally conceived in 2001.

As with similar complex and historic renovation projects, the project involved multiple stages, successfully leveraged private dollars with public dollars, and had multiple funding sources and partners.

Due to the complexity of the project and because it involved significant investment of public dollars, in December 2009, the City Administration requested an outside audit of this project to validate the fiscal activities and status of the project and to identify any issues that may warrant fiirther due diligence and follow-up.

As demonstrated by our request for the independent review, the Administration acknowledges the importance of independent verification, analysis and feedback on cost control measures, project delivery, contracting processes, and internal controls to assure accountability. In those areas of the Fox Audit in which the Administration is in agreement, pro-active corrective plans are being developed. However, it should be noted that the Administration is not in fiill agreement with all the audit findings and recommendations.

Regarding the Audit Report's headline that the Project resulted in cost growth--the report fails to recognize the fact that the Fox Theater project was consistent with the comprehensive vision of Council, which was stated in 2001 and reaffirmed in 2003 and 2004, for the full historic restoration of the Fox Theater. The Audit Report inaccurately characterizes the renovation project cost as increasing by 172 percent because it compares the cost of the initial phase of the project to the cost of the full historic restoration. The estimate of $33 million noted in the Audit was for the initial phase of the project. The full cost of the project was always projected to include complete historic restoration of the Fox Theater. The actual final cost of the full historic restoration project was approximately $91 million.

When the 2001 estimated full renovation cost is adjusted for inflation, the actual cost at completion in 2008 would have been $98.3 million, **8%** ***below*** actual costs, not **172%** above as stated in the Audit.

The following is a summary of key areas of disagreement with the Final Fox Audit Report:

(1) The audit report fails to recognize the fact that the Fox Theater project was consistent with the comprehensive vision of Council, which was stated in 2001 and reaffirmed in 2003 and 2004, for the full restoration of the Fox Theater.

(2) The audit incorrectly references $33 million as the initial projected project cost. The Fox Renovation Project was originally planned as a multi-phased project. Initially the Council approved the first phase of the project, projected at $33 million. At that time funds were not identified for the entire project. However, when construction began in 2006, full funding was in place for the complete historic renovation of the project as originally envisioned, for a total project cost of $91 million.

(3) The final project costs were lower than originally estimated in 2003, after factoring in pre-development costs and the impact of inflation related to the costs of concrete and steel, which had skyrocketed during the national construction boom in the early-mid 2000's. Adjusted for inflation, the actual cost at completion of the project would have been $98.3 million; the final cost of the project, at $91 million, was 8% below projections, not 172% above as stated in the Audit.

(4) The Council was informed and engaged on the status and progress of the project. From the initial planning phase through the project completion, the Council was presented with numerous reports and/or approved resolutions on more than 14 occasions (Attachment C).

(5) Best practices in administration and oversight were performed on the project. The project was monitored with four different independent layers of oversight on the contracts, which included oversight by Redevelopment Agency Staff, oversight by the project manager, oversight by the contractor, oversight by the architect, and oversight by Bank of America's construction monitor. It should be noted that the Audit identified two instances of possible overpayment to two contractors that require further follow-up and analysis by the Administration.

(6) It appears that the Audit did not acknowledge all of the documentation provided with respect to the financial feasibility study conducted. The Administration provided the audit team with over 2,400 pages of financial closing documents consisting of loan documents, financial projections, operating agreements, the disposition and development agreement, and formation documents of the various entities of the Project. These documents provided the financial framework for the project and were instrumental in leveraging the Project's Redevelopment Agency funds with private funding, resulting in outside alternative financial sources that totaled over $45 million.

I look forward to working with your office to improve our public services and ensure the provision of accurate information to the public.

Sincerely,

Scott Johnson for

Deanna J. Santana
City Administrator

Attachments

- Memorandum from Patrick Lane, Redevelopment Manager
- Revised Point by Point Response to the Fox Performance Audit

October 5, 2011

To: Dearma Santana, City Administrator

From: Patrick Lane, Redevelopment Manager

Cc: Dan Lindheim, Margaretta Lin, Walter Cohen, Gregory Hunter

Re: Response to City Auditor's Audit of Fox Performance Audit

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This is an updated response to the Fox Audit and replaces the August 12, 2011 memorandum of the same name. To prepare this update I reviewed the September 8, 2011 final draft of the City Auditor's Fox Theater Project performance audit and made changes to the previous response based on corresponding revisions to the City Auditor's July 11, 2011 draft of the Fox Theater Project performance audit. Below is a summary of my responses. A more detailed response to the audit's findings and recommendations is provided in Attachment A, Point by Point Response to the Fox Performance Audit.

Three main points are critical to the understanding of the Fox Theater Project and the City's Audit responses:

- The Fox Theater is owned by the Redevelopment Agency and leased to a series of entities created to develop the project. The local funds for the project were provided by the Redevelopment Agency. The City/General Fund provided no funding for this project. Funding for the Project consisted of a combination of funds from the Oakland Redevelopment Agency, private investors through tax credit programs, loans, chartable contributions, state grants and a small federal grant. The Agency created Fox Oakland Theater Inc. - which created Fox Theater Manager, Inc., Fox Theater Landlord LLC and Fox Theater Master Tenant LLC all of which are collectively as "FOT" - for purposes of generating tax credit investments and other project needs.

- Given the complexity of the Project, the City administration requested that an outside audit be conducted to validate the fiscal activities and status of the project and to identify any issues that may warrant further due diligence and follow-up. The City Auditor's audit has revealed important information and City staff is engaging in the necessary follow-up work to address outstanding fiscal reconciliation and other issues.

- The audit incorrectly references $33 million as the initial projected project cost in 2004. In 2003, the Fox Renovation Project was planned as a multi-phased project, with approximately $33 million available in 2004 for the first phase. However, when construction began in 2006, full funding was in place for the complete historic renovation of the project as originally envisioned, for a total project cost of $91 million. The final project costs were lower than originally estimated in 2001, after factoring in pre-development costs and the impact of inflation related to the costs of concrete and steel, which had skyrocketed during the national construction boom in the early-mid 2000's. Adjusted for inflation, the actual cost at completion of the project in 2008 would have been $98.3 million; the final cost of the project, at $91 million, was 8% below projections, not 172% above as stated in the Audit.

1. The Fox Theater Project Was Always Envisioned as a Full Renovation Project And Costs Were In Line With Council Information and Approvals

Contrary to the audit report findings, the Fox Theater project was envisioned as a full renovation project since 2001. One of the concepts, the "Ruins/Basics" concept, contemplated different phases to be completed as time and funds were available. All significant aspects of the project were presented to City Council at numerous public meetings.

The final development costs for the Fox Theater, including acquisition, pre-development, soft and hard construction costs, was approximately $90.9 million. The original cost estimate of $66.9M, when adjusted for inflationary increases in construction costs and adding the predevelopment costs, was in line with the development costs presented to the Council in 2001 and discussed again in 2003 and 2004 for the complete restoration of the theater. Adjusted for inflation, the final costs at completion of the project were eight percent (8%) below estimates. Staff communications to Council regarding project costs and scope were more than adequate. The Council was provided reports and/or approved resolutions on 14 occasions, at least three of which included multiple meetings and supplemental reports when the Council requested additional information. These reports cross reference each other and all of the reports should be considered together, see the Chronology of Fox Theater Council Actions that is included with Attachment A.

2. Project Successfully Leveraged $45.5 Million from Outside Sources

Contrary to the audit finding, the City did not fund any costs related to this project; the only local funding for the Fox Project was provided by the Agency. By the end of 2011, after approximately $4.0 million in loans and grants have reimbursed to the Agency, the Agency's outstanding contribution of $45.4 million will have leveraged $45.5 million in outside funds, and the Agency's share of the costs will have fallen from 59% in 2004 to 50% in 2011. The outside sources of fimds included private investors through tax credit programs, loans, chartable contributions, and state and federal grants.

3. The Fox Theater Nearly Doubled the City's LBE and SLBE Participation and Met Council Requirements and Federal Regulations

Council agreed that the project should waive competitive procurement requirements in order to maintain strict project schedules and increase Small/Local Business Enterprise (S/LBE) participation levels. The Fox Theater achieved 37.47% S/LBE participation. The project's S/LBE participation was nearly double the City's requirements (20%), was greater than the FY 2007-09 Citywide S/LBE participation (35.92%) and much greater than the FY 2007-09 Citywide LBE/SLBE participation for Large Projects (28.84%). However the goals set for the project, 50% LBE/SLBE participation, were not met.

Construction of the Fox was broken down into smaller components in order to encourage the participation of LBE and SLBE contractors, which is a recommended approach by federal regulations. Notwithstanding Council's consent to the waiver of competitive bidding, most of the subcontracts for the project were competitively bid and, in some cases, bids were negotiated in order to come within project costs and to award to an LBE or SLBE bidder. Under federal guidelines, in general, projects with federal funding are to be competitively bid, but waivers are permitted. The applicable federal regulations permit awarding of contracts, such as design-build or construction manager contracts, on a non-low bid basis (price being one of the factors), 24 CFR § 85.36(3). Moreover, the federal procurement regulations allow for modification of award procedures when exigencies will not permit a delay. As stated above the primary reasons for modifying the contract award process was to avoid costly project delays. The Agency could not undo all of the previously awarded contracts long after the fact just because the federal grant was awarded. The grant was for two specific purposes: (i) electrical; and (ii) painting of the historic ceiling. The painting work competitively bid and awarded and the electrical contract was design/build.

4. Contracting Procedures and Internal Controls were Appropriate Including Monitoring of Turner and CCG's Contracts and Payments

The four different layers of project oversight provided ample contract administration and independence over project management decisions. Two of these layers also provided significant contract administration and independence over CCG and CCG's sub-consultants. Review of change orders, construction draws and other documentation followed traditional procedures, including review by the architect (Architectural Dimensions), owner's representatives (CCG development staff and construction experts), Redevelopment/FOT representatives (two architecture and renovation construction experts) and Bank of America had a construction monitor for their loan and equity funds. Construction change orders therefore went through multiple levels of review by various Agency professionals and expert consultants.

Summarized below are several possible contractor overpayments identified in the Audit that require further analysis. CEDA has requested that CCG provide the funds in question in an interest bearing escrow account in the interim and CEDA is considering bringing in an outside consultant firm to analyze payment details on the Tumer Construction contract.

- One of the Audit findings asserting overpayment of $178,726 to CCG for unsupported costs was found to be based on incomplete information. The Audit report does not reflected one month's invoices that were missing from spreadsheets presented to the auditor leading to a finding that unsupported costs of $178,726 were paid to CCG. Staff subsequently provided copies of the invoices to the Auditor supporting these costs.

- On another Audit finding the report overstates the potential overpayment of $178,843 in fees to CCG. It appears that $36,343 in payments for developer/management fees to CCG may be over payments, staff is reviewing records and discussing this issue with CCG and has requested repayment of these fimds. However, during the transition period when FOT was taking over the project, CCG was providing service without a contract. It therefore appears that $142,500 paid for services for April through August 2006 were reasonable.

- The audit identified a potential cost saving refund. FOT may be entitled to refimds due to potential costs being less than budgeted for Turner's contract. Under the contract with Tumer, project savings are split between Tumer (30%) and FOT (70%). The Audit identified a total of approximately $321,000 of savings. FOT may be due a refund of approximately $224,684. CEDA is in discussion with Tumer to determine if this is accurate and if necessary, CEDA may bring in an outside consultant to analyze the specific contracts and payment records.

While the Audit did not find that that there were any actual conflicts of interest, the Audit asserted that "controls to limit potential conflicts of interest were not used for the Fox Theater Project." Standard City of Oakland and State of Califomia conflict of interest requirements were used to limit potential conflicts of interest for the Fox Theater Project. Staff will review the City's conflict of interest policies and procedures to determine what, if any, changes are necessary to eliminate any potential conflicts of interest in future projects.

5. The Project Was Successful at Raising Outside Funds And the Feasibility Analysis Provided was Comprehensive

The financial feasibility analysis was more than adequate for the scope of the project—it appears that the Audit did not acknowledge all of the documentation provided with respect to the fmancial feasibility study conducted. The Administration provided the Auditor with over 2,400 pages of financial closing documents consisting of loan documents, financial projections, operating agreements, the disposition and development agreement, and formation documents of the various entities of the Project. These documents provided the financial framework for the project and were instrumental in leveraging the Project's Redevelopment Agency funds with private funding, resulting in outside altemative financial sources that totaled over $45 million.

Capital totaling $32 million from private altemative fmancing sources was successfully obtained to fund the Fox Theater Project

The govemance stmcmre created to attract private sector capital for the Fox Theater Project was necessary and adequate

6. The Project Has Been Instrumental in Downtown's Economic Revitalization.

The nationally acclaimed Fox Theater renovation was a highly successful project that is serving as a centerpiece for revitalization of an area that had fallen into serious blight and disrepair. The Agency spent over $130 million on the Fox Theater, Uptown, Fox Court, Telegraph Streetscapes and small Façade and Tenant Improvement Program projects in the area. The area has been transformed from being blighted and underutilized to being one of the hottest neighborhoods in the Bay Area. The Fox Theater has spurred economic development, dynamic growth and new revenues to Oakland—as was intended when originally conceived in 2001. The area now has two beautifully restored theaters that are the heart of an emerging entertainment district. The Theater attracted over 160,000 paying customers its first year, over 180,000 its second year and is projected to reach 200,000 in this, its third year. This is almost double the initial projection of 100,000 paying customers per year for the first three years. These visitors have enlivened the whole area and created a demand for new bars, restaurants, cafes, and entertainment venues, which continue to open—all of which contribute to Oakland's economy and tax base. The project has been a major artistic and economic success. In addition, the Fox Theater has received numerous awards celebrating its historic restoration see Exhibit B - List of Awards and Special Events, in Attachment A - Point by Point Response to the Fox Performance Audit.

7. The City Is Either In the Process of Implementing, Already Follows the Audit Recommended Practices and Procedures, or Partially/Fully Disagrees with the Audit Recommendations

As demonstrated by our request for the independent review, staff acknowledges the importance of independent verification, analysis and feedback on cost control measures, project delivery, contracting processes, and internal controls to assure accountability. In those areas of the Fox Audit in which staff is in agreement, pro-active corrective plans are being developed. However, it should be noted that staff is not in full agreement with all the audit findings and recommendations. The Audit report contains 17 recommendations—most of which were already conducted as part of the Project procedures and processes or have been implemented. Some of the recommendations are good practices that the City should implement, as part of efforts to continuously improve public service.

We concur with the Auditor's following specific recommendations:

Recommendation 7: Ensure that contract compensation provisions for future Agency contracts be tailored to each category of payment under the contract. For example, if a fixed amount is to be paid for a service, the compensation provision should identify the service and state that payment for that service is based on a "fixed fee". If there are costs that are to be reimbursed the contract should identify those costs and state that those costs will be reimbursed at cost without mark-up.

Recommendation 11: Perform a thorough examination of acmal cost incurred by Tumer under Phase 2 constmction contract to determine whether an adjustment in contract price is warranted. The City administration is in the process of implementing this recommendation.

Recommendation 12: Establish change order pricing procedures that require:

- The preparation of independent estimates of contract changes
- The preparation of detailed contractor change order proposals in accordance with specific criteria on allowable costs and mark-up
- Use labor rates at prevailing wage levels (unless justified by documentation)
- The performance and documentation of a cost analysis of contractor proposals, and
- The preparation of records of negotiation.

The following recommendations are areas that the City administration followed as part of the Project procedures and protocols:

Recommendation 2: Develop policies and procedures and/or a policy for future capital projects, that states what, when and how information regarding project scope and costs should be communicated to the City Council/Committee by the respective City agency.

Recommendation 3: For future projects, evaluate ways to increase LBE and SLBE participation without limiting competition and complying with applicable Federal and State laws on competitive bidding and allowable local preferences.

Recommendation 4: Develop procedures to ensure that waivers of competitive procurement are not in violation of federal grant requirements.

Recommendation 5: Utilize contracts that provide incentives for cost savings instead of cost growth. If constmction manager at risk contracts are to be used, the contract should be stmctured so that the constmction manager assumes significant risks.

Recommendation 6: Ensure contractual decisions are made by individuals that are independent and objective, and do not directly benefit from contractual decisions.

Recommendation 8: Establish procedures to ensure that adequate records are maintained on the contract amounts paid, and on the basic and amended contract value of all contracts under a project, and that cumulative payments are checked against contract balances prior to authorizing contract payments, and contract amendments are executed where appropriate.

Recommendation 9: Request supporting documentation from CCG for all unsupported costs and if documentation is not provided, these costs should be retumed to the Agency.

Recommendation 16: Adopt policies and procedures to conduct a comprehensive financial feasibility analysis of the changes to a project's scope and adjust the relevant components/elements of the financial feasibility model.

Recommendation 17: Consider hiring competent third party assistance with relative experience in the area of financial feasibility modeling and implementation to the extent that the Agency lacks the time, staff or competency.

The following recommendations are areas that were not supported by Audit findings or Project facts, but are general best practices for City projects.

Recommendation 13: Update AI 595 to make clear that those involved in selecting vendors be guided by the requirements of Califomia Government Code Section 1090.

Recommendation 14: Implement a process that requires all individuals involved in selecting vendors (including non-City employees) on City sponsored projects (including projects sponsored by non-City entities established by the City) to sign conflict of interest disclosure statements identifying any potential direct or indirect financial interests in any such vendors under evaluation.

Recommendation 15: Develop a comprehensive constmction project management policies and procedures manual detailing the significant policies and procedures for effective management, oversight, and administration of large capital improvement projects.

The following recommendations are ones with which the City administration disagrees or partially disagrees.

Recommendation l: For future capital projects, project scope should be reevaluated only when funding sources are guaranteed and secured. If funding sources are not guaranteed, a contingency plan should be in place to reduce the project scope if those funds are not received.

Recommendation 10: Seek recovery of the $178,843 in Developer/Management fees overpaid to CCG (See comments in Section 4, Page 3 above.).

Details about the City's responses to the Audit recommendations are provided in Attachment A.

ATTACHMENT A

Point by Point Response to the Fox Performance Audit

AUDIT FINDINGS: CHAPTER 1 - Fox Theater Project Scope And Cost Increased By 172 Percent Or $58 Million From Initial Inception To Final Constmction

Audit Recommendation #1 - For future capital projects, project scope should be reevaluated only when funding sources are guaranteed and secured. If funding sources are not guaranteed, a contingency plan should be in place to reduce the project scope if those fiinds are not received.

Audit Recommendation #2 - Develop policies and procedures and/or a policy for future capital projects, that states what, when and how information regarding project scope and costs should be communicated to the City Council/Committee by the respective City agency.

RESPONSE– The Fox Theater Project Was Always Envisioned as a Full Renovation Project And Costs Were In Line With Council Information and Approvals.

The purpose of redevelopment is to eliminate blight. The Fox Theater was one of the key projects for revitalizing the Uptown neighborhood. The Agency spent over $125 million on the Fox Theater, Uptown, Fox Court, Telegraph Streetscapes and small Façade and Tenant Improvement Program projects in the area. The area has been transformed from being blighted and underutilized to being one of the hottest neighborhoods in the Bay Area. The Fox Theater is the critical element of this revitalization. Drawing almost 200,000 customers per year, the theater has created a demand for new bars, restaurants, cafes, and entertainment venues, which continue to open. The Theater has achieved even more than expected.

Since 2001 the Fox Theater project was envisioned as the full restoration project that was ultimately completed and the project scope and costs did not increase significantly. One of the concepts, the "Ruins/Basics" concept, contemplated completing the full renovation in phases as funds became available. Other concepts included full renovation of the theater. The City Council and Agency Board were provided this information on several occasions and even approved a resolution stating this was the intent. All significant aspects of the project were presented to the Community and Economic Development Committee and the City Council at numerous public meetings, including 14 reports and at least five supplemental reports; see Exhibit A, Chronology of Fox Theater Council Reports.

A. The Cost of the Fox Theater Project Was Eight Percent Under the Initial Estimate When Adjusted for Inflation and Predevelopment Costs. The audit incorrectly references $33 million as the initial projected project cost in 2004. In 2003, the Fox Renovation Project was planned as a multi-phased project, with approximately $33 million available in 2004 for the first phase. However, when construction began in 2006, full funding was in place for the complete historic renovation of the project as originally envisioned, for a total project cost of $91 million. The final project costs were lower than originally estimated in 2001, after factoring in pre-development costs and the impact of inflation related to the costs of concrete and steel, which had skyrocketed during the national construction boom in the early-mid 2000's. Adjusted for inflation, the acrual cost at completion of the project in 2008 would have been $98.3 million; the final cost of the project, at $91 million, was 8% below projections, not 172% above as stated in the Audit.

On April 24, 2001 Council was presented with an informational report outlining various options for rehabilitating the Fox Theater and the estimated costs for each. The report was based on analysis by Hardy, Holztman, Pfieffer - nationally recognized theater consultants. In 2003, after considering several proposal for the Fox renovation, the Agency selected Califoruia Capital Group to proceed with developing plans and costs estimates for the first phase, based on the ruins concept, of an ultimate completed renovation. The resolution approving CCG funding clearly intended the ruins concept to be a temporary first step in the theater renovation.

> WHEREAS, the CCG development team has prepared concept drawings and detailed cost estimates for revitalizing the Fox Theater into a cabaret-style performing arts venue that would activate the Fox for an unspecified time period before future funding could be obtained for a full theater restoration [Agency Resolution 2003-83 (December 2, 2003)];

In 2006, when substantial additional sources of funds became available primarily through federal tax credits and state grants, the project could be accelerated, skip over the limited "ruins" phase, and move directly to the full renovation. Contrary to numerous explanations from staff describing the cost of the project, the starting point for the audit cost analysis was the ruins concept that was never intended to be the final project and was never approved or funded. The audit finding regarding the increase in costs is therefore distorted and misleading. The figures used in Exhibit 2 Funding Sources and Exhibit 3 Comparison of Project Costs were from diverse sources and the auditor was unable to match the line items for an accurate comparison. Some of the discrepancies include:

1) The full project was presented in 2004 as an alteruate and the final project costs were eight percent below the estimate by the theater consultants when adjusted for inflation. The final development cost of the theater, including the purchase price and improvements previously paid by the Agency, was $90.9 million. The Fox Master Plan in 2001 estimated the full theater renovation "Roadhouse" concept at $66.9 million, based on 2001 construction costs. Inflation in construction costs between 2001 and 2006 was approximately 24.8% or 4.5% per year based on Engineering News Record San Francisco City Cost Index/Building Cost Index. By adjusting the 2001 "base" cost estimate for the full renovation project for inflation, the cost in 2008, when the project was completed, is $98.3 million The final actual cost at $90.9 million is eight percent below the inflation adjusted estimate. The final project included grants and loans for upgrades requested and partially paid by Another Planet Entertainment ("APE") and Oakland School for the Arts ("OSA"), and the additional improvements for the "Restaurant Space", and the development cost were still actually less than the first estimates.

2) The Audit comparison is between different projects – 1) the mins concept for a 500 seat cabaret venue and limited renovation of wrap around buildings for OSA versus 2) the full theater restoration of a 3,000 person performance venue and renovation of the wrap-around buildings for the OSA, including significant additions to the second and third floors, a restaurant and bar.

3) Both major tenants of the Fox required additional improvements. When the project was being analyzed in 2004 and 2005 under the original contract with California Capital Group ("CCG") no operator had been found for the theater and OSA was still fund raising and programming its needs. The budget prepared at the end of this analysis was much different than what was built. Both tenants provided capital funds and requested increased scope, including:

    a. APE provided $500,000 for tenant improvements in its lease, but required substantial changes to the theater that were over and above its contribution. APE essentially requested the fully restored theater minus the fixed seating on the main floor to allow the theater to operate with either a 3,000 person capacity with general admission or approximately 2,500 person capacities with movable seating.

    b. OSA obtained the CBS billboard revenue and used this for lease payments which then leveraged a $6.5 million conventional loan. OSA also pledged to provide a $1.5 million Charter School Facility Incentive Grant, which OSA was unable to secure; instead OSA provided cash through a fund raising campaign. With these funding sources provided by OSA, came an expanded scope including providing arts spaces in the new 2nd and 3rd floor additions to the two one-story wrap buildings. OSA also pledged to build out the $3.7 million in tenant improvements for these additions. The project scope and funding sources were substantially motivated by the tenant driven changes.

4) The "Ruins Concept" anticipated Agency on-going operating subsidies and major renovations in the future, with additional Agency expenditures. Comparing the final renovation cost of the theater to the estimated costs of the "mins concept" (first phase only), over estimates the overall increase in acmal project costs substantially. In the mins concept presented to the Council, the Paramount Theater of the Arts would have been the operator, and would have required a $500,000 per year operating subsidy from the Agency. The Theater would have initially operated at a reduced capacity, no balcony and only 500 to 600 seats on the first floor, meaning limited ticket revenue. It would have also required major additional improvements in the fumre to increase capacity and ticket sales and reduce the operating subsidy, but with additional Agency development subsidies required. This would be more expensive than what was actually built because it is more expensive to do work in multiple phases and it would intermpt operations at the theater.

5) The budgets presented to the City Council in 2004 and 2006 excluded the cost to complete, although the reports describe the previous costs - $6.5 million spent by the Agency on purchase of the property, improvements and predevelopment planning. The audit compared these Sources with a Final development budget that for tax

credit purposes included appraised value of the FOT lease with the Agency $9.7 million. Thus the Audit's use of the $9.7 million figure exaggerates Agency contribution in the final sources figure; to be accurate the cost to the Agency of $6.5 million should be included in all sources columns.

6) The use of Historic Tax Credits in the project required additional improvements in order to comply with the historic preservation requirements and receive any historic tax credits. The National Parks Service required revisions to the Phase II application for certification of the project for historic tax credits before the start of constmction, including reconfigured the new building to set back from the historic building farther and other smaller changes. The Phase III required further revisions to the building after the receipt of the temporary certificate of occupancy, including building out the restaurant space and minor finish revisions such as painting the namral wood window frames brown. Not making these changes would have prevented the project from receiving approximately $15.7 million in enhanced tax credit equity.

When all of these comments are considered, the Sources and Uses are balances at approximately $90.9 million.

B. The City Did Not Pay for Any Project Costs. Contrary to the audit finding, the City did not absorb any increased project costs or fund any project costs at all. First, the City (General Fund and other City funds) did not fund the project at all. This was a Redevelopment Agency project and only Redevelopment funds were involved. Second, most of the increased costs were financed through tax credits, conventional loans, and outside grants. The Agency did make additional loans to support the project after construction began, some of which have already been repaid. Several of those loans are on full repayment schedules and/or will be reimbursed from grants. The other Agency loans (approximately $39.8M) may be partially repaid but the remaining loan balances can be converted to Agency equity ownership of the Fox at the end of the financing process. The percentage of the project to be funded by the Agency acmally fell from 59% to 50% from 2004 to 2011 as the following table shows:

The important comparison should be between Agency and non-Agency sources, which fell as a percentage as the development team was able to secure additional funding sources. Although several grant sources were not secured, the project continued to secure additional grant and other equity and loan sources. In particular, Bank of America invested additional equity because of increased tax credits and also brought in a new source of New Market Tax Credit enhanced debt through the Local Initiatives Support Corporation. This change funding sources for the Fox Theater can be seen in the following table:

Changes in Funding Sources

	2004	% Project	2010	% Project	Change	% Change
Agency	$19,650,000	59%	$49,400,250	54%	$29,750,250	151%
Other	$13,850,000	41%	$41,485,713	46%	$27,635,713	200%
Total	$33,500,000	100%	$90,885,963	100%	$57,385,963	171%

	2004	% Project	2011	% Project	Change	
Agency	$19,650,000	59%	$45,400,250	50%	$25,750,250	131%
Other	$13,850,000	41%	$45,485,713	50%	$31,635,713	228%
Total	$33,500,000	100%	$90,885,963	100%	$57,385,963	171%

While the City did not pay for any of the costs, it benefits from increases in tax revenues direct from the theater, restaurant, and bar operations in the project and indirectly from the additional economic activity the theater generated for bars, restaurants and other retail and entertainment businesses in the Uptown Area and throughout the Downtown.

C. It is often not possible to set the budget for City and Agency capital projects after funding sources are guaranteed and secured. Funding sources are apt to change and the City needs to maintain flexibility. There are several types of projects that frequently have this issue, including:

Phased Projects – Which often are planned to change their scope and schedule as funds are obtained. This is how the Fox Theater project was initially proposed. These projects usually have much greater scopes than budgets and continually reevaluate fimding sources, phasing and schedules.

Grant Funded Projects - Often need to complete the design phase before applying for grants and then modify the scope after the grant is awarded and the grant amount is determined. If there are multiple grants and/or funding sources the scope may change several times.

Redevelopment Agency Funded Projects – Are often modified after new Agency funds are obtained. In the Fox Theater Project the initial 2004 budget was set based on the funds available from the Central District 2003 Bonds. The project scope was expanded after the Agency issued the Central District Series 2005 Bonds and the scope expanded again after the Central District Series 2006 Bonds were issued. The Agency was also able to identify other funds in 2008 and 2009 that allowed the scope to expand.

D. The project was unable to secure approximately $7.6 million in grant funds and the Agency had to provide additional funding, but a substantial portion will be repaid. OSA has already repaid over $1.0 million of the fimds it borrowed from the Agency and will repay the remaining $1.7 million by the end of the year reducing the unsecured funds to approximately $4.9 million. Furthermore, the Council was never told all of these grants would be available at the same time and the amounts mentioned in most of the reports was the maximum allowable not the amount the project was likely to receive. In addition, some of the grants replaced other grants. The Agency provided a $7. 5 million bridge loan for several grant sources that only partially materialized. There seem to be several misunderstandings related to the list of funding sources that were not secured, including:

1) Proposition 55 Grant ($4,983,922) - The grant was eliminated in the predevelopment phase when it was realized that the grant's requirements and process would not work with the proposed project. In discussion with the state, the Federal Charter School Facility Grant, which is also awarded through the state, was offered as a replacement for Prop 55. These 2 grants were therefore never expected together and have never been shown in the same budget to the Council. The Federal Charter School Facility Grant was with OSA and OSA was required to provide it under its lease with FOT. When this source was not received, OSA made payments in lieu of the grant. If the OSA payment is included in lieu of the Federal Charter School Facility Grant, and the Federal Charter School Facility Grant as a partial replacement for the Proposition 55 Grant, then the unsecured Proposition 55 Grant was <u>$3.5 million</u>. With the loss of the Proposition 55 grant, OSA was also required to build $4.5M of it's tenant improvements and the OSA rent, paid through the CBS billboard revenue, was used to borrow $6.5M from Bank of America. When OSA could only raise $2.2M, OSA borrowed $2.3M from the Agency. OSA has paid almost $1.0M and is expected to repay the remaining $1.7M by the end of the year. If the OSA Capital and the CBS Revenue/$6.5 million Bank of America Loan is considered a replacement for the Proposition 55 Grant, then the unsecured amount was <u>$0</u>. This illustrates how successful the project was at replacing eliminated sources given the fluid nature of grant funding and fund raising for the Agency, FOT and OSA.]

2) Proposition 40 Grant ($1,048,607) – The project was awarded funds in three different application rounds and in the end was only $548,607 short of the maximum allowable grant. The Agency received an additional $500,000, but the funds could only be used for activities after the grant award and so have been used to fund the tenant improvements for the "Restaurant" and "VIP Space" on the comer of 18th Street and Telegraph Avenue. This area was left vacant until leases were signed. The tenant improvements have and will be completed in 2011 and processing of this grant continues. The portion not secured was only <u>$548,607</u>.

3) FOOF Fund Raising ($770,000) - If the Bank of America Grant is added to the other FOOF payments, $800,000 was raised. The unsecured portion is only <u>$200,000</u>. What's more, the $1.0M estimate for FOOF fimd raising was made in the predevelopment phase before any fimdraising had begun. The fund raising was acmally higher than estimated when the project was approved for development in 2006 and FOOF is continuing to fund raise to repay the $1.3 million Agency loan.

<u>Actual - Funding Sources that was not secured</u>

3,483,922	Proposition 55 Grant – This was replaced partially by Charter School Grant
548,607	Proposition 40 Grant (only received $4.5 million not full $5.0 million)
375,000	State Facade Grant (only received $375,000 not full $750,000)
200,000	FOOF ($230,000 plus 3 - $190,000 Bank of America Grant payments)
3,006,000	HUD Funding (only received $594,00 not full $3,600,000)
$7,613,529	**Total for unsecured funding**

($2,700,000) OSA Repayments
($783,922) CBS/Bank of America Loan off set for Prop 55
$4,129,607, Funding Shortfall

If all of these issues are considered, the unsecured funds are $7.6 million; which is offset by the approximately $1.0 million that has already been repaid by OSA, another $1.7 million that is expected before the end of the year and the rest of the short fall for the unsecured Prop 55 funds was replaced with a $6.5 million loan based on the CBS billboard revenue to OSA. The Agency has had to make up for about $4.1 million in unsecured funds.

E. Council was provided complete information regarding Fox project costs and options. Based on review of Board reports and observing taped City Council sessions regarding the Fox Theater Project, the audit erroneously found no evidence that the City Council was provided with the following: 1) Project ahematives during the design phase; 2) Options to reject or modify the project; and 3) Changes to the scope of the project identified as required changes or proposed changes.

These conclusions are based on considering each report and Council action separately. Council reports often reference and discusses previous activities. The former reports are considered part of the current report. The reports and resolutions reference the earlier reports and other documents such as the Initial Study/Mitigated Negative Declaration and the report required under Section 33433 of the Califomia Health and Safety Code ("33433 Report"). The 33433 Report includes: the estimated fair market value of the property at the highest and best use and the value of the interest conveyed under the disposition and development agreement also referred to as a reuse appraisal. The Council was provided reports and/or approved resolutions on 14 occasions, at least three of which included multiple meetings and reports, see Exhibit A, Chronology of Fox Theater Council Reports. The July 18, 2006 report when the Council approved proceeding with the project, was extensively detailed. The Council has always indicated when it needs additional information as it did for the 2006 report. The Council sought additional information on the subcontracts and it was provided in a supplemental report. If the Council needed additional infonnation at any stage, it would have requested it. Several times the Council approvals were delayed for one or more supplemental reports (June 27 and July 18, 2006 for the DDA with FOT or December 1, 2009, December 15, 2009 and January 5, 2010 for the additional $2.0 million Agency loan).

More infonnation and details were presented to Council than perhaps any project other than the Army Base. Nevertheless, the Agency Administrator has requested that we conduct a brief review to identify any "lessons leamed" regarding whether there was an absence of required policy action on the part of Council for the purpose of analyzing areas where the legislative process could have been more clear or transparent.

AUDIT FINDINGS: CHAPTER 2 - Agency Justified Awarding Contracts On A Sole Source Non Competitive Basis By Requiring LBE And SLBE Subcontractor Participation

Goals Be Established At Higher Than Normal Levels. However, LBE And SLBE Participation Goals Were Not Achieved

Audit Recommendation #3 - For future projects, evaluate ways to increase LBE and SLBE participation without limiting competition.

Audit Recommendation #4 - Develop procedures to ensure that waivers of competitive procurement are not in violation of federal grant requirements.

RESPONSE - The Fox Theater Nearly Doubled the City's LBE and SLBE Participation and Fully Met Council Requirements and Met Federal Regulations.

There is no way to increase LBE and SLBE participation without limiting competition. Reducing who you want to contract with, i.e. to LBE and SLBE, automatically reduces competition. The project waived competitive bidding to allow the contractor to seek bids and then if necessary negotiate with LBE and SLBE to match or come close to the lowest bid so they could be awarded the contract.

F. The S/LBE participation was higher than program requirements, the Citywide average and similar projects. The Agency, as a grantor and lender for the Fox Theater project, approved FOT's intent to modify contract award procedures. What the Audit failed to mention was that the approval of modified award procedures was done primarily to ensure the project moved forward in a timely manner, to lower costs, in addition to better enable the project to achieve higher LBE and SLBE participation goals. The resolution approving the waiver states the following as the rational:

> WHEREAS, in order to better enable the Developer to maintain strict project schedules with respect to project deadlines and flexibility to increase local and small business participation and attempt to attain the goal of fifty percent (50%) Local Business Enterprise (LBE) and twenty percent (20%) Small Local Business Enterprise (SLBE) participation that the Agency desires, it is recommended that the Agency authorize the Developer to waive competitive bidding and request for proposal requirements for all professional services, procurement and construction contracts needed to complete construction of the Fox Theater Project, and to employ non-competitive means for selection of contractors and award of such contracts; [Agency Resolution 2006-0057, p. 4 emphasis added].

The staff report discussed the need the need to modify competitive bidding requirements in order not only to achieve higher LBE and SLBE participation, but more importantly to permit negotiating with contractors and subcontractors to lower costs, and to avoid the potential for bid disputes that might delay the project. [Agency Report, July 15, 2006, p. 16]. The project had two major concerns that required the project to move rapidly: 1) Fox Court needed to start construction or the Agency was liable for a fee for delaying the project and OSA was required to relocate and temporarily occupying space on San Pablo Avenue for its portable classrooms; and 2) these classrooms were restricting access to businesses in the area. The Agency was therefore motivated to complete the project as rapidly as possible. The report also noted at the outset that time was of the essence to proceed quickly because: subcontractor bids had been received, but were only valid for a limited time, and delays could cause the materials and labor to increase if the project had to be rebid; In addition, and most important, OSA had to move from its temporary site behind the Fox to make way for a housing project (which the Agency had already approved for that site) to avoid being in violation of an existing development agreement and a $400,000 increase in an agency loan to the developer. Thus, the use of modified contract award procedures was concemed with moving the project expeditiously forward to avoid cost increases and project delays.

Moreover, the supplement report dated July 18, 2006, showed that subcontracts for the project were competitively bid and the resuhs of that bidding for the subcontractor selection process to date. Staff noted that despite significant outreach efforts negotiating with bidders was necessary to increase particularly the SLBE representation in the project.

Although it is true that the project did not meet the LBE/SLBE goals set by the Agency Board in the July 18, 2006 resolution. But, as the resolution states, the effort was only to "attempt to attain the goal of fifty percent (50%) Local Business Enterprise (LBE) and twenty percent (20%) Small Local Business Enterprise (SLBE) participation". [Agency Resolution 2006-0052, p. 4.]. The report also discussed the difficulty the project would have meeting this goal:

> The pre-bid goal for this project is to attain 50% LBE and 20% SLBE for contracts for the project. A summary of the bids shows that out of the 113 bids received, 39% were from LBE firms and 27% from SLBE firms. Acceptance of only the low bidders will result in 43% LBE and 12% SLBE participation. This exceeds the City of Oakland's S/LBE requirements by over 100%, but is lower than the 50% goal. [Report July 18, 2006 page 7].

When all of the project phases were bid, the LBE participation fell, but the SLBE participation increased. It is the SLBE participation that is hardest to increase in large projects. The larger the project, the more you need to break the project up in order for the elements to be small enough for small contractors to bid.[1] The audit compared the participation in the Fox Project with the participation in citywide projects in FY2007-09. This is an invalid comparison, because it does not take into account the fact that many small projects are 100% SLBE and other projects are 100% S/LBE.

A more valid comparison than the one referenced in the audit report, would be to compare the Fox Theater Project to the eight large affordable housing projects completed in FY 2007-09 (14th Street Apartments, Coliseum Gardens Phase III, Mandela Townhomes, The Orchards on Foothill, Jack London Gateway Senior Housing, Tassafaronga Village, St.

[1] Along this line, federal regulations suggest breaking up larger projects into smaller components to encourage participation by smaller and minority businesses.

Andrews Manor and 10800 Edes Avenue Homes Phase B). These represent 41.10% of the projects in this period; and the results is very different. These projects are also building projects with multiple disciplines, similar to the Fox Project. The total S/LBE participation projected by early bids was 43%, the Fox acrual S/LBE participation was 37.47%, the FY 2007-09 Citywide S/LBE participation was 35.92% and the FY 2007-09 Citywide Large Project S/LBE participation was 28.84%. Thus the Fox bettered participation in similar size projects.

	SLBE	LBE	Total
Fox Predevelopment (Lowest Bids)	12.00%	31.00%	43.00%
Fox Actual	19.41%	18.06%	37.47%
Citywide 2007-2009	20.11%	15.80%	35.92%
Large Projects Citywide 2007-2009	15.53%	13.31%	28.84%

From this analysis, it is still correct to conclude that the higher goals were not met, but the Council was apprised that the goals might not be achievable when the Council was asked to approve the project and the bidding method. What is more important is that the project was able to achieve substantially higher S/LBE participation than other large building projects by waving the competitive bidding requirement, 37.47% versus 28.84%.

We also note that the Agency transferred the Fox property to FOT as a non-profit corporation and its for-profit subsidiaries as entities separate from the Agency and City to be developed under a 60 year lease and a disposition and development agreement. FOT and its subsidiaries are not public entities and not subject to statutory restrictions on contractor hiring procedures unless required in the DDA or funding agreements. . However, However, where the Agency is acting as a lender or dealing with a less experienced developer, the Agency may include DDA terrus that would perruit Agency approval of construction contracts, contractor, and tenants in a commercial project—just as a comruercial lender. to better assure the Agency that project will be successful and in the event the Agency has to take back an uncompleted project, the Agency would have a construction contract and contractor it can live with. Because the Fox project included substantial Agency funds and the Agency had reversion rights in the project, Agency staff wanted to include the Council in more of the decisions than would be typical in an Agency assisted development and sought Council approval for modified contracting procedures.

G. The project met federal regulations. The City received a grant of $600,000 as part of an earmark for a small portion of the Fox construction costs as part of an earmark. The grant agreement was executed on March 13, 2008; by then construction had been underway for some time and subcontractors selected. The grant agreement specified that it applied to two specific items of work: restorative painting and electrical work. The restorative painting was competitively bid and the electrical work was performed on a design-build basis. The applicable federal regulations permit awarding of contracts, such as design-build or construction manager contracts, on a non-low bid basis (price being one of the factors). 24 CFR § 85.36(3). Moreover, the federal procurement regulations allow for modification of award procedures when exigencies will not permit a delay. As discussed in section 2C above, one of the primary reasons for modifying the contract award process was to avoid costly or fatal project delays. Thus, federal bidding processes were complied with for the portions of the project the grant applied to. Further, to have the $600,000 grant control how the entire $91.5 million project proceeded would be a case of the tip of the tail wagging the dog; more funds would arguably have been spent complying in all aspects of the project than the amount of the grant was worth. But, as stated above, the project complied.

There is no evidence that not using a fully competitive process increased costs; it may have reduced costs. The audit suggests that non-competitive procurement process may have resulted in higher costs. This is pure speculation and not borne out by any facts. The City and Agency permit waivers on their projects in part because full competitive bidding is not necessarily the best way to achieve the lowest price or the best overall results. Bidding can increase project costs in several ways: preparing full bid packages and responding to inquiries increase the costs for design professionals, bidders may build in more profit and risk into bids; bidders may include additional amounts in the bid in order to cover the fact that they win some bids and lose others; a bid contest can delay projects by many months increasing carrying costs; and if a prime contractor delays or fails to complete a project, the costs can be catastrophic to a project. These problems are minimized when a constmction manager is used and the subcontracts bid or negotiated. Constmction managers take less profit because there is less risk. It is easier to readily replace a subcontractor who fails to complete than the entire contractor. Given the risks of litigation if the housing project failed to start on time or the delay that could risk losing millions of dollars in tax credits, the manner in which FOT and the Agency proceeded was the most pmdent.

The construction management contract was awarded to Tumer on a percentage industry standard basis. The contract was based on a standard American Institute of Architects constmction manager at risk contract form. Tumer did not use its crews to perform any acmal construction work on the project, but supervised the work of the subcontractors through its percentage allowance. All the subcontracts were bid or utilized design-build. The Agency Supplemental Report dated July 18, 2006 set out the significant efforts undertaken by project managers to solicit bids and to obtain bids from LBE and SLBE firms. Part of those efforts provided LBE and SLBE with technical assistance to put them on a more competitive basis in bidding on the Fox project. The waiver was intended permit negotiation so that the costs could be lowered or LBE and SBLE firms could participate in the project. If the entire constmction contract were competitively bid, not only would this have resulted in more time being lost, but because all the subcontracts were bid, would most likely not have resulted in any cost savings over fully competitively bidding all of the subcontracts.

AUDIT FINDINGS: CHAPTER 3 - Inadequate Project Organizational Stmcmre And Contract Oversight And Administration By The Agency Resulted In Payments Exceeding Contract Authorized Amounts And Overpayment Of Contractor Costs

Audit Recommendation #5 - Utilize contracts that provide incentives for cost savings instead of cost growth. If constmction manager at risk contracts are to be used, the contract should be structured so that the construction manager assumes significant risks.

Audit Recommendation #6 - Ensure contractual decisions are made by individuals that are independent and objective, and do not directly benefit from contracmal decisions.

Audit Recommendation #7 - Ensure that contract compensation provisions for future Agency contracts be tailored to each category of payment under the contract. For example, if a fixed amount is to be paid for a service, the compensation provision should identify the service and state that payment for that service is based on a "fixed fee". If there are costs that are to be reimbursed the contract should identify those costs and state that those costs will be reimbursed at cost without markup.

Audit Recommendation #8 - Establish procedures to ensure that adequate records are maintained on the contract amounts paid, and on the basic and amended contract value of all contracts under a project, and that cumulative payments are checked against contract balances prior to authorizing contract payments and that contract amendments are executed where appropriate.

Audit Recommendation #9 - Request supporting documentation from CCG for all unsupported costs and if documentation is not provided, these costs should be retumed to the Agency.

Audit Recommendation #10 - Seek recovery of the $178,843 in Developer/Management fees over paid to CCG.

Audit Recommendation #11 - Perform a thorough examination of acmal costs incurred by Tumer under the Phase 2 constmction contract to determine whether an adjustment in contract price is warranted.

Audit Recommendation #12 - Establish change order pricing procedures that require:

1. The preparation of independent estimates of contract changes
2. The preparation of detailed contractor change order proposals in accordance with specific criteria on allowable costs and mark-up
3. Use labor rates at prevailing wage levels (unless justlfied by documentation)
4. The performance and documentation of a cost analysis of contractor proposals, and
5. The preparation of records of negotiation.

Audit Recommendation #13 - Update AI 595 to make clear that those involved in selecting vendors be guided by the requirements of Califomia Government Code Section 1090.

Audit Recommendation #14 - Implement a process that requires all individuals involved in selecting vendors (including non-City employees) on City-sponsored projects (including projects sponsored by non-City entities established by the City) to sign conflict of interest disclosure statements identifying any potential direct or indirect financial interests in any such vendors under evaluation.

Audit **Recommendation #15** - Develop a comprehensive construction project management policies and procedures manual detailing the significant policies and procedures for effective management, oversight, and administration of large capital improvement projects.

RESPONSE - Project Change Orders are Common Industry Practice and Contracting Procedures and Internal Controls were Appropriate Including Monitoring of Turner and CCG's Contracts and Payments

This was not a standard City capital project. Procedures and practices were amended to meet the complex requirements of the tax credit investors and the various grantors for the project. The project actually added layers of oversight because of the structure. Independent and objective City/Agency staff was involved in the decisions for the project in several capacities. City personnel acted in both their normal roles as Agency project managers and functioned as the board, officers and staff for the various FOT entities. Most of the findings for this chapter are either fail to appreciate the projects unique character or overstate potential problems without finding actual examples where there problems occurred. But three of the recommendations - #9, #10 and #11 - highlighted areas where the Agency needed to verify that expenditures were appropriate. After additional review most of these expenses were determined to be justifiable, but further review is needed for a couple items.

H. The Project organizational structure provided sufficient independence over project management decisions. The Audit concludes the arrangements with Turner and CCG present a conflict because their compensation increased when change orders were approved. This arrangement is no different than the typical construction contract and fee developer arrangements.

At a very early stage in the project Agency staff informed the Council that the general contract would not be bid. In a report to Council in 2005, Agency staff stated its intent to hire a construction manager and bid the subcontracts in lieu of bidding the entire contract. [Report June 28, 2005 p. 9.] In such an arrangement, a construction manager has no risk in the construction. In negotiating the construction management contract, FOT decided to move some of the construction risk onto the construction manager in the project by modifying this approach and moving from a straight construction manager contract to a construction manager-at-risk arrangement. The construction manager at risk contract form was a standard AIA form contract modified for the Fox project. The contract was negotiated using outside counsel expert in construction law matters

Further, the audit is mistaken when it concluded that CCG increased its income based on increased change orders. Although in the beginning FOT's contact with CCG was loosely based on two percent of the construction costs, less than standard for such agreements, subsequent amendment were not based on increased costs, but rather on the basis of actual work performed and CCG's costs over time. Although final CCG payments may have approximated two percent of the actual development costs--that is coincidental and not by design.

Of course the Fox constmction had change orders. The rehabilitation of a stmcture that has been abandon for 35 years was a high-risk venture; the addition of historic renovation standards made it riskier and more likely that changes orders would be required. Moreover, bidding the constmction contract would not have affected the number of change orders. Bidding by general contractors would not have changed the bid documents from those that the subcontractors originally bid on. The Fox projects treatment of change orders was no different than in other constmction jobs. In any typical constmction contract, change orders additive change orders include profit, risk and overhead. Additionally, the costs for architect and engineering services increase because these services are needed to assist in evaluating change orders and preparing documentation. Further, Fox project management worked throughout the project to reduce constmction costs through negotiating change orders, rejecting many, value engineering, and deductive change orders.

But the audit does not find that any one of the change orders was not warranted by changed conditions, changes in plans and specifications, additional requirements from inspectors or the state and federal historical preservation inspectors, or the needs of the tenants. The only individual change orders the Audit criticized were three in which the Auditor calculated the labor costs exceeded prevailing wages (the Audit failing to note that prevailing wages are the minimum that must be paid as standard wages and that acmal and union wages may exceed prevailing wages).

I. **There was sufficient contract oversight and administration by Agency/FOT over CCG and Turner contracts.** Change orders and payment requests in the constmction phase had substantial review requirements. Tumer prepared "Potential Change Orders", which often went through several revisions before they became final "Change Orders". The "Potential Change Orders" would be reviewed in weekly constmction meetings, which included Tumer, Architectural Dimensions, CCG (development staff and constmction experts), Redevelopment/FOT representatives (two architecture and renovation constmction experts) and Bank of America had a constmction monitor for their loan and equity funds. After the Change orders were negotiated and everyone agreed to the scope and cost, the minor change orders could be executed without Redevelopment/FOT approval but the major change orders required everyone's approval - Tumer, Architectural Dimensions, CCG and Redevelopment/FOT. In addition, Bank of America had a constmction manager at the constmction site who made weekly reports from the field, worked closely with the constmction management team and who reviewed change orders. Bank of America also approved any budget amendments required by increased constmction and soft costs with the monthly payment draws.

Payment requests followed the same procedures, preparation by Tumer, and review by Architectural Dimensions, CCG and Redevelopment, except that two FOT officers/board members were also required to review the requests before the were sent to Bank of America Constmction Lending for final review and release of funds held in the project account. These procedures seemed more than adequate for Bank of America

J. The contracts were clear on how CCG and the sub-consultants were to be paid. But CCG was allowed to receive funds to cover the costs and provide invoices, cancelled checks, bank statements and general ledger accounts after the payments. The audit in fact reviewed all of the payments, relying mostly on spreadsheets supplied by FOT and CCG, and only found $178,726 in unsupported expenditures. These were later found to be missing invoices from January 2007 that were later supplied to them, see K. below. The Agency and FOT's contract with CCG and CCG's contracts with its design sub-consultants was based on a monthly fee to CCG, which was adjusted in each phase based on the tasks required in the period, and reimbursement without markup for any of the sub-consultants. The typical compensation term in each contract or amendment with CCG read as follows: "Compensation and Method of Payment: Contractor will be paid for performance of the scope of services an amount based upon acmal costs but that will be "Capped" so as not to exceed $amount based upon the Scope of Service in Schedule A ..." The Scope of Service includes three exhibits: 1) Task List; 2) Schedule; and 3) Budget, with tasks and sub-consultants listed. Use of the phrase "based upon acmal costs but shall not exceed" does imply that costs/compensation could vary, depending upon what the acmal costs were, so long as there was a ceiling to the costs. The type of services and the costs for them would change during the contract and amendments and CCG was allowed to amend the sub-consultant budgets with FOT approval but changes to CCG's developer fee required a formal amendment of the contract. Understandably, this may have provided grounds for confusion, as CCG always requested payment for the maximum amount permitted under each contract. However, this was permitted per the stated compensation term in each contract.

K. The Agency and FOT effectively monitored contract expenditure levels. Staff prepared extensive spreadsheets of revenue and expenditures, with detailed sources and uses of funds that were tracked by the consultant based on monthly draws. Most of the discrepancies found in the audit were made from review of these documents. Staff was aware of several contracts, mostly architectural and engineering, going over their budget. For the construction phase it is typical to contract on a time and materials basis since it is difficult to determine the scope for unknown conditions. Most of the work in the constmction phase is responding to requests for information from the contractors or design modifications for unanticipated condition. The design contracts with the four firms - Architecmral Dimensions and Associates ("AD"), KPA Group ("KPA"), ELS and Starkweather Bondy Architecmre LLP ("SBA") – should have all become time and materials contracts in the final phase. CCG did prepare one contract, with ELS, that was open ended as related to time and materials and therefore the audit finding that this contract was over the not to exceed amount by $219,375 is inaccurate. The other contracts were not amended, but FOT and Agency staff was aware of the rising costs and even negotiated to reduce the fees due. In particular, the AD contract which was almost half of the increase, was negotiated as a direct payment from FTLL in installments - as part of constmction contract close out and the final equity payment. The payments were part of a settlement agreement approved by Fox Theater Manager's board and executed March 4, 2010. The agreement reduced the amount due by $68,175 and eliminated over $42,714 in requested interest for delays in payment. Finally, it should be noted that FOT never approved contract amendments with CCG, or its sub-consultants, until the funds were approved and available, which for the final project costs was after the $2.0 million loan from the Agency was approved on January 5, 2010.

L. **The $178,726 in expenditures to CCG are fully supported.** The audit stated that: "Unsupported costs of $178,726 were paid to CCG," and made the following recommendation: "We recommend that Agency management request supporting documentation from CCG for all unsupported costs and if documentation is not provided, these costs should be returned to Agency and FOT." The audit was correct in showing that there was $178,726 in unsupported costs between the December 18, 2006 spreadsheet of expenditures for Amendment 2, 3 and a portion of 4 (Fox Accounting Amendments 2-3-4 Dec-18-06.xls) and the January 19, 2010 spreadsheets of construction draws, which start with Amendment 4 (Fox Budget FINAL Jan-19-11.xls and FOX EXPENDITURES Jan-31-11.xls). But there were additional documents that had not been recorded in these spreadsheets. Review of the records during the audit found the missing costs were for a one-month period between the predevelopment and construction phases in January 2007. CCG presented documentation for $184,661.80 in expenditures for this period. This amount includes expenditures from interest that CCG earned on the Fox Project funds on deposit in a project account, which is why they were able to document payments that were greater than the amount of unsupported costs in the audit.

M. **CCG was reimbursed for work outside of the contract.** There are two issue related to the developer fee payments: 1) payments to CCG for periods not covered in the contract and amendments, but still justifiable; and 2) over-payments to CCG that might not be justifiable and should be recovered.

There is a period between completion of 90% construction documents, Amendment 2 of the CCG contract which ended March 31, 2006, and closing on the financing/start of construction, Amendment 3 of the CCG contract which began August 21, 2006. This was the period in which FOT and the various development entities were created and CCG contract was being transferred to this new entities. This was one of the busiest times for the development during which the construction work was being bid, the tax credit investor was being selected, the deal was being structured and the project was being approved by the Council. On August 8, 2006 at its first meeting the FOT board approved a $1,050,000 contract with CCG. But because of a limit in funds, Amendment 3 of the CCG contract was for only $900,000. Instead of covering the period from April 1 to November 30, 2006, Amendment 3 only covered October and November 2006. When the project received full funding and Amendment 4 was executed in December 2006, the 6-month period from April through September was not included but the fees for this period were paid out of the first Amendment 4 payment. The fees paid for this six month period was $142,500 ($23,750 per month the same as October and November in Amendment 3). Since CCG performed many services during this period and these fees seem reasonable, FOT should use the prior board approval to execute an additional amendment to CCG's contract to cover the missing period and increase the fee $142,500.

There seem to be two over payments as well - $27,143 and $9,200. During staff s review of documents during the audit it was determined that here were two payments for December 2006, one for $31,381 the monthly rate for Amendment 4, and one for $27,143. Amendment 4 was signed November 27, 2006, it should have covered December. It seems that $9,200 was paid to CCG over the course of Amendments 4 and 5. It is hard to determine why these payments were over by this amount since there were numerous monthly payments, but it seems to be an over payment. If the fees are increased by $142,500 and the $27,143 and $9,200 over payments are recovered or justified by CCG, the developer fees payments would be correct. Staff is in discussion with CCG about these over payments and has requested a repayment of $36,343.

N. FOT may be entitled to refunds for Turner's Guaranteed Maximum Price (GMP) contract. The Audit argues that Tumer received approximately $321,000 that should have been cost saving. Under the contract Tumer would be eligible to receive 30% of the saving, but not the full $320,977. FOT may therefore be due a refund of 70% of the cost savings or approximately $224,684. Staff has begun discussions with Tumer and CCG but further review of this issue is required. Tumer has argued that this was covered in the final settlement when Tumer cut the outstanding change order request substantially. Negotiations continue and if necessary CEDA may bring in an outside consultant to analyze the specific contracts and payment records.

O. The project followed proper Change Order pricing procedures. The Fox project's treatment of change orders was no different than in other constmction jobs. In any typical constmction contract, change orders additive change orders include profit, risk and overhead. Additionally, the costs for architect and engineering services increase because these services are needed to assist in evaluating change orders and preparing documentation. Further, Fox project management worked throughout the project to reduce constmction costs through negotiating change orders, rejecting many, value engineering, and deductive change orders.

The audit does not acknowledge that change orders are common in constmction projects. While the number of change orders and combined increase were large, 34% or $16,124,637 over the initial contracts of $47,793,563, this is typical of historic renovations. This is particularly tme for a building that was vacant for 35 years and when federal and state historic standards are required for the constmction. Many of the change orders were the result of meeting historic renovation standards or were requested by the tenants. Staff constantly negotiated change order requests to lower prices or refused them outright. Included in the final 28 change orders processed at the end of the project were nine ($533,682) that were rejected, 13 ($781,460) that were reduced an average of 35% and only six ($100,543) that were accepted as proposed. From initial proposed change orders to final approved change orders these 28 items were reduced from $1.4 million to $610,358 or 57%.

The Audit criticized change order labor pricing for three change orders for exceeding prevailing wage rates and states that labor rates should be priced at prevailing wage. However, prevailing wages are the minimum that must be paid as standard wages on a project where they are required by law and that actual or union wages and benefits may exceed prevailing wages.

P. The Project met the City's Administrative Instructions for conflict of interest as well as California State requirements on conflicts. At the outset we note that the Audit did not find any confiicts of interest in the Fox Project. Nonetheless, the Audit failed to discuss the conflict of interest provisions that were in place in the project, some of which exceeded standard City/Agency requirements. As with all City/Agency professional service contracts, there is standard language regarding conflict of interest, including prohibitions on donations to City elected officials. But FOT went further with the CCG contract by amending to the contract to include non-standard language regarding Government Code 1090. Further, in discussing staff conflicts the Audit failed to note that all City/Agency must annually file Political Reform Act public disclosures of their financial interests (Form 700) and comply with the City's two Administrative Instmctions ("AI") on conflict of interest – AI 21 and AI 595 Employee Conflicts of Interest / Incompatible Employment. During the course of this project, the City Attomey's Office acted as lead counsel for FOT and was in a position to analyze any potential conflicts of interest. Together, these steps represent more conflict safeguards than are typically present on City or Agency or private Agency funded development projects. But we are looking into the recommendation to see if it could be used to revise the City procedures to further reduce the potential for conflicts of interest.

AUDIT FINDINGS: CHAPTER 4 - The Financial Feasibility Analysis Performed By The Agency Was Inadequate For The Scope Of The Project Resulting In Under Estimating The Financial Needs Of The Project

Audit Recommendation #16 – Adopt policies and procedures to conduct a comprehensive financial feasibility analysis of the changes to a project's scope and adjust the relevant components/elements of the financial feasibility model. The financial feasibility model for projects should list, but not be limited to the following elements. Further, the model must be stmctured around project specific features.

- Project scope/description
- Organizational stmcture
- Resumes of principals
- Operators and/or developers
- Statement of sources and uses
- Project budget and financial projections
- Financial statements
- Site control and plan
- Building floor plan
- Appraisal/valuations "as-is", "as-completed", at "stabilize

- operation"
- Environmental assessment
- Financing commitments
- Equity requirement
- Tenant leases or letters of interest, and
- Job creation projections

Audit **Recommendation #17**- Consider hiring competent third party assistance with relative experience in the area of financial feasibility modeling and implementation to the extent that the Agency lacks the time, staff or competency.

RESPONSE - The **Project Was** Successful at **Raising** Outside Funds And the Feasibility Analysis **Provided** was Comprehensive

The Agency performed substantial financial feasibility analysis, both intemally and through two separate consultants, for the project. One of the consultants provided 37 page projections that included a development budget, operating budgets for several entities, loan schedules, tax projections and investor cash flows. This analysis was sufficient to obtain a $6.5 million constmction loan and $25.5 million in equity investment from Bank of America.

Q. The project prepared comprehensive **financial** feasibility analysis including: **1. Project** scope/description; 2. **Statement** of **sources** and uses; 3. **Project** budget and **financial projections**; **4.** Financial statements; and **5. Real** estate appraisal **or** valuation.

The audit found that "the financial feasibility analysis was inadequate for the scope of the project". In particular that: "there were shortcomings associated with the following five major elements: 1. Project scope/description; 2. Statement of sources and uses; 3. Project budget and financial projections; 4. Financial statements; and 5. Real estate appraisal or valuation." But this is inaccurate. The project scope was detailed as far back as 2001 in the Fox Theater Master Plan. A project budget or sources and uses was provided to the Council on several occasions and a much more detailed spreadsheet was prepared and updated monthly as part of the constmction draws starting in early 2007. A detailed analysis or projections used to meet the requirements of Bank of America and the CDEs were prepared several times in 2006 and again in 2009, although these long (37 page) and detailed projections were never shown to Council, they were available. Financial statements are prepared for all of the four entities but audit financials are not available for FOT because they are not needed and expensive--approximately $12,000 per year. These documents would only be useful if the Agency was planning to use FOT on another project. FOT is a single purpose entity and another entity would be created for any future project.

It is hard to determine from the audit what level of information was expected for these items, but much of the information was in fact presented. The question that should be asked is whether any additional information would have improved the Council's ability to make decisions; too much information might have the effect of burying the key information. Moreover, when the Council believes it needs additional information, it does not hesitate to request it. The project is described in the reports to Council, which included reduced graphics. In the section regarding the project scope/description the audit stated that "the "Ruins Concept" at $27.0 million (excluding land and predevelopment cost) ... was similar to the "Basic Concept" at $70.0 million described in an earlier 2001 Fox Master Plan. This is not true. In the 2001 Fox Master Plan, the "Basic Concept" was estimated at $43.7 million and the "Arts Center" concept was estimated at $69.0 million and the "Roadhouse" concept was estimated at $66.9 million. The final project combined elements of the "Arts Center" concept and the "Roadhouse" concept. The total cost of the project was amazingly close to the Hardy Holzman Pfeiffer report prepared in 2001. As stated earlier in this response, if the "Roadhouse" project concept was adjusted for inflation (see response to Chapter1) the total cost of the project would have been $83.4 million. This is close to the final cost of the theater if the already expended purchase price and improvements are eliminated - $85.0 million.

In the section regarding the statement of sources and uses the audit stated that "sources and uses statements (dated 12/14/04, 06/28/05, 06/27/06, and 07/18/06) omitted or failed to accurately reference land and predevelopment costs." While the sources and uses did exclude these costs, the sources and uses were only illustrating the cost to complete the project and more importantly the Fox Theater Master Plan also only considered the costs to complete the projects. But these reports also discussed the Agency's expendimres to date in other sections. More importantly, the audit did not consistently incorporate the same historic costs in the Funding Sources and Project Costs comparisons, which both understated the initial costs and inflated the growth in costs.

In the section regarding the project budget and financial projections the audit stated that "The Fox Theater Project's original plan did not project the effect of rising development costs on cash flow. Unabated, deviations in these elements may result in substantially unfavorable effects in other elements of the feasibility analysis. Specifically, when a commercial development is undertaken, the financial analysis should evaluate the operating assumptions for the project, the likelihood of reaching stabilization (rental income and other income in excess of operating costs and debt service and operating reserves) and the resultant net cash flow. The failure to realize these projected operating results will diminish the project's ability to sustain itself When there is an inability to produce a consistent net operating income (NOI), the project will be at risk of default on its financial obligations, and the sponsor/developer (Agency) must determine its capacity or desire to provide ongoing financial support to the project or repay any financial obligations of the project." While this is typical for a normal project, and would be tme of the Fox Project if the additional funds used to complete the project included conventional financing. But the one additional loan used to finance the project, a Local Initiatives Support Corporation/Bank of America New Markets Tax Credit enhanced loan where funds were set aside for all debt service payments from the loan principal. The project received $800,000 and $700,000 was set aside for all of the fees and interest payments. There was no additional risk assumed during the changes to the budget from 2006 to 2010. What is more, the tax credit stmcture included several "projections" which included income and expense analysis for the various entities. They were prepared in 2006 and again in 2009 for the Local Initiatives Support Corporation financing. These 38 page projections were very detailed and were required to confirm that the project would operate successfully.

In the section regarding the financial statements the audit stated "Development projects of this magnitude, with a non-profit sponsorship, should have audited financial statements. The Fox Theater Project has a layered organizational stmcture, which was required to facilitate attracting New Market Tax Credits and Historic Tax Credits financing. Each organization in the project has audited financial statements except FOT, Inc., which is the primary organization through which substantially all funds pass through. While FOT, Inc. financial statements were unaudited, this did not adversely affect the project's ability to be awarded tax credit contributions. However, should Agency desire to monetize or attract additional capital, it is likely that capital providers will place limited reliance on unaudited financial statements." This seems contradictory, FOT should be audited but not being audited did not adversely affect the project's ability to be awarded tax credit contributions. FOT was a pass through entity. Funds came in and went out. The only funds needed by the entity were for accountant fees for the tax remms, bank fees and a few small expenses. All of the other funds flow through to the entities which were audited, primarily Fox Theater Landlord LLC and Fox Theater Master Tenant LLC. Staff felt that auditing FOT would be an unnecessary expense that the Agency would have ultimately paid.

In the section regarding the real estate appraisal or valuation the audit stated " While the "as-is" appraisal commissioned by Agency valued the pre-development cost, an "as-completed" appraisal would have provided a value for the entire Fox Theater Project and provided a basis to evaluate the project cost to project value. A review of the estimated value at stabilized operations would provide Agency with the ability to assess its potential retum on investment and potential return of capital." The Agency did prepare a 33433 Report, including review of the project and DDA by an outside economic consultant (Keyser Marston Associates, Inc.) who prepared a fair reuse value or the Fox Theater, July 6, 2005. This type of report is required under redevelopment law to show that the project requires the proposed Agency financing/subsidy. Further, it should be noted that the value to the Agency or to the City, is not in the market value of the completed project, but rather in the value to the community in renovating an historic resources and in the catalytic economic effect of the renovated and operating Fox Theater to the surrounding community.

R. The Agency, FOT and CCG were successfully in obtaining $32.0 million in capital and debt from Bank Of America to fund the Fox Theater Project. The project successfully attracted Bank of America to invest and continue to increase its investment in the Fox Theater as the national economy declined and the value of the tax credits was reduced. Bank of America provided all of the debt ($6.5 million) and equity ($26.0 million) for the project and the govemance strucmre was set up to the bank's requirements. The initial equity offer from Bank of America was $15.0 million in June 2006, but by December 2010 this had grown 73%. CCG was instmmental in attracting Bank of America and negotiating the deal. Bank of America had worked with CCG on the Romnda Building and based on this experience invested in the Fox Project.

S. The Agency, FOT and CCG were successfully in creating a complicated governance structure to generate Historic and New Markets Tax Credit equity. Syndicating the tax credits required the Agency to create a non-profit corporation (FOT), a for profit corporation (Fox Theater Manager) and two limited liability companies (Fox Theater Landlord LLC and Fox Theater Master Tenant LLC). This strucmre required a team of attomeys, accountants and four community development entities ("CDEs") with New Markets Tax Credit allocations - Bank of America, National Trust for Historic Preservation, Charter School Development Corporation and Local Initiatives Support Corporation. CCG, FOT and the Agency have been able to manage the development and operations of this very complicated project.

CONCLUSIONS - The Project Has Been Instrumental in Downtown's Economic Revitalization.

We concur with the audit findings that the project was successful at raising altemative fimding, including private funds. An Agency owned theater would have save several million dollars at least, if only the legal, accounting and New Market Tax Credit fees. But the Agency would have needed to provide at least $20.0 million more in subsidies and still would have needed to seek $6.5 million in traditional debt for the project.

There is one final point to add, the Fox Theater was not developed as a stand alone project. The project was seen as both filling a major hole in the Uptown Area and as catalyst for other economic revitalization in the surrounding areas. The project took a mndown, decrepit blight and mmed it into a major asset. The area now has two beautifully restored theaters that are the heart of an emerging entertainment district. The Theater attracted over 160,000 paying customers its first year, over 180,000 its second year and is projected to reach 200,000 in this, its third year. This is almost double the initial projection of 100,000 paying customers per year for the first three years. These visitors have enlivened the whole area and created a demand for new bars, restaurants, cafes, and entertainment venues, which continue to open—all of which contribute to Oakland's economy and tax base. The project has been a major artistic and economic success. In addition, the Fox Theater has received numerous awards celebrating its historic restoration and has hosted special events and tours, see Exhibit B List of Awards and Special Events.

Since the lighting of the historic marquee in 2001, investors and businesses have been flocking to the Uptown with over twenty new restaurants and nighttime entertainment venues have opened in close proximity to the Fox. On any given night restaurants like Flora, Pecan, Ozumo, Plum, Hibiscus and the recently open Rudy's Can't Fail Café as well as bars and clubs like the Uptown, Somar, Era Art Bar and the Dogwood are crowded with patrons from the Fox and its nearby twin sister, the Paramount. On any given evening these two theaters attract as many as 6000 patrons to the Uptown area, providing a huge customer base for the nearby bars and restaurants and giving the street a sense of vitality and safety that has been missing for over forty years.

But the Fox Theater is much more than just a theater, it is also houses the Oakland School for the Arts a performing arts middle/high school. The Fox provides OSA with a new first class facility for almost 600 full- time smdents from all over the Eastbay. Many of these students are from disadvantaged families. With a college placement rate of over 95%, the Fox project is providing them with an opportunity to advance their education, attend college and become productive artists and members of the community. During the day, they populate the street and surrounding neighborhood with a message of education and learning.

From a purely economic standpoint, all of this has meant new sales tax revenue to the city, an increase in business license taxes, an increased property tax base and additional tax increment for fumre projects in the neighborhood. In addition, new jobs have been generated by the new restaurants and bars and over 150 people now find employment at the Fox Theater. But just as important as the jobs and increased revenues, the Fox has brought people back to a once unstable and unsafe neighborhood. It has changed this once blighted backwater of Oakland into the most important entertainment area in the Bay Area. It has brought new life to Oakland and provided hope for the students of the OSA.

EXHIBIT A

Chronology of Fox Theater Council Reports

7/18/2000	1. Authorization for a professional services contract with Hardy, Holzman Pfeiffer Associates for the Fox Theater Master Plan
4/24/2001	2. Reports and discussions of the Fox Theater Master Plan
10/14/2003 12/2/2003	3. Authorization for an Exclusive Negotiating Agreement with Fox Theater I Corporation (proposed entity combining Oakland School for the Arts and Paramount Theater) and a $432,500 professional services contract with CCG as fee developer
9/21/2004	4. Authorization to apply for, accept, and appropriate Proposition 40 grant funds ($5.0 million) for the historic renovation of the Fox Theater
12/21/2004	5. Report on the schematic design phase an authorization for a $746,000 amendment to the professional services agreement with CCG
6/28/2005 7/19/2005	6. Authorization for a DDA with Oakland Renaissance New Markets Tax Credits, Inc. including $22.5 million from the Agency
6/27/2006 7/18/2006	7. Authorization for a DDA with Fox Oakland Theater, Inc. ("FOT") including $32.0 million loan and $5.4 million in grants and other sources from the Agency
10/31/2006	8. Authorization for guarantees by Agency in favor of the lender and tax credit investment entities
12/15/2006	Closed on financing and started construction
2/13/2007	9. Authorization to apply for, accept, and appropriate Proposition 40 grant funds ($3.0 million) for the historic renovation of the Fox Theater
7/10/2007	10. Report on the City's local contracting and hiring goals for the Fox Theater
7/15/2008	11. Authorization for an amendment to the DDA with FOT including $7.5 million bridge loan and $7.0 million in grants and loans from the Agency
12/19/2008	Temporary Certificate of Occupancy issued
1/5/2009	Oakland School for the Arts begins classes
2/5/2009	Grand Opening Fox Theater
2/6/2009	GASS Entertainment starts operations with 1st concert
5/12/2009	12. Authorization for an amendment to one of the 7/15/2008 loans to authorize $1.3 million of the $2.7 million tenant improvement loan to be with Friends

	of Oakland Fox ("FOOF")
6/21/2009	Closed on additional New Markets Tax Credit enhanced loan through Local Initiatives Support Corporation
12/1/2009 12/15/2009 1/5/2010	13. Authorization for a $2.0 loan to FOT to complete the renovation of the Fox Theater
2/2/2010	14. Authorization to apply for, accept, and appropriate Proposition 40 grant funds ($1.0 million) for the historic renovation of the Fox Theater
10/1/2010	Signed Lease with Rudy's Can't Fail Cafe
6/1/2011	Rudy Can't Fail Cafe Grand Opening

	Denotes report dates for Community & Economic Development Committee and/or City Council/Agency Board Meetings

EXHIBIT B
List of Awards and Special Events

The Fox Theater has won a number of awards; hosted other special events; been the subject and site of tours and talks for over 125 groups including local non-profit groups, docents from the Pardee Home, seniors, city planners, and community; and hosted "free" community events for which the local non-profit organizations including OSA are not charged rent.

Awards

2009 Resolution California State Legislature, recognizing the "Grand Opening of the Fox Oakland Theater...it's unique status as one of the oldest and most important historic buildings in Califomia...helping generate both approval and funding for the current restoration project."

2009 National Preservation Award of the National Tmst for Historic Preservation

2009 Certificate of Recognition California State Legislature, In Honor of Dedication to the Sustainable Future of Your Community"

2009 Certificate of Recognition California State Legislature, "**2009** Green Heroes, In Honor of Collaboration on Green Jobs and a Green Economy for Oakland"

2009 Certificate of Recognition City of Oakland, "**2009** Green Heroes Award Winner, for dedication and commitment to making Oakland a model city"

2009 Secretary of Interior Conservation Award

2009 Platinum Award, Building Design and Construction, Reconstruction Award

2009 Award of Merit, Excellence in Structural Engineering, Structural Engineers Association of California

2010 California Redevelopment Association Award of Excellence, Mixed-Use Development

2010 Excellence in Engineering, National Council of Structural Engineers Associations

SPECIAL EVENTS

The City of Oakland has "free" access to the theater on 5 occasions per year. For these events the City pays no rent, but it has to pay for any set up, security, stage hands or other operating expenses directly related to the event. The event must meet four criteria:

1. Organization: The event must be sponsored by an eligible organization, which may include school districts, community organizations or non-profit organizations which are located in the City of Oakland and serving Alameda County and the Bay Area.
2. Purpose: The event must be of community, educational and cultural interests to the people of Oakland.

3. Accessibility: The event must be free to the general public or raise funds for causes that serve the community, educational and culmral interests of the people of Oakland.
4. Use of Space: The event must attract sufficient interest from the community to maximize the use of the auditorium.

In addition to the 2011 Mayor's Inauguration, City sponsored events at the Fox have included the following organizations: Intemational Council Of Shopping Center/Urban Land Instimte; Children Hospital Oakland; Oakland Chamber of Commerce; and Friends of Oakland Fox, which sponsored the grand opening gala. The Fox Theater was also highlighted in June 2009 at Uptown Unveiled! - A City of Oakland Culmral Arts & Marketing special event that attracted over 9,000 people to tour the theater one evening.

Oakland School for the Arts also has "free" access to the theater on 5 occasions per year. The school uses this access for graduation with artistic presentations, major school productions and fund raising events.

TOURS and FOX TALKS

Tours and Talks for over 125 groups have been made presenting the Fox to local non-profit groups, docents from the Pardee Home, seniors, city planners, and community. Some of these presentations include:

October 2009 National Trust for Historic Preservation; the Old U.S. Mint San Francisco, Participating Presenter with Architectural Dimensions

April 2009 City of Oakland Rotary Brown Bag Lunch Presentation

July 2009 Walking Tours Oakland Heritage Alliance

November 2009 Presentation, San Francisco City Hall Fellows Program

November 2009 Young Preservationists, Tour and Talk

February 2010 American Planning Association of Northem Califomia (Fox Talks with Architect Jim Heilbronner and Jeffrey Chew)

Oakland Tours Program with Annalee Allen

April 2010 History Channel Segment

May 2010 Tours for Oakland Unified School District Children learning about Oakland Historic Places.

October 2009 Uptown Masquerade Bash Benefit

December 2009 Volunteer support Oakland School for the Arts, 3 day Visual Arts Show

January 2010 Norton Buffalo Benefit Concert Sponsor

February 2010 Open House Tours for 1 Year re-opening Amiversary