Attachment 1 – Confidential Information

Additional Information Pertaining to the Review of the Redevelopment of the Sony Centre for the Performing Arts

Date:	June 4, 2014
To:	Board of Directors of the Hummingbird Centre for the Performing Arts (operating as the Sony Centre for the Performing Arts) and City Council
From:	Auditor General

CONFIDENTIAL INFORMATION

The following is a summary of issues that came to our attention which were outside the scope of the redevelopment of the Sony Centre. The majority of the matters that are identified in the report relate to events which occurred during the period pre-dating the appointment of the current Board in October 2011.

A. EXECUTIVE COMPENSATION FOR THE CHIEF EXECUTIVE OFFICER

From 2002 through 2008 the CEO was compensated as a consultant to the Sony Centre

(1) The Sony Centre's Chief Executive Officer (CEO) assumed his position in 2002. At that time, the CEO was compensated as a consultant through a company called Stage By Stage Holdings. This arrangement was approved by a previous Board even though it was clear that the CEO was an employee of the Sony Centre and not a consultant.

The Canada Revenue Agency deemed the CEO to be a direct employee of the Centre

In 2008, the Canada Revenue Agency reviewed the CEO's consultant status and determined that the CEO was an employee and not a consultant. As an employer, the Sony Centre became responsible for deducting Canada Pension Plan contributions, employment insurance premiums and income tax.

The Sony Centre, during the period from 2002 to 2008, failed to deduct the required Canada Pension Plan and employment insurance premiums and as a result might have been assessed interest and penalties for not doing so. It is our understanding that the Canada Revenue Agency, at that time, determined that it would not impose a penalty.

Similar arrangements have been the subject of Auditor General's reports in 2001

The contractual arrangement the Sony Centre Board entered into with Stage By Stage Holdings, though approved by the then Chair of the Board, was inappropriate.

This is also a concern raised by the Auditor General in a 2001 report on the use of consultants. At that time, it was recommended that all consultant agreements be reviewed in order to determine whether or not the City's contractual arrangements with consultants constituted an employee/employer relationship.

$572,000 in payments to Stage By Stage Holdings were considered a cost of developing the Sony Centre's business plan

(2) During our review of transactions related to the redevelopment, we noted that certain payments were made to "Stage By Stage Holdings" from 2005 through 2008 and were charged to the Sony Centre's business plan. It is our understanding that these payments, totaling $572,000, were an allocation of costs under the consulting agreement that were attributable to the development of the Sony Centre's business plan.

These payments related to the contractual agreement between the Sony Centre and Stage by Stage Holdings

Revised Paragraph

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B. TRANSACTIONS RELATING TO THE CHIEF EXECUTIVE OFFICER

(1) PAYMENTS TO THE CHIEF EXECUTIVE OFFICER

The CEO's wedding took place at the Centre in September 2010

In a 2010 year-end report to the Sony Centre's Finance Committee, PricewaterhouseCoopers (PwC) the Centre's external auditors indicated that:

> *"During the year, the Centre sold services to a senior employee for $15,153 (2009 – nil). Management has indicated that the services were valued at current market rates. This amount was included in receivables at the year-end (2009 – nil) and was paid in full in 2011."*

While the above disclosure from PwC does not indicate what the services were, the CEO's wedding took place at the Centre and the payment related to all expenses for the wedding. The wedding took place in September 2010.

The PricewaterhouseCoopers report further states that:

The Centre purchased the rights to publicize the CEO's wedding from Stage By Stage Holdings for $7,910

> *"In addition, the centre entered into a contract with a company owned by the same senior employee for the provision of promotion services. Management has indicated that the contract was valued at current market rates and an amount of $7,910 was paid to this company in the year."*

This amount relates to an agreement between Stage By Stage Holdings (SBSH) and the Sony Centre. In a communication to the then Chief Financial Officer, Mr. Brambilla indicated that:

> *"This will confirm that Dan and Nancy Brambilla have assigned to Stage By Stage Holdings (SBSH) their rights to publicity. In this regard, SBSH controls the right to publicize their wedding that took place at the Sony Centre (the Centre) on September 24th 2010.*
>
> *The Centre has expressed an interest in being able to publicize and otherwise exploit the wedding in an effort to promote the rental of the Centre to third parties for the purpose of having weddings booked at the Centre. In this regard, the Centre wishes to be able to use the names and images of Dan and Nancy at the wedding as well as the images of others attending the wedding (subject to the Centre receiving necessary releases from such parties).*
>
> *In addition, the Centre wishes to have Dan and Nancy be active participants in the selling of the Centre for this purpose, including without limitation having the right to ask them both to be available for interviews by third parties wishing to rent the Centre for weddings so that Dan and Nancy can assist the Centre in selling such third parties. This would include all details relating to the food and beverage service, furniture and flower arrangements and such other matters as potential renters may request.*
>
> *Therefore in consideration of the sum of $7,000, SBSH herby [sic] grants the Centre the right described above for a period of 10 years from the date hereof."*

The external auditor included general comments related to the transactions in their 2010 report on audit results presented to the Board's Finance Committee

While the $7,910 was paid to SBSH prior to December 31, 2010, the $15,153 remained outstanding at that time. PricewaterhouseCoopers confirmed that this amount was subsequently received in 2011.

Even though these transactions were generally communicated to the Finance Committee through the PwC report, there is no specific written Board approval for this arrangement. The communication by PwC was general and did not address the specifics of each transaction.

In terms of whether or not the $7,910 represented the current value of services provided, we are not able to determine if this in fact was the case.

The payment to Stage By Stage Holdings was authorized by the Centre's CFO

Further, it is unusual that the agreement and the direction to pay SBSH the $7,910 would be communicated to the Chief Financial Officer (CFO), an individual who reported directly to the CEO. An arrangement which benefited the CEO should have been communicated to and approved by the Board.

In essence, this particular transaction raises the following concerns:

- It could be argued that the services paid for should have been a part of the CEO's day-to-day responsibilities.
- The CFO should not have been put in the position of having to authorize the payment of $7,910 to the CEO or to a company owned by the CEO. The payment should not have been made without Board approval.
- In terms of good business practice, the payment once approved should not have been made until the receivable owing by the CEO of $15,153 had been paid.

(2) EXPENSE REIMBURSEMENTS

The CEO was reimbursed in error for expenditures which had been paid for directly by the Sony Centre

During our review of transactions related to the redevelopment, we identified expenses, such as the purchase of lighting and furniture, incurred by the CEO on behalf of the Sony Centre. One reimbursement to the CEO was made for a $4,050 deposit on lighting fixtures which had not in fact been paid for by the CEO but by the Sony Centre directly. This transaction occurred over three years ago. After we identified the error, this amount was repaid by the CEO along with three years interest to the Sony Centre.

Additional procedures were performed to verify whether any other errors may have occurred in the reimbursement of expenses incurred by the CEO directly or through Stage By Stage Holdings.

Other transactions may warrant further consideration by the Board

While no additional errors were identified, other transactions were noted that were not materially significant to the operations of the Sony Centre.

Expenses for business trips where the CEO was accompanied by his spouse

- The Sony Centre reimbursed the CEO for expenses incurred on two separate business trips where he was accompanied by his spouse. These reimbursements include an estimated $1,250 for airfare and event tickets for the CEO’s spouse.

Reimbursements of tickets to political fundraising events

- The Sony Centre reimbursed the CEO for tickets to various political fundraising events during the period from December 2007 to January 2011. These amounts were as follows:
    - $2,500 for the Mayoral Harmony Dinner in 2011
    - $600 for a fundraiser for Bob Rae in 2010
    - $500 for an “Evening with David Caplan” in 2008
    - $350 for a “Spring Fling” fundraiser for George Smitherman in 2008
    - $350 for a fundraiser for Peter Fonseca in 2008
    - $350 for a “Back to Work” fundraiser for George Smitherman in 2007

Management advises that from 2003 up until City Council's October 2008 decision not to proceed with the CityCentre cultural project, such expenditures were incurred to solicit support for federal and provincial funding for the redevelopment from both elected and unelected officials. Two of the events identified occurred after fundraising efforts ceased.

The appropriateness of using taxpayer money to fund certain political parties is questionable even though the amounts are not significant. In all but one case, the expenses were approved by the then Chair of the Board.

In any event, these expenditures should have been paid directly by the Centre and not as an employee reimbursement.

Meals and entertainment expenses

- The Sony Centre reimbursed the CEO for various meals and entertainment expenses including:

  - $890 for a staff holiday lunch with seven employees in December 2009, where 38 per cent of the pre-tax bill was for alcoholic beverages.

  - Multiple reimbursements for 50 per cent of the cost of meals purchased from the on-site cafeteria operated by the Sony Centre's food services provider. For example, a reimbursement of $225 was made for 50 per cent of meals purchased during the period from November 15, 2010 and December 2, 2010.

  Based on the limited documentation attached to expense reimbursement submissions, we were unable to validate the business rationale for such expenses.

A complete audit of employee expenses and reimbursements, including those of the Chief Executive Officer, was not conducted.

C. COST OF FUNDRAISING AND SPONSORSHIPS

Cost of the redevelopment included $15,000 in fees for assistance with sponsorship arrangement

During our review of transactions related to the redevelopment, we identified the negotiation of an in-kind capital sponsorship arrangement which coincided with the purchase of goods and services. An independent contractor provided assistance with the sponsorship arrangement for a one-time fee of $15,000 (approximately 10 per cent of the value of goods received through the sponsorship) which was included in the cost of the redevelopment.

The same independent contractor was engaged throughout the redevelopment on a retainer basis with an entitlement to commissions on net sponsorship and house program advertising revenues generated. This arrangement has since been extended to include donations from corporate sponsorship and seat dedications as well as major underwriting gifts and sponsors for specific programming.

An independent contractor was paid $532,000 for sponsorship services

Between 2008 and 2012, the independent contractor was paid approximately $532,000. In each of 2010, 2011, and 2012, the fee, including commissions paid, was approximately 35 per cent of commissionable revenues (on a weighted average basis).

Commission rate is high when benchmarked to other municipalities

This rate is at the very high end for the industry, where commissions typically can range anywhere from 10-35 per cent. As a benchmark, in 2009, the City of Markham, considered a proposed commission fee structure for a non-exclusive arrangement of 15 per cent commission on cash and in-kind sponsorships valued at up to $999,999. A 2013 study commissioned by the City of Kitchener indicated the most common commission rates were 10 per cent and 20 per cent.

In addition, we consulted with staff of the City's Economic Development and Culture Division who confirmed that 20 per cent commissions are an average and that 35 per cent is a high commission.

Management is of the view that the fee, including commission paid, is reasonable.

D. ADDITIONAL INFORMATION REQUESTED BY AUDIT COMMITTEE

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CONCLUSION

As requested by the Board of Directors of the Sony Centre and by the City's Audit Committee, this report presents the issues that came to our attention which were outside the scope of our original review of the redevelopment of the Sony Centre for the Performing Arts.