

**COUNTY OF MILWAUKEE
INTEROFFICE COMMUNICATION**

DATE: May 24, 2013

TO: Supervisor Marina Dimitrijevic, Chairwoman, County Board of Supervisors

FROM: Scott B. Manske, Comptroller
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SUBJECT: Milwaukee Public Museum Lease and Management Agreement

REPORT OVERVIEW

At its January 31, 2013 meeting, the Committee on Finance, Personnel and Audit was briefed on the potential cash flow issues being faced by Milwaukee Public Museum (MPM) should it be required to make the required pension payment due in September of 2013 and were briefed on the discussions occurring between MPM and Milwaukee County staff regarding options to deal with the short-term cash flow issues and long-term sustainability of MPM.

Subsequently, at its May 16, 2013 meeting, an informational update of the current proposals to help ensure the financial success of MPM was provided by a Workgroup, made up of members from Comptroller and representatives from the County Board, Corporation Counsel and the Department of Administrative Services, with the understanding that specific recommendations would be presented by the Workgroup to the Committee in June. This report outlines those recommendations.

HISTORICAL BACKGROUND

In March of 1992, Milwaukee County entered into a lease and management agreement with the MPM under which MPM assumed the primary responsibility for management and operation of the Museum. The original term of the lease was from March 31, 1992 until March 31, 1997 with nine successive renewal periods of five years subject to termination clauses. The base level of County operating support for MPM was \$4.3 million per year in the original lease. The current lease agreement period expires on December 31, 2017 with four additional terms of five years and one of two years that stretches the agreement through 2039. The current County funding commitment is \$3.5 million annually through 2017.

MPM Pension Plan for Former County Employees

In addition to the lease agreement, an agreement as to employees was also executed on March 31, 1992. In 1992, the museum was a department of Milwaukee County, and the employees of the museum were County employees covered by Milwaukee County labor contracts and benefits. That agreement with MPM allowed for affected employees to be offered positions by the MPM in connection with the execution of the lease. Any employee who accepted a position became an employee of MPM. Upon becoming MPM employees, they were no longer members of the Employees Retirement System (ERS) and began to participate in the MPM sponsored pension plan that was created in 1992. The MPM pension plan was to mirror the County ERS benefits that existed at the date of transition in 1992. However, the pension costs of MPM differed, depending if the employee was vested in the County ERS plan, or not.

- For vested Milwaukee County employees, who transferred to MPM at the transition date, the County was responsible for the pension liability for all service credit earned while at the County. MPM became responsible for all future service credit pension costs for these vested transfer employees, while at MPM.
- For non-vested Milwaukee County employees, who transferred to MPM, MPM was responsible for pension costs for all service credit earned both at the County and all future service credit earned at MPM.

Only former Milwaukee County employees are in MPM plan under discussion in this report. Employees who subsequently joined MPM are not members of the MPM pension plan that exists solely for former County employees.

There were approximately 53 individuals who transferred from County employment and ERS membership to MPM employment and the MPM plan in 1992. Of those 53, 11 are still active employees of MPM. The actuary report requires MPM to make a pension payment of \$640,523 by September 2013. The 2010, 2011 and 2012 required pension payments were \$402,463, \$399,092, and \$667,325, respectively. MPM has successfully made the prior annual pension payments, but has not yet made the 2013 required contribution which is due in the fall.

The MPM pension plan is subject to IRS rules for funding purposes which require a lower rate of return assumption than the County ERS plan. The County ERS plan currently uses a rate of return of 8.0%. The MPM pension plan for former County employees requires a rate of return of 6.2%, which will drop to 5.0% in the next two years. The lower interest rates will require higher pension contributions from MPM, which will put a strain on maintaining a positive bottom line.

The County requested MPM to engage their actuary to provide estimates of future pension contributions, and unfunded liability based on these changes in discount rates. In addition, the MPM pension actuary determined the cost to fully fund the MPM pension plan for former County employees, so as to eliminate future MPM contributions to the plan.

2004 MPM loss and recovery

In May 2005 it was reported that MPM would end the 2004 fiscal year with a deficit of approximately \$4.1 million and was facing another large shortfall for 2005. A Workgroup was formed that eventually led to a financial recovery plan for MPM that included private donation pledges, a working capital loan of up to \$6 million guaranteed by the County, capital infrastructure and annual operating support guarantees and a favorable restructuring of existing debt by the banks holding the loans. Since that time, MPM has successfully repaid the working capital loan without requiring the County guarantee to be called, significantly reduced its outstanding long-term debt through bank write-offs and repayments, invigorated its capital donor campaigns and has reduced its expenses to better match annual revenues.

2012 Financial Results, and Current Financial Issues

Despite these positive steps, MPM still has financial difficulties that threaten its existence as a viable ongoing entity. The audited financial statements as of August 31, 2012 showed a \$3.5 million total loss. The loss included a \$2.7 million non-cash increase in long term pension and health care benefits for former County employees, who transitioned to the Museum in 1992. Current regulations require MPM to report these liabilities, but do not require a cash contribution. The remaining loss was due to the attendance for the Cleopatra exhibit being well below expectations. These revelations were shared with the County and the Workgroup was formed to develop recommendations to help ensure MPM's viability as a regional cultural destination that is supported by visitors and public and private donations. From these meetings, MPM delineated a list of financial issues that it would face in the coming year that it had to resolve to remain viable. This list included funding for the MPM pension plan for former county employees.

MEETINGS ON A SOLUTION

The Workgroup recommended and the Committee on Finance, Personnel and Audit approved a \$100,000 appropriation transfer from the Appropriation for Contingencies (Org. Unit 1945) to provide for actuarial and legal analysis, as needed, of any possible agreement with MPM at its March 14, 2013 meeting. As of this report, no funds have been expended for this purpose and are likely not to be expended.

At the April 16, 2013, meeting of the Committee on Parks, Energy and Environment, members from MPM testified that senior managers at MPM have agreed to take furlough hours in 2013 to assist MPM in meeting its bottom line for 2013. MPM has indicated that additional reductions to operating expenses may be necessary to ensure the sustainability of the museum for this and future years.

The Workgroup attended numerous meetings with MPM and reviewed a variety of options. The conclusion of the Workgroup was that the best solution is to request the County Board to authorize a payment to fund the remaining unfunded liability of the

MPM pension plan that was held exclusively for the former Milwaukee County employees who remain in the MPM pension system. As of January 1, 2013, the assets of the plan are \$5.75 million. A contribution of approximately \$3.0 million from the County in September of 2013 with an investment return of 7% would provide the plan with \$9.0 million in assets by the end of 2014 which should eliminate the need for payments to the pension plan provided it maintains its investment return.

The Workgroup recommends that the additional funding to MPM be provided from the debt service reserve which has an available cash balance of \$18 million.

There are a number of benefits to MPM from the elimination of the unfunded pension liability. First, the required payment of \$640,000, due in September, is included in the payment by Milwaukee County of the unfunded liability and therefore would not have to be paid by MPM. Second, MPM currently pays about \$40,000 for pension insurance annually and that amount is projected to drop by approximately \$10,000 after the proposed lump sum payment is made. The additional funding will eliminate future year pension funding requirements, freeing up operating cash flow for MPM.

MPM BUILDING AND CAPITAL IMPROVEMENTS PROJECT ISSUES

The building and artifact collections of MPM continue to be the property of Milwaukee County. MPM estimates of the deferred building maintenance costs are approximately \$30 million. As a part of the discussions, transfer of ownership of the building was raised as MPM seeks to fundraise for elimination of existing debt of \$4.5 million and to finance future building needs. MPM management suggests that there would be increased fundraising ability by MPM should it have full ownership of the building. However, MPM is not currently in a financial position to assume the maintenance and up keep of the building as it stands. MPM is seeking additional capital improvement funds from Milwaukee County in order to have the building in a condition in which it could be transferred to the MPM without significant outstanding deferred maintenance needs that would add to the fiscal burden of MPM.

The Workgroup recommends a future commitment of up to \$4 million in capital improvement funds during 2014-2017 from Milwaukee County, from within Milwaukee County's bonding cap, for the MPM facility with the objective to begin discussions regarding the transfer of the building in 2017 if certain conditions spelled out in the revised Lease and Management Agreement are met and policymakers approve.

LEASE AND MANAGEMENT AGREEMENT REQUESTED CHANGES

In addition, discussions on several revisions proposed to the Lease and Management Agreement by MPM have occurred. A number of the revisions relate to the item discussed above but MPM is requesting additional changes be included in a new agreement.

The following is a summary of the recommended terms of agreement. Additionally, attached to this memo is a Comparative Chart outlining changes in the current Lease and

Management Agreement, and a final recommended version of the new Lease and Management Agreement, with Exhibits to follow.

SUMMARY OF RECOMMENDED TERMS OF AGREEMENT

1. Milwaukee County will provide a total of \$3,000,000 in funding to the defined benefit plan assets of the MPM Pension Plan for Former Milwaukee County Employees prior to August 31, 2013. Included in the \$3,000,000 amount paid by the County is the payment of \$640,523 which is due by September 15, 2013 for the 2012 plan year.

Importantly, this payment is contingent on MPM securing at least \$3,000,000 in donor commitments toward the elimination of MPM's existing total bank debt of approximately \$4,500,000.

2. The current Lease and Management Agreement provides for a commitment of \$3,500,000 for annual support to MPM through 2017. The new agreement will extend the commitment for annual support funding to MPM through 2022 as noted below:
 - a. Calendar Year 2014 – 2017: \$3,500,000 (Current Commitment)
 - b. Calendar Year 2018 – 2019: \$3,350,000
 - c. Calendar Year 2020 – 2021: \$3,200,000
 - d. Calendar Year 2022: \$3,000,000

If MPM has received at least \$5 Million in cash and donor commitments for capital spending related to the facility by June 30, 2017, annual funding for operations will increase to \$3,500,000 each year from 2018 through 2022.

3. The new agreement makes the annual funding commitment by the County contingent on MPM meeting or exceeding certain operating and financial goals:
 - a. MPM obtaining donor commitments for any remaining MPM existing bank debt of approximately \$1,500,000 by December 31, 2015.
 - b. Annual attendance of MPM, its theater/planetarium and special exhibits, events and programs exceeds 400,000.
 - c. Museum generates positive unrestricted operating earnings as defined by the change in unrestricted net income plus depreciation is greater than zero.
 - d. Total MPM Endowment net assets are a minimum of \$5,000,000 with a minimum of \$2,000,000 in unrestricted net assets.
 - e. MPM's Total Net Assets continue to exceed the value as of fiscal yearend 2013 audited results excluding gains associated with pension contribution and gift commitments for debt elimination.

4. To the extent that MPM does not meet certain operating and financial goals outlined in #3 above, Milwaukee County may reduce subsequent annual support funding to MPM by \$250,000 for remaining years 2014 – 2022.
5. MPM retiree medical obligations for former Milwaukee County employees will remain the responsibility of the museum.
6. Milwaukee County will provide up to \$4,000,000 from 2014-2017 in capital project funding, from within Milwaukee County's bonding cap, to address structural repairs to the museum facility.
7. If MPM has received at least \$4 Million in cash and donor commitments of the \$5 Million referenced in #2 above for capital spending related to the facility by June 30, 2017, and the County and MPM agree to enter into good faith negotiations to transfer the facility and land and to create a new agreement consistent with such a transfer. Subject to applicable law and to the extent permissible under law, Milwaukee County will make a dollar-for-dollar commitment up to an additional \$4,000,000 for capital project funding between 2018 and 2022 provided the museum facility and land is transferred to MPM by December 31, 2017.
8. Any new debt, except for working capital, collateralized debt by donor pledges or personal assets, is subject to approval by the County Executive or designee.

RECOMMENDATION

The Workgroup, made up of members from the Comptroller's Office, the Board of Supervisors, Corporation Counsel and Department of Administrative Services, respectfully requests authorization to execute an agreement with MPM based on the Recommended Terms of Agreement, the proposed Lease and Management Agreement and approval by the MPM Board of Directors.

Attachments:

Resolution

Fiscal Note

Comparative Chart of Current and Proposed LMA

Proposed Lease and Management Agreement

cc: Chris Abele, County Executive
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