PENINSULA LIBRARY SYSTEM

ANALYSIS OF OPTIONS FOR THE ORGANIZATIONAL STRUCTURE OF PENINSULA LIBRARY SYSTEM, PACIFIC LIBRARY PARTNERSHIP AND CALIFA; OPTIONS FOR BUILDING OWNERSHIP AND MORTGAGE

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ANALYSIS OF OPTIONS FOR THE ORGANIZATIONAL STRUCTURE OF THE PENINSULA LIBRARY SYSTYEM, PACIFIC LIBRARY PARTNERSHIP AND CALIFA; OPTIONS FOR BUILDING OWNERSHIP AND MORTGAGE

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EXECUTIVE SUMMARY/KEY RECOMMENDATIONS

The Peninsula Library System authorized this Report to evaluate staffing, revenue allocation and office building mortgage and ownership options among the three member-based entities, Peninsula Library System (PLS), Pacific Library Partnership (PLP) and Califa Library Group (Califa). Municipal Resource Group LLC (MRG) has evaluated the data and findings in the Report in the overall context of the current and future capacities of the three organizations to deliver effective and efficient membership services. The global focus of the Report is to enable the three entities to:

- Position themselves for the future
- Meet the funding challenges that are currently arising, and will continue to do so in the future
- Respond to and take advantage of opportunities that may arise in the future to improve services and service areas

1. Organizational Structure

Under the current organizational structure, PLS is the operating entity and provides services to PLP, Califa and NorthNet. Services include administration, operation, accounting, technology and delivery services, along with the rental of space.

Key Recommendations

The three separate PLS, PLP and Califa organizations should be retained.

Califa

1.1 Califa should become an independent operating entity, with a full time Executive Director and its own staff for operations; Califa should issue an RFP for administrative and support services and include PLS/PLP in this process; if PLS/PLP is not the provider of administrative and support services Califa should consider whether to continue to rent space from PLS.

1.2 Califa should explore avenues for purchasing cost effective benefits for its employees.

1.3 Califa should pay pro-rated rent for any space needs for shared positions (assuming a contract with PLS/PLP for administrative and support services), as well as full rent for Califa positions.

PLP

1.4 PLP should become the operational entity, the “parent” or “umbrella” organization, for the delivery of services to consolidated regional and legacy cooperative library systems, as well as local system services and contract services, with a full time Executive Director and staff.

1.5 Current PLS staff should be transitioned to become PLP staff.

1.6 PLP should employ a full time Executive Director.
1.7 PLS should continue hold title to the property and rent space to PLP and Califa.
1.8 PLP should review the current cost allocation structure and membership fee structure, based on the implementation of the new organizational model.
1.9 Depending upon the transition processes and results, the PLP membership fee structure may need to be reviewed.
1.10 PLAN services should be managed by PLP.
1.11 The PLP Joint Powers Agreement would need to be amended to provide that PLP, rather than PLS, would serve as Treasurer/Controller and fiscal agent for PLP.
1.12 The Califa transition should take place first, followed by the PLS/PLP transition.

PLS

1.13 Assuming the Califa and PLS/PLP transitions, PLP should, in the interim:
  - Clarify and implement new contract costs for PLS staff provided to PLP and Califa.
  - Increase PLS fees as needed.
  - Clarify and implement additional PLAN costs to be charged to PLAN members.
  - Identify new potential revenue sources.

Budget Recommendations

1.14 Budget documents for all three organizations should be revised to include the following:
  - Staff components, both permanent and contract
  - Summary of funds flowing out and into each entity
  - Program budgets, including revenues, expenditures and use of fund balance/reserves
  - Fund balance detail, including multi-year trends
  - Budget narratives, including purposes, services and projects
  - Overall review of financial condition, trends, risks, etc.
  - Each budget should be presented in a similar format.

1.15 Califa should not use its previously accumulated capital to balance its annual operating expenses.
1.16 PLP and Califa boards should each adopt a fund balance reserve policy and adopt a specific target fund balance equal to an amount between 25% and 30% of its annual operating expenditure budget.

2. Allocation of Costs

PLS has historically used an estimated allocation system to allocate portions of staff costs to all three organizations. Starting in 2015, staff has begun to track actual time spent for each entity, including unallocated multi-system time.

Key Recommendations

2.1 All administrative staff should track their time by contract/entity and future budgets and contracts should be based on time spent on work related to each entity.

2.2 All entities should obtain an outside cost allocation plan in the future to accurately allocate and charge costs for services among the organizations.

3. Membership / Fiscal Agency Fees

With PLS as the current operating entity, it recovers significant funds from other agencies, including Califa, PLP, NorthNet (NLS) and other services and programs. PLS allocates PLAN membership costs based on an agreed upon fee structure. PLP currently allocates its membership fees on a tiered basis, based on the size of each member's budget. Califa currently allocates its member fees based on the number of employees.

Key Recommendations

3.1 Membership fees should remain as structured; if membership fees are not fully covering costs, and other revenue enhancement options are not productive, then membership fees should be increased.

4. Building Ownership and Mortgage

PLS currently holds title to the property and the building that houses the administrative offices of PLS, PLP and Califa. PLS currently has a loan of $2,250,000 on the property. PLS has been making principal prepayments over the past several years, in addition to the regular monthly principal and interest payments. As of September 15, 2015, PLS owed $1,740,694.17 in principal on the mortgage.

Key Recommendations

4.1 PLS should continue to hold title to the real estate.

4.2 PLS should prepay principal to the maximum extent possible as soon as possible, while avoiding the prepayment penalty and while maintaining a target fund balance recommended at $900,000.

4.3 PLS should again explore refinancing the existing loan in February 2019, once the prepayment penalty no longer applies. The variable rate mortgage and the balloon payment terms should be renegotiated, if possible.

4.4 In the event that PLS does not renegotiate or refinance the loan in February 2019, it should develop a funding strategy and mechanism to pay the balloon payment due in 2027.

4.5 The contract between Califa and PLS should be restructured to clearly describe the amount of rent being paid by Califa to PLS.

4.6 PLS should obtain a current appraisal of the real estate so that it is aware of the property value and the PLS equity in the property.

I. INTRODUCTION, PURPOSE AND METHODOLOGY

Introduction

The Peninsula Library System engaged Municipal Resource Group LLC (MRG) to evaluate staffing, revenue allocation and office building and ownership options. In the course of conducting the evaluation, MRG felt it was also important to analyze the organizational structure, data and recommendations in the context of the current and future capacities of the three organizations – Peninsula Library System (PLS), Pacific Library Partnership (PLP) and Califa Library Group (Califa) – to deliver effective and efficient membership services. The global focus of the Report is to enable the three entities to:

- Position themselves for the future
- Meet the funding challenges that are currently arising, and will continue to confront the organizations in the future
- Respond and take advantage of opportunities that may arise in the future to improve services and service areas

The missions of the three organizations are distinctly different. PLS is a legacy cooperative library system focused on locally provided services to libraries in San Mateo County. PLP is a consolidated regional cooperative library system, focused on managing and providing services to legacy and regional cooperative library systems throughout Northern California. Califa is service bureau focused on providing member-enhanced, value-added statewide services to California libraries. The current organizational structure is the result of an operational model established some time ago, and it may not be the best fit going forward. It is important to align the future organizational models with the individual strategic directions of each organization, as well as with each organization's unique geographic responsibilities, services and representation.

Throughout this Report, the future drivers of change that the organizations are currently facing and will be facing have been identified, such as the uncertainty of State funding for statewide services. These "change drivers" have been integrated into the discussions and recommendations in this Report.

In developing an overview for the Report, the consultants took a step back to look at organizational options, as if the current structure did not exist and the three organizations were being developed today. Under the current organizational model with PLS as the operating entity, services have been successfully provided to all three organizations, primarily due to the innovative and demonstrated commitment of staff. However, if all three organizations were being developed today, it is highly unlikely that the current organizational structure would be the one chosen. This Report outlines a recommended new organizational structure for all three organizations, to fit current and future challenges and services.

Purpose and Methodology

The Peninsula Library System authorized this Report to evaluate staffing, revenue allocation and office building mortgage and ownership options among the three member-based entities, PLS, PLP and Califa. The purposes of the project are to (1) identify alternatives to the current practice of PLS employing all staff, and evaluate potential impacts and effectiveness of alternate arrangements; (2) identify alternative recipients of grant revenues, including transferring the federal Library Services and Technology Act (LSTA) grant (Infopeople) from PLS to Califa, and evaluate the potential impact on fiscal agency fees and on the member entities' financial support; and (3) research alternatives to the current ownership of the PLS office building, as well as options for repayment of the existing mortgage, and evaluate the financial impact of each alternative on member entities.

The evaluation methodology included eight basic tasks:

1) Evaluate the effectiveness of the existing organizational structure, staffing model, responsibilities, processes, practices, roles, resources and other factors in meeting the service requirements of PLS, PLP and Califa.

2) Identify the advantages and disadvantages of Califa hiring its own staff and, if Califa were to do so, whether it would still contract with PLS for accounting, technology and other support services, and how Califa employees would receive health, retirement and other benefits.

3) Assess the current accounting practices and procedures related to the allocation of costs and evaluate effective alternatives that can meet PLS, PLP and Califa goals while minimizing work effort and complexities.

4) Identify options for organizational structures, responsibilities, processes, practices, roles, resources and reporting relationships necessary to meet PLS, PLP and Califa requirements and expectations.

5) Evaluate how shifting of grant funding from PLS to Califa will impact the revenue base of PLS and PLP.

6) Identify options for allocating fiscal agency fees, including member revenue and cost recovery revenue, to provide for transparency and to support the financial health of PLS, PLP and Califa.

7) Identify options, along with related benefits and challenges, for building ownership – should real estate continue to be owned by PLS or should title be shared with, and be partially purchased by PLP and/or Califa?

8) Identify options, along with advantages and disadvantages, for accelerated mortgage payments on the existing loan vs. other uses or investments with the same funds vs. refinancing the mortgage.

The assessment included interviews with PLS, PLP and Califa board members, staff and contractors, as listed in Exhibit A. It also included a review of key PLS, PLP and Califa documents to assist in understanding and evaluating the entities' organizational structures, member financial obligations, legal commitments, real estate ownership, loan obligations, debt management, investment and cash management strategies, grant requirements and financial condition. Industry standards and best management practices were drawn from the authors' experience with library services and municipal finance departments, and a variety of professional sources, including publications of the Government Finance Officers Association and California Society of Municipal Finance Officers (CSMFO).

It is important to note that an evaluation of current practices tends to focus on areas that can be improved rather than on existing areas of strength and success. The research revealed that many of the current practices are well designed and effective. However, this Report focuses on areas where the member organizations may enhance effectiveness.

It is also important to note areas that are not the subject of this evaluation and Report. It was not intended that this Report be an evaluation of the performance of individual PLS staff members. It was also not intended that this Report would evaluate external customer requirements, although the recommendations in the Report are designed and expected to enhance member services.

II. PLS, PLP AND CALIFA BACKGROUND INFORMATION

PLS Background

PLS was formed in 1972 as a joint powers agency (JPA) by the cities of Burlingame, Daly City, Menlo Park, Redwood City, San Mateo, San Bruno and South San Francisco, the San Mateo Community College System and San Mateo County. PLS was a cooperative library system, established under the authority of the California Library Services Act (CLSA) but no longer functions in that capacity. The primary focus for PLS is a shared integrated library system called Peninsula Libraries Automated Network (PLAN). PLS is governed by an Administrative Council consisting of representatives from each member agency. PLS contracts with, and provides administrative services to CLSA systems NorthNet and PLP, and Califa.

PLP Background

PLP was established as a JPA in 2009, comprised of PLS, the Bay Area Library and Information System JPA (BALIS), Monterey Bay Area Cooperative Library System JPA (MOBAC) and Silicon Valley Library System JPA (SVLS).

This consolidated regional system serves the information needs of people in the larger Bay Area community. Its purposes are to 1) improve the services of its constituent member libraries by maintaining prior CLSA programs and leading research and development efforts to ensure libraries are aware of and respond to demographic, economic and other changes, 2) experiment with innovative approaches to programming and services, and 3) enhance collective resources.

PLP provides services through funding received from CSLA and fees paid by members. PLP is governed by an Administrative Council comprised of all library directors of the agencies within PLP. Nothing in the consolidated JPA prevents a member-legacy system from continuing local best practices to meet its own needs, including its own committee structure.

Goals/Benefits of PLP:

- Achieve economies of scale by investing in a set of shared resources in programs and services that will benefit people served by the communities in the four legacy systems
- Reduce duplication of effort and investment of resources in redundant activities and programs
- Facilitate the ability of member libraries to work together to increase the quantity and quality of the services and programs for the people in the broader geographic area
- Enable each member to be more responsive to the changing needs and expectations of its community
- Allow member libraries to have a stronger, more effective and unified voice

- Capitalize on the talents and competencies of a larger group of member library staff and increase the opportunity to share and learn from each other
- Collaborate to invest in research and development of new initiatives and pool resources to support development of these initiatives
- Invest in common infrastructure
- Extend the network and communities of practices among the people who work in the member libraries
- Provide the structure and support for member libraries with common interests to communicate and share in a broader geographical arena.

Califa Background

Califa is a statewide membership-based service bureau formed in 2004 as a 501(c)(3) non-profit organization. There are approximately 220 Califa members. Califa was designed to provide member-enhanced, value-added services to all California libraries. On behalf of its members, Califa brokers and facilitates the delivery of products and services for those libraries. Califa sponsors state-wide projects, receives substantially all of its funding from California and federal grants, and receives membership fees from its member libraries. At least 16 grants totaling more than $5 million have been awarded to Califa and have been (or will be) included in the current budget. The largest grants relate to the Infopeople program and to the CENIC Broadband project. Califa is at the forefront of cutting edge innovation for libraries throughout California and is positioned to continue to do so in the future. Califa is governed by a Board of Directors.

III. EVALUATION REPORT AND RECOMMENDATIONS

1. RECOMMENDATIONS CONCERNING ORGANIZATIONAL STRUCTURE

Current Practices

In general, PLP provides services to JPA members representing libraries throughout the Bay Area; PLS provides services to libraries throughout San Mateo County; and Califa provides services to libraries throughout California. Thus the three entities provide core services to three different constituencies, with some overlap.

- PLS is the only entity with employees. PLS employs approximately 23 full-time equivalent (FTE) positions, of which 12.6 FTE are administrative positions.
- PLS provides administration, operation, accounting, technology and delivery services to PLP, along with the rental of space.
- PLS provides administrative, accounting and technology support to Califa, along with the use of space.
- PLP contracts with and provides administrative services to NorthNet (NLS), a geographically large Northern California consolidated CLSA system.
- PLP provides administration, delivery, system operation/committee support and other programs to its member libraries.
- Califa brokers and delivers products and services to its members, statewide.

All three entities receive and distribute grant revenues for programs that benefit libraries. All three entities provide library services and/or products to libraries. In addition, the California State Library (CSL) funds all three entities for certain services, such as those provided through LSTA grants. All three entities often act only as the fiscal agent for large grants and not as the provider of services, which are performed by third party contractors. For instance, under the large Infopeople grant, Califa currently acts only as fiscal agent and not as the provider of services.

Attached as Exhibits B, C and D are broad organizational charts for the three entities.

Attached as Exhibit E is an existing organizational chart, by position.

Budget Summaries

PLS Budget

In its adopted fiscal year 2015/16 budget, PLS provides the following services at the following costs:

Table 1: PLS Services, FY 2015/16

Services	**FY 2015/16 Budget**
Communication and Delivery	$448,144
Administration	$1,376,343
System Operations	$28,079
PLS Building	$360,500
PLAN Central (services to all members)	$1,299,160
PLAN Local (services to individual members)	$1,800,000
Total Expenditures:	**$5,312,226**

The budget for PLS Building expenditures includes $268,000 in debt service, which is approximately $97,000 more than the scheduled debt service, and which is in large part supported by drawing down on the PLS fund balance. The purpose of this additional amount is to pay principal on the mortgage at a faster rate than required by the mortgage note.

The fiscal year 2015/16 PLS budget shows that the above PLS costs are funded by the following sources:

Table 2: PLS Source of Funds, FY 2015/16

Revenue and Source of Funds		**FY 2015/16 Budget**
Federal grants (indirect fees for FY 14/15 LSTA and NEH grants)		$200,000
Other agencies:		$1,257,377
Califa contract	$730,950	
PLP contract	$352,883	
NorthNet services	$ 83,510	
Delivery services (SVLS, CLSA, etc.)	$ 66,000	
Califa server maintenance	$ 15,034	
Other	$ 9,000	
PLAN shared cost (all members)		$1,280,626
PLAN reimbursable cost (pass-thru paid by individual members)		$1,800,000
PLAN recovery cost		$3,500
Communication & delivery shared cost (all members)		$382,144
Workshop fees		$4,000
Rental income:		$276,000
PLP /PLAN	$ 60,000	
Non-library tenants	$216,000	
Interest income		$24,079
Use of fund balance (for optional mortgage principal payments)		$84,500
Total Budgeted Revenue and Source of Funds		**$5,312,226**

In summary, in its fiscal year 2015/16 budget, PLS primarily receives money from administrative fees on grants, contracts to cover administration, PLS members to cover communication and delivery and PLAN costs, reimbursements from members, and rental income.

PLS financial condition is also reflected by the extent to which the entity's reserves and undesignated fund balance are adequate and stable, or whether they are being used to support ongoing obligations.

Fiscal Year 2015/16 PLS:	**Reserves**	**Undesignated**	**Total**
Beginning Fund Balance	$255,533	$1,519,708	$1,775,241
Ending Fund Balance	$217,533	$1,519,708	$1,737,241

Total fund balance for PLS decreased by approximately $260,000 in fiscal year 2013/14, increased by approximately $264,000 in fiscal year 2014/15 and is projected to decrease by $38,000 in fiscal year 2015/16. The PLS Board adopted an Operating Reserves Reserve Policy in June 2015 which established a target operating reserve equal to three months of operating costs, excluding reimbursable or pass-through programs, depreciation, in-kind and other non-cash expenses. The total projected fund balance at June 30, 2016, represents approximately 32% of total budgeted fiscal year 2015/16 expenditures, or approximately 49% of 2015/16 expenditures if $1.8 million of PLAN reimbursable costs were excluded. Based on the Reserve Policy requirement noted above, e.g. three months of operating costs, or 25%, the current year fund balance is nearly double the amount required.

PLP Budget

In its fiscal year 2015/16 budget, prior to mid-year budget revisions to add in additional grants, PLP provides the following services at the following costs:

Table 3: PLP Services, FY 2015/16

Services	**FY 2015/16 Budget**
Administration	$620,943
Delivery	$290,010
System Operation/Committee Support	$461,127
Public Library Staff Education Program (PLSEP) (LSTA)	$96,430
Total Expenditures:	**$1,468,510**

The fiscal year 2015/16 PLP budget shows that the above PLP costs are funded by the following sources:

Table 4: PLP Source of Funds, FY 2015/16

Revenue and Source of Funds	**FY 2015/16 Budget**
Member participation fees	$550,762
Other agencies (NorthNet admin contract)	$134,641
State CLSA grants	$360,013
Federal grants: Indirect fees $137,644 PLSEP $ 96,430	$234,094
Reimbursable from members	$175,000
Workshop fees	$8,000
Interest income	$6,000
Total Budgeted Revenue and Source of Funds	**$1,468,510**

In summary, in its fiscal year 2015/16 budget, PLP primarily receives its revenues from member participation fees and reimbursements, state CLSA grants, NLS for contract administration services (which includes state CLSA funds), and federal and state grants.

PLP financial condition is also reflected by the extent to which the entity's fund balance is adequate and stable, or being used to support ongoing obligations.

Fiscal year 2015/16 PLP:

Beginning Fund Balance $1,052,399
Ending Fund Balance $1,052,399

Total fund balance for PLP increased by approximately $245,000 in fiscal year 2013/14, increased by approximately $125,000 in fiscal year 2014/15 and is projected to not change in fiscal year 2015/16. The projected June 30, 2016, fund balance of $1,052,399 represents approximately 72% of budgeted fiscal year 2015/16 expenditures.

Under the PLP contract with PLS, PLP pays PLS $462,393 for administration, operation and accounting services ($352,883), delivery services to PLP member SVLS ($26,000) and administration services to NLS ($83,510). At the same time, under a PLP contract with NLS, NLS pays PLP $124,641, including the $83,510 in NLS administration services, $28,800 for a NLS Coordinator and $12,331 for miscellaneous PLP administrative costs. PLP contracts with NLS on the revenue side because PLP is seen as the regional entity for services to NLS, and then contracts with PLS on the cost side, even though it would be more efficient for NLS to contract directly with PLS for those services. However, aligning NLS with PLP, a similar organization, supports organizational transparency and mirrors similar relationships in the state where consolidated regional systems administer other regional systems, either consolidated or legacy. PLP is considered a consolidated regional system and PLS is considered a legacy system

Califa Budget

In its fiscal year 2015/16 budget, Califa provides the following services and programs at the following costs:

Table 5: Califa Services, FY 2015/16

Services	**FY 2015/16 Budget**
Operations (includes $3.5 million in vendor pass-thru payments)	$4,173,477
E-books	$300,000
ENKI Library	$250,000
Califa grant (California Library Collaborative Grant)	$261,818
Early Learning with Families Statewide Initiative: Year 3 (ELF)	$645,820
Get Involved: Expanding/Sustaining Skilled Volunteer Eng.	$78,800
Total Expenditures:	**$5,709,915**

Califa contracts with PLS for administration, accounting and technology support for Califa operations. The total fiscal year 2015/16 contract equals $745,986, of which $494,512 is paid out of Operations shown above and the remaining $261,818 is paid out of the Califa grant program shown above.

The fiscal year 2015/16 Califa budget shows that the above Califa costs are funded by the following sources:

Table 6: Califa Source of Funds, FY 2015/16

Revenue and Source of Funds	**FY 2015/16 Budget**
Grants – Indirect fees on FY 2014/15 grants	$239,269
Special grants – Indirect fees on CSL Broadband Services – Year 1	$112,500
Califa membership fees	$68,000
Interest income	$8,200
Income from product/vendor	$155,000
Workshop fees	$13,000
Vendor pass-through	$3,500,000
Use of fund balance: Safari database $200,000 ENKI library $200,000 Other $77,508	$477,508
Database revenue	$100,000
ENKI Library subscriptions	$50,000
LSTA grants: Califa $261,818 ELF $645,820 Volunteer Eng $78,800	$986,438
Total Budgeted Source of Funds	**$5,709,915**

The 2015/16 amount shown for indirect fees on CSL Broadband Services is to be reviewed based upon time tracking by staff.

In addition to the above revenues, Califa plans to amend its fiscal year 2015/16 budget at mid-year to include more than $4.8 million in active grants and related reimbursements. This includes approximately $1.8 million in grant revenues for the Infopeople grant and Eureka Leadership Program grant (which was formerly part of the Infopeople grant), approximately $1.8 million in grant revenues and member reimbursements for the CENIC Statewide Broadband Year 1 grant, and the remaining $1.2 million dispersed over twelve additional grant programs (including four grants carried over from the prior year).

In summary, Califa primarily receives its revenue from grant indirect fees, membership fees, income from products/vendors, vendor pass-through revenues, database revenue, subscriptions and grants.

Califa financial condition is also reflected by the extent to which the entity's fund balance is adequate and stable, or whether it is being used to support ongoing obligations.

Fiscal year 2015/16 Califa:

Beginning Fund Balance	$2,031,290
Ending Fund Balance	$1,553,782

Total fund balance for Califa decreased by approximately $120,000 in fiscal year 2013/14, decreased by approximately $470,000 in fiscal year 2014/15 and is projected to decrease by $477,508 in fiscal year 2015/16. In total, by June 30, 2016, the Califa fund balance will have dropped by more than $1 million since July 1, 2013. The projected June 30, 2016, fund balance of $1,553,782 represents approximately 27% of $5,709,915 in fiscal year 2015/16 expenditures initially budgeted or approximately 15% of approximately $10,709,000 in fiscal year expenditures once significant mid-year budget adjustments are adopted. However, if $3.5 million of vendor pass-through costs and $2.5 million of Infopeople, Eureka Leadership, Early Learning with Families and Get Involved Volunteer Engagement grant costs are deducted(for which Califa serves only as a fiscal agent), the reserve would represent approximately 34% of the annual net $4,509,000 in operating expenditures.

The budgeted fiscal year 2015/16 Califa reduction in fund balance is for the purpose of $200,000 support for the ENKI Library program, $200,000 support for Safari Database expenditures and $77,508 support for general Califa expenditures.

Discussion and Analysis

PLS vs. PLP as Operating Entity

As noted above, under the current structure, PLS is the operating entity, employing all staff, who provide programmatic and administrative services to contracting organizations, including PLP, NLS and Califa. This organizational structure is the result of legacy operational models, e.g. PLS having been organized in 1972 vs. PLP in 2009 and Califa in 2004, but it can no longer be considered the most effective operational model going forward. It is important to align the future organizational models with the individual strategic directions of each organization, as well as with each organization's unique geographic responsibilities, services and representation.

In essence, there are three types of services provided by the three entities. <u>Local</u> services include programmatic and administrative services and unique (non-CLSA) services, such as PLAN, provided to any member consolidated or legacy cooperative library system. <u>Regional</u> services include programmatic and administrative CLSA and related services to both consolidated regional cooperative library systems and legacy cooperative library systems (PLP and NLS, and their legacy cooperative system components). <u>Contract</u> services include administrative services to any organization that chooses to contract for such services, such as Califa.

Under the proposed model, PLP is the most suitable operating entity. This new model would address the strategic direction of the parent organization (PLP), and position it strategically for future growth and change as both a regional cooperative library system service provider and as a contract service provider. Under the new model, there would be a full time Executive Director, and current PLS staff would be transitioned to become PLP employees.

Exhibit F provides a proposed organization chart that reflects the proposed changes to the organizational structure.

Executive Director Position

All employees associated with the three entities are currently employed by PLS, although many administrative employees appear to wear three hats – one for each entity. For example, one position serves as Executive Director for PLS, as Chief Executive Officer for PLP and as Executive Director for Califa. This raises potential complications for all three entities related to setting priorities among the entities and to the potential appearance of conflicts of interest between the three entities. While there is a need to prioritize workflow in any organization, it becomes potentially more problematic when three separate entities are served by one leadership staff. The priorities among and for the three organizations are not clear to some board members and staff.

While there are some efficiencies in having staff support all three entities, this Report recommends that Califa retain its own full time executive director dedicated to Califa activities. This will allow Califa to clearly focus on its objective of providing services and products to libraries statewide and to foster cutting edge activities like the CENIC Statewide Broadband program. A Califa executive director would oversee Califa operations and strategic planning. Separating Califa operations from PLS and PLP operations and decision-making would clarify the roles of staff and allow Califa to operate independently.

Califa is currently paying PLS for 19 hours per week of the executive director's time, at a cost of $110,000 per year. The incremental cost of employing a new full time Califa executive director, along with clerical help, is estimated to be $170,000 more per year than what Califa is currently paying PLS for administrative services, assuming that Califa employs a full-time executive director.

Similarly, if Califa employs its own executive director, the payment that PLS receives from Califa would decline by approximately $110,000 (for the cost of the executive director), and this would increase the annual net cost to PLS and PLP by $110,000, if PLS/PLP continues to employ a full-time executive director. In addition, as part of this shift, it would be appropriate for Califa to pay rent to PLS rather than the current 5% overhead rate collected to cover the Califa use of space.

Califa Support Staff

There have been challenges for administrative staff in balancing the workload priorities of the three entities. This Report recommends that Califa create its own employment base, by hiring its own full time executive director and employing the four existing PLS positions (2 of these positions are currently vacant) dedicated to Califa activities to conduct the business operations. It is recommended that these four positions devoted entirely to Califa activities be transitioned to Califa employment, reporting directly to a Califa Executive Director, in part to address this issue, but also as part of the overall transition to a separately administered Califa entity.

Funding Implications

When grant opportunities are considered by staff, it is not always clear how it is determined which of the three entities will apply for the grants. It appears that the CSL tries to balance grants to various systems so that indirect fee revenues are received by all entities, but this is not consistently evident. A general practice in the past, on the part of PLS, PLP and Califa, has been to continue to use the entity that previously applied for a grant to apply for a renewal of the same grant. Recently, however, a federal grant for the Infopeople program, with $1.5 million in program costs, was applied for and awarded to Califa for fiscal year 2015/16 following many years of having been awarded to PLS. The Infopeople grant program predated the formation of Califa, so PLS was the original grantee for this grant. This change allowed for a statewide program to be aligned with Califa, an entity providing statewide services, consistent with the Executive Director's strategic direction that statewide programs be aligned with the statewide organization Califa, rather than with one of the regional CLSA systems. This change raised issues about setting priorities among the three entities and also moved $190,000 in annual indirect fee revenues from PLS to Califa beginning in fiscal year 2016/17, based upon the current methodology employed by PLS (where indirect fees are recognized in the year following receipt of related grant revenues). Since this annual source of revenue has been part of the balanced PLS budget in the past, PLS must address a revenue shortfall of approximately $190,000 beginning in fiscal year 2016/17. On the other hand, this shift will strengthen the budget of Califa by adding new revenue to the Califa budget beginning in fiscal year 2016/17.

If Califa does separate from PLS/PLP and hire its own employees, as described above, then the PLS annual budgetary deficit would increase from $190,000 to approximately $300,000 if PLS continued to employ a full-time executive director. However, if a full-time PLS/PLP executive director position is continued, PLS and PLP would share the staff costs, based upon the relative allocation of costs between PLS and PLP.

The anticipated PLS budget shortfall in fiscal year 2016/17 is also tied to the fact that there are staff costs not recovered through contracts with Califa or PLP. This is reflected in the fiscal year 2015/16 budget, which shows a $172,470 cost of PLS salaries and benefits not recovered through the contracts with the other entities. This includes a full-time Building Manager, half-time Accountant, two part-time Office Assistants and two part-time Account Clerks. These costs have been essentially funded by indirect grant fee revenues. To the extent that these positions serve PLP and Califa activities, they should be paid for by PLP and Califa. To the extent that these costs benefit PLAN activities, such costs should be recovered through higher membership fees for PLAN.

CSL has informed Califa that within four years, CSL will eliminate the current $261,000 grant received by Califa, as well as the $165,000 Infopeople grant indirect fee revenue to be received by Califa beginning in fiscal year 2015/16. These changes would not necessarily affect the fiscal year 2015/16 net Califa fiscal operations because Califa could terminate the services of the contractors for the Califa grant activities. The loss of these grant revenues from CSL highlights the uncertainty surrounding the continued receipt of other grants and the sustainability of Califa if it continues to depend upon such grants. At the same time, Califa fills an important role as a statewide entity in fulfilling CSL statewide goals, so there may be motivation for CSL to continue funding Califa.

Budget Formats and Content

The workflow, priorities and structure of the organizations are not obvious in the budgets of the three entities. While the budgets appear to properly account for significant revenues and expenditures, there is little narrative that accompanies the budget numbers. The budget documents do not tell an easy-to-understand story nor do they clearly communicate the flow of funds between the three organizations. Some board members have been unclear about the role of each entity and this has led to questions about interactions between the entities.

Recommended Actions:

The three separate PLS, PLP and Califa organizations should be retained. While there are overlaps in the areas they benefit, they serve separate constituencies in different geographical areas and no obvious material benefits would accrue should any of the organizations be eliminated or merged with others.

CALIFA

1.1 Califa should become an independent operating entity, create its own employment base and hire its own executive director and simultaneously transfer the four existing PLS positions dedicated to Califa activities to conduct the business operations, so that it may clearly focus on its objective of providing services and products to libraries statewide and so that it may foster cutting edge activities like the CENIC Statewide Broadband program. By separating Califa operations from PLS and PLP operations and decision-making, this would clarify the roles of staff and allow Califa to act independently. The issues of establishing priorities and potential appearance of conflict of interest among the three entities would be eliminated. PLS, PLP and Califa would then be in a position to apply for grants with less concern about priorities among the three entities. They may even compete for the same grants. The Califa Board of Directors would need to become involved in this process and the current PLP/PLS/Califa Executive Director would need to take a lead role in working with the Califa Board to facilitate this transition.

The incremental cost of employing a new full time Califa executive director, along with clerical support, would be approximately $170,000 per year. At the same time, the contract payment from Califa to PLS would decline by approximately $110,000 for the proportionate cost of the executive director. Califa should conduct a request for proposals (RFP) for support services such as technology support, accounting support and clerical support, and include PLS/PLP in this RFP process, as this could be more efficient than hiring new support staff.

1.2 If Califa hires its own employees, it would need to explore options for purchasing cost effective benefits for its employees. This may be accomplished by contracting with the current PLS benefit service providers. If this is not feasible, health insurance is also available from insurance brokers such as CalNonprofits Insurance Services, which provides benefits to many non-profit employers, including those with few employees. There is a process to go through to satisfy insurance companies when transferring employees to an employer for which no previous employment exists, but brokers are well versed in the spin-off process and can assist Califa in securing coverage. There would also be the need to establish a personnel system (which could mirror the existing PLS personnel system) and there would be a minor cost associated with this transition and ongoing management. The impact should be minimal to Califa if the personnel system is managed by PLS/PLP and the associated costs are included in the PLS/PLP administrative contract with Califa.

1.3 Pro-rated rent for space occupied by shared positions (assuming Califa continues to contract with PLS/PLP for administrative support services) should be recovered from Califa, as well as full rent for dedicated positions. (See "Recommendations Concerning Allocations of Costs" for a discussion of allocating costs for these positions.) If PLS/PLP is not the contract entity for administrative and support services, Califa should consider whether it should continue to rent space from PLS.

PLP

1.4 PLP should become the operational entity, the "parent" or "umbrella" organization, for the delivery of services to legacy and consolidated regional cooperative library systems. The missions of PLP, as well as PLS and NLS are aligned. However, PLP serves a broader regional constituency, and as such, is better positioned to be a regional service provider. While PLS has historically been the operational entity, it no longer makes sense to have regional library services provided by an organization that was designed for a much smaller geographic service area and service population. PLP is a broader JPA with multiple JPA members. This configuration would be more effective in providing services not only to PLS, but also to other PLP member JPA's, as well as other consolidated regional cooperative library systems or legacy systems not currently served by PLP. Additionally, it would ensure the key role of the broader regional PLP Board for operational decision making. Exhibit F is a proposed organization chart outlining the new model.

1.5 The transition from PLS to PLP as the operational entity would entail the transition of existing staff from the current employer to a new one, as well as establishment of new fiscal systems, developed specifically for the regional network model. See Recommendation 1.2 above for additional information on transition issues. If staff needs assistance in implementing this transition, PLS/PLP should bring in consultants to assist with this process. While it will require some effort to complete the transition, the new organizational structure will position PLP in a much more effective manner to be a future focused service provider of consolidated regional and legacy system services. Additionally, the transfer of organizational responsibilities from PLS to PLP will eliminate the current revenue/cost conflict with the NLS contracts, as NLS would only contract directly with PLP.

1.6 Under the reorganized structure, PLP should employ a full time executive director. A key change driver is that PLP members are interested in having the organization provide a broader range of services and this requirement, combined with future service model changes and additions, supports the recommendation for a full-time executive director. This change driver may also result in new and different staffing models, as PLP continues to align its staffing capacities with member service needs.

1.7 PLS should continue to hold title to the property and lease space to PLP and Califa. See discussions above in Recommendations regarding Califa and below in Section 4 regarding recommendations on financing of the property.

1.8 The establishment of PLP as the operating entity will significantly change or eliminate some or all of the cost allocation processes. At the point that the PLS/PLP transition occurs, a new cost allocation plan will need to be created, particularly if Califa contracts with PLP for administrative support services.

1.9 Depending upon the transition processes and results, the PLP membership fee structure may need to be reviewed.

1.10 PLAN services should be managed by PLP, and PLAN staff should become PLP staff. While PLAN services are currently provided only to PLS members, positioning PLAN as part of the broader regional service organization would allow potential future growth of shared system and technology related services to other consolidated or legacy regional system members.

1.11 Section V.(a) of the PLP Joint Powers Agreement would need to be amended to provide that PLP, rather than PLS, would serve as Treasurer/Controller and fiscal agent for PLP in order for PLP to become the operational entity, subject to legal review.

1.12 The establishment of Califa as an independent operating entity should take place first, followed by the transition from PLS to PLP as an operating entity.

PLS

1.13 To deal with an approximate annual PLS budget shortfall of $300,000 if Califa hires its own executive director and PLS/PLP employs its own full-time executive director, PLS should consider taking a combination of the following actions:

- Identify how much of its employee costs not currently charged to the PLP and Califa contracts are actually associated with PLP and Califa services, and then increase the share of costs to PLP and Califa to cover those costs (see Recommendations Concerning Allocations of Costs below);
- Increase PLS member fees by amounts not recovered from PLP and Califa;
- Identify additional existing PLAN Central costs not currently charged to PLS members, if any, and then charge those costs to members;
- Identify new potential revenue sources.

In theory and in practice, all PLS costs should either be for services that are recoverable through member billings or contracts for services, or be related to the building and financed by rental income and contract charges.

Budget Recommendations

1.14 The budgets presented to the PLS, PLP and Califa boards should include the following additional elements to enable a better understanding of the flow of funds, allocation of resources and interconnectedness of the three budgets. If staff needs assistance in implementing these changes, PLP/PLS should bring in consultants to assist with this process.

- A schedule should be added to each budget describing the number of employees and contract staff associated with each entity. The schedule should show, for each position, the job title, the number of hours employed per week and the number of hours scheduled to work under contract for each entity receiving contract services (PLS, PLP, Califa and NLS).
- A clear summary should be added for each of the three entities showing how much money is flowing from each to another entity, including PLS, PLP, Califa, NLS and the State of California (separating out state CLSA funds and federal pass-thru LSTA funds).
- Program budgets should clarify revenues, expenditures and use of fund balance or reserves for each program.
- Budgets should include information on beginning and ending fund balances and reserves, and trends showing increases and decreases in fund balances and reserves over recent years.
- A narrative should be added to each of the three budgets explaining the purpose of the entity and the services to be provided and projects to be undertaken during the budget year.
- Narratives should be added to each budget describing current financial condition, financial trends, financial risks, financial opportunities, current initiatives funded in the budget and the focus of each budget.
- Each of the budgets should be presented in a similar format for easier reading and comprehension. For instance, all three budgets should have a summary budget schedule combining the activities of all programs and divisions. Currently, only the PLS budget has a summary schedule.

1.15 Califa should not continue to rely upon use of its previously accumulated capital to balance its budget, particularly because of the uncertainty of continued funding from the State. The budget shortfall for Califa (based on the current fiscal year 2015/16 budget) is projected to be $477,000 if Califa does not become an independent organization, or $647,000 if Califa hires a full-time executive director. Options to balance the budget would include reducing or eliminating the ENKI Library and Safari Database subsidies and/or increasing membership fees.

1.16 The PLP and Califa boards should each adopt a fund balance reserve policy and adopt a specific target fund balance equal to an amount between 25% and 30% of its annual operating expenditure budget. The Government Finance

Officers Association (GFOA) recommends that entities maintain a minimum fund balance equal to at least 2 months (or 17%) of annual expenditures. However, because of the current environment where some grant revenues are uncertain, the three entities should have balances on hand between 25% and 30% of annual budgeted operating expenditures, excluding member pass-through costs and excluding significant costs associated with grant revenues where the entity serves only as a fiscal agent and not as a provider of services. Specific fund balance targets are recommended in Table 7. The targets were calculated using the latest actual or projected budget information provided by PLS staff, but excluding $1,800,000 for PLS for PLAN reimbursable costs, and excluding, for Califa, $3,500,000 in vendor pass-through costs and $2,500,000 in pass-through grant costs. The current Califa "operating reserve" of $225,000 would be part of the target fund balance.

Table 7: Recommended Fund Balance Targets

	Recommended Fund Balance Target	**Projected Fund Balance at June 30, 2016**
PLS	$900,000	$1,737,241
PLP	$400,000	$1,052,399
Califa	$1,200,000	$1,553,782

2. RECOMMENDATIONS CONCERNING ALLOCATION OF COSTS

Current Practice/Analysis

Currently, PLS employs approximately 23 full-time equivalent (FTE) positions, of which 12.6 FTE are administrative positions. Two of the authorized positions for Califa (the Accounting and Administrative Coordinator and the Membership/Outreach Manager) are not currently filled.

The administrative positions and the current budgeted allocations to the three entities are presented in Table 8:

Table 8: Budgeted Position Allocations

Classification	Work Week	PLP	Califa	PLS
Chief Executive Officer	Fulltime	52.5%	47.5%	
Chief Financial Officer	.85	55.0%	30.0%	
Office Manager	Fulltime	30.0%	70.0%	
Building Manager	Fulltime			100%
Secretary	.75	37.5%	37.5%	
Office Assistant	.45	24.0%		21.0%
Office Assistant	.45			45.0%
Accountant	.25	20.0%	5.0%	50.0%
Account Clerk	.60			60.0%
Account Clerk	.80	56.0%		24.0%
Project Manager	Fulltime		100%	
Operation Manager	Fulltime		100%	
Accounting/Admin Coordinator	Fulltime		100%	
Membership/Outreach Mgr.	Fulltime		100%	
IT Manager/Support	.10		10.0%	

PLS staff has begun to track the actual staff time spent for each entity for some of these administrative positions. Actual time spent on each entity for the period July to October 2015 is presented in Table 9:

Table 9: Actual Position Time Allocations

Classification	PLP/ NorthNet	Califa/ Infopeople/ CENIC	PLS	Multi-System*
Chief Executive Officer	n/a	n/a	n/a	n/a
Chief Financial Officer	30.34%	36.26%	20.86%	12.54%
Office Manager	36.75%	20.46%	11.44%	31.35%
Building Manager	29.68%	12.96%	36.60%	20.76%
Secretary	13.32%	16.88%	33.06%	36.74%
Office Assistant	15.71%	44.17%	40.12%	0.00%
Office Assistant	22.72%	26.03%	36.87%	14.38%
Accountant	7.44%	50.35%	27.26%	14.95%
Account Clerk	15.41%	60.93%	22.94%	0.72%
Account Clerk	23.20%	28.79%	32.53%	15.48%

* Multi-system time represents time spent on activities such as staff meetings and payroll process that are not directly related to one entity.

The above Tables show that time is being spent differently from time charged through the allocation of positions in the budget and contracts. For instance, the Office Manager position is budgeted to spend 30% of time on PLP activities and 70% of the time on Califa activities, whereas the actual time tracked shows 36.75% of time on PLP activities and 20.46% of time on Califa activities, in addition to 11.44% of time on PLS activities (each of which would be adjusted upward when the multi-system time is allocated proportionately to the three entities). However, the period tracked is only for a portion of a fiscal year and may not reflect the relative time spent during the entire annual program and accounting cycle. It is not surprising that actual time spent would differ from allocations of time, because time has not been previously tracked in an organized manner.

Recommended Actions:

2.1 It is recommended that all administrative staff track their time by contract/entity and that future budgets and contracts be based on time spent on work related to each entity, including consolidated regional systems like NorthNet, as measured by time logs. Time should be tracked for an entire year to fully capture the ebb and flow of projects and work demands. Unallocated multi-system time should be allocated back to each entity in the ratio of direct time spent for each position for one entity as compared to total direct time spent on all entities, under the assumption that multi-system time benefits all entities in the same ratio.

[For instance, if the Accountant spent an average of 10 hours on PLP per week, 15 hours on Califa, 5 hours on PLS (for 30 hours of direct time per week) and 10 hours on multi-system activities, the ten hours of multi-system time would be allocated back to PLP (10/30 x 10 hours = 3.33 hours), to Califa (15/30 x 10 hours = 5 hours) and to PLS (5/30 x 10 hours = 1.67 hours). Then total weekly average hours for PLP would be (10 + 3.33 = 13.33 hours), hours for Califa would be (15 + 5 = 20 hours) and hours for PLS would be (5 + 1.67 = 6.67 hours).]

2.2 All entities should obtain an outside cost allocation plan in the future to accurately allocate and charge costs for services among the three organizations (or two if Califa is a completely separate entity).

3. RECOMMENDATIONS CONCERNING MEMBERSHIP/ FISCAL AGENCY FEES

Current Practices

PLS Fiscal Agency Fees
PLS recovers from its members and contractors the following annual amounts:

Table 10: PLS Member Payments FY 2015/16

Source of Funds		**Member Payments**
Other agencies:		$1,257,377
Califa contract	$730,950	
PLP contract	$352,883	
NorthNet services	$ 83,510	
Delivery services (SVLS, CLSA, etc.)	$ 66,000	
Califa server maintenance	$ 15,034	
Other	$ 9,000	
PLAN shared cost (all members)		$1,280,626
PLAN reimbursable cost (pass-thru paid by individual members)		$1,800,000
PLAN recovery cost		$3,500
Communication & delivery shared cost (all members)		$382,144
Workshop fees		$4,000
Rental income:		$60,000
PLP	$ 35,000	
PLAN	$ 25,000	

PLS allocates its PLAN membership costs to the seven member cities, San Mateo County and the San Mateo County Community College District (SMCCCD) primarily on the basis of resident circulation and technology. A base fee is charged to all jurisdictions, with a higher base fee for SMCCCD than for non-academic members. Additional costs are allocated to all entities other than SMCCCD on the basis of resident circulation (50%) and technology (50% with equal weighting given to the number of network devices, the number of wired PC's and the average number of Wi-Fi users per day). This formula was approved in February 2013 and is being phased in through fiscal year 2016/17. The formula appears reasonable as it includes a base fee and allocates most costs on the basis of member use (circulation and technology).

PLS allocates its PLAN delivery costs to the seven member cities, San Mateo County and the SMCCCD primarily on the basis of the number of delivery stops (25%) and volume (75%). Again, this appears to be a reasonable allocation tied to user benefit.

Specific PLS costs benefitting individual members are separately charged directly to those members.

Rental income shown in Table 10 is separately discussed in "Recommendations Concerning Building Ownership."

PLP Fiscal Agency Fees

PLP recovers from its members and contractors the following annual amounts:

Table 11: PLP Member Payments FY 2015/16

Source of Funds	**Member Payments**
Member participation fees	$550,762
Other agencies (NorthNet admin contract)	$134,641
Reimbursable from members	$175,000
Workshop fees	$8,000

PLP currently allocates its membership fees on a tiered basis, based on the size of each member's budget. The schedule sets fees for public library systems at a base fee of $5,641 (to recover 30% of costs). An additional fee is based on the size of the agency's budget, with a minimum of $2,000 and a maximum of $55,000. A separate schedule sets fees for academic libraries, with no base fee and with a minimum fee of $1,500 and a maximum fee of $5,000, based on the size of the agency's budget. This formula was developed with stakeholder input and was phased in over several years. Specific costs benefitting individual members are separately charged directly to those members.

Califa Fiscal Agency Fees

Califa recovers from its members the following annual amounts:

Table 12: Califa Member Payments FY 2015/16

Source of Funds	**Member Payments**
Califa membership fees	$68,000
Workshop fees	$13,000
Income from products/vendors	$155,000

Califa currently allocates its membership fees based on the number of member-agency employees, with fees ranging from $100 to $500, except that consortia are charged $150. This appears to be a reasonable fee structure; it enables members to acquire brokered library services and materials at minimal cost. Califa has been able to keep its member fees reasonable because it has brought in other supporting revenue from grant indirect fees and income from products/vendors.

<u>Recommended Actions:</u>

3.1 Membership fee allocations should remain as structured. Califa membership fees have remained low due to the subsidy of LSTA funds and the receipt of other revenue. However, if it is determined that PLS, PLP or Califa membership fees are not fully recovering PLS, PLP or Califa costs, respectively, and if other methods to balance the budgets are not productive, then membership fees should be increased to recover more of the costs benefitting those members, and to balance the budget. Califa should cover its base operating costs through membership fees and use other revenues to cover variable costs.

4. RECOMMENDATIONS CONCERNING BUILDING OWNERSHIP AND MORTGAGE

Current Practices and Condition:

Ownership and Use

PLS currently holds title to the property and the building that houses the administrative offices of PLS, PLP and Califa.

The building currently has tenants comprised of PLP, PLAN (part of PLS), Califa and five private businesses. Rent is charged to PLP in the amount of $35,000 per year and to PLAN in the amount of $25,000 per year. Rent is charged to the five non-library tenants for a total of approximately $216,000 per year. Rents range from $1.92 to $2.85 per square foot. Rent is not charged to Califa for use of space; instead a $35,523 overhead payment, based on 5% of staff costs provided by PLS to Califa is charged to Califa under the PLS/Califa contract, which has been considered to include the use of space.

When commercial leases expire, PLS staff checks market conditions so that the appropriate rent is included in leases. (See “Recommended Actions 1.4” for recommendations concerning recovery of costs for the use of space by entities to which PLS provides services).

Total leasable space amounts to 13,245 square feet. PLS administration and the PLS meeting room inhabit a combined 25% of the space; PLP and PLAN inhabit a combined 17% of the space and the five businesses inhabit the remaining 58% of the space.

Since PLS owns title to the real estate, neither PLP nor Califa have any ownership stake in the property. The deed of trust for the mortgage has a “due on sale – consent by lender” clause that allows the lender to call the full amount due upon the sale or transfer of the property. Therefore, a transfer of ownership may trigger the need for a new mortgage, at no better than the existing rates and term, and would serve no particular purpose. In addition, shared ownership could lead to disagreements among owners regarding real estate management of the property.

Mortgage

The building was purchased by PLS in 2002 for $4,750,000 with a down payment of $1,500,000 and a mortgage of $3,250,000. The property was refinanced to take advantage of lower interest rates on February 15, 2012, with a new loan of $2,250,000, 84 initial monthly payments of $14,234.61 through February 15, 2019, and an initial interest rate of 4.5%. The interest rate becomes a variable rate after February 15, 2019, and will be based upon the 8-year Federal Home Loan Bank Classic Advance Rate plus a margin of 2.25%. The next 95 payments, from March 15, 2019 through January 15, 2027 are scheduled to be $14,335.44 each, assuming an effective interest rate of 4.62% during that period of time (although that interest rate and these monthly payments would change if the Federal Home Loan Bank Classic Advance Rate increases). The interest rate in effect after February 15, 2019, cannot be less than 4.5% and cannot be more than 13.0%. A rough estimate of the "worst case" monthly payment, if interest rates did climb to 13% after February 15, 2019, would be $21,000 per month (or $252,000) per year.

A balloon payment of $781,033.82 (assuming no prepayments have been made) is due on the last payment date, February 15, 2027. PLS has not addressed how this balloon payment would be funded in 2027, and if the mortgage is not renegotiated or refinanced in 2019, a funding system would need to be put into place to pay the balloon payment in 2027.

The mortgage allows for prepayments on the loan. The prepayment penalty for the remaining loan period between now and February 15, 2019 is 1% of the amount prepaid. However, PLS may prepay principal up to 20% annually without a prepayment penalty.

PLS has been making additional principal payments without paying prepayment penalties as allowed under the terms of the loan. During fiscal year 2014/15, PLS prepaid more than $264,000 in principal. PLS is currently making prepayments of $7,765.39 each month. As of September 15, 2015, PLS owed $1,740,694.17 in principal.

PLS staff recently researched the feasibility of refinancing the mortgage again to take advantage of reducing the interest rate and saving money, but the available terms were not better than the existing terms.

Options available to PLS concerning payment of the mortgage include:

1) Make the scheduled payments only, with the risk of higher interest rates after February 2019 and the continued requirement of a balloon payment in February 2027. This approach would mean that PLS would stop making extra principal payments of $7,765.39 each month.

2) Continue making extra principal payments of $7,765.39 per month, which would reduce the overall principal amount, reduce interest payments on the mortgage, reduce the impact of the interest rate risk after the interest rate becomes variable in February 2019, and reduce the amount of the balloon payment due in February 2027. In addition, making the extra payments allows PLS to use idle cash to pay off an obligation costing 4.5% in interest when it is only earning 0.3% on the idle cash (although, as interest rates on idle cash increase over time, this interest rate spread will narrow).

3) Pay off as much of the loan balance as possible using idle cash in February 2019 when there is no prepayment penalty, to mitigate the potential impact of an increase in interest rates. This would allow PLS to improve its financial condition by using idle cash currently earning 0.3% interest to pay off an obligation costing 4.5% in interest. However, this option would deplete idle PLS cash at that point in time.

4) Refinance the loan after February 2019 to eliminate variable interest costs at a time when the prepayment penalty on a full loan payoff would be zero. The feasibility and viability of this option would depend on the interest rates and other loan terms available at that time.

5) Pay principal down to the maximum extent possible as soon as possible, while avoiding the prepayment penalty and while maintaining the target PLS fund balance proposed in Recommended Action 1.16. It would be prudent for PLS to use idle cash to pay off an obligation costing 4.5% in interest rather than to invest this cash and only earn 0.3% in interest. Since the outstanding balance on the loan is about $1.7 million and the loan allows for annual prepayments of up to 20% of the principal balance without penalty, PLS could make up to approximately $340,000 in extra principal payments this year, avoid a penalty and still maintain a fund balance in excess of the reserve target. (Other financial issues discussed in this Report would also need to be addressed to maintain the recommended fund balance.)

<u>Recommended Actions:</u>

4.1 PLS should continue to hold title to the real estate. The building represents an investment for PLS. There is no compelling reason to transfer title, and doing so would likely trigger a new mortgage with rates and terms that are likely not better than the existing mortgage. In addition, a transfer among the owners could create opportunities for disagreement concerning the use of the property. If PLS determined that it is more economical to move its administrative operations and/or PLAN operations to another location and pay rent at the new location, while renting out its current space in the existing building, that option would exist.

4.2 PLS should prepay principal to the maximum extent possible as soon as possible, while avoiding the prepayment penalty and while maintaining a target fund balance recommended at $900,000. This would allow PLS to improve its financial condition by using idle cash to pay off an obligation costing 4.5% in interest when it is only earning 0.3% on the idle cash, and allow PLS to maintain a reasonable reserve fund.

4.3 PLS should again explore refinancing the existing loan in February 2019, once the prepayment penalty no longer applies. The variable rate mortgage and the balloon payment terms should be renegotiated, if possible.

4.4 In the event that PLS does not renegotiate or refinance the loan in February 2019, it should develop a funding strategy and mechanism to pay the balloon payment due in 2027. No such strategy exists at the current time.

4.5 A contract between Califa and PLS should clearly describe the amount of rent to be paid by Califa to PLS. The rent charged should include the use of space for both Califa staff (including existing four Califa assigned staff, new Califa executive director and new Califa clerical staff) and a pro-rata portion of any PLS/PLP staff who work partly on Califa support activities.

4.6 PLS should obtain a current appraisal of the real estate so that it is aware of the property value and the PLS equity in the property.

Exhibit A – Interviews

During the evaluation, interviews and meetings were held with PLS, PLP and Califa representatives. Appreciation is expressed to the following individuals for their cooperation, insights and assistance in this evaluation.

Linda Crowe	Califa Contractor and former PLS Executive Director
Anne-Marie Despain	PLS Board Chair and San Mateo County Library Director
Susan Hildreth	PLS Executive Director, PLP Chief Executive Officer and Califa Executive Director
Terry Jackson	PLS Contractor managing PLP
Paula MacKinnon	Califa Assistant Director
Donna Truong	Chief Financial Officer, PLS, PLP and Califa
Eleanor Uhlinger	Califa Board President and Naval Post Graduate School University Librarian

EXHIBIT B

PENINSULA LIBRARY SYSTEM

ORGANIZATION CHART

Organizational and Governance Description

Peninsula Library System

Established under CLSA as a JPA in 1972

Administrative Council
Executive Director

Administration

Operations

- PLAN
- Member Services
  - Delivery

HR

- Payroll & Benefits

Finance

- Budget
- Bill/Invoice Processing
- Contract Management
  - Infopeople
  - CLSA Systems
  - CALIFA
  - State Library (CSL)

PLS provides administration and all staff support in order to fulfill contractual obligations to PLP, BALIS, MOBAC, SVLS, and NorthNet, (all CLSA Library Systems); CALIFA; and other entities such as the California State Library and Infopeople.

EXHIBIT C

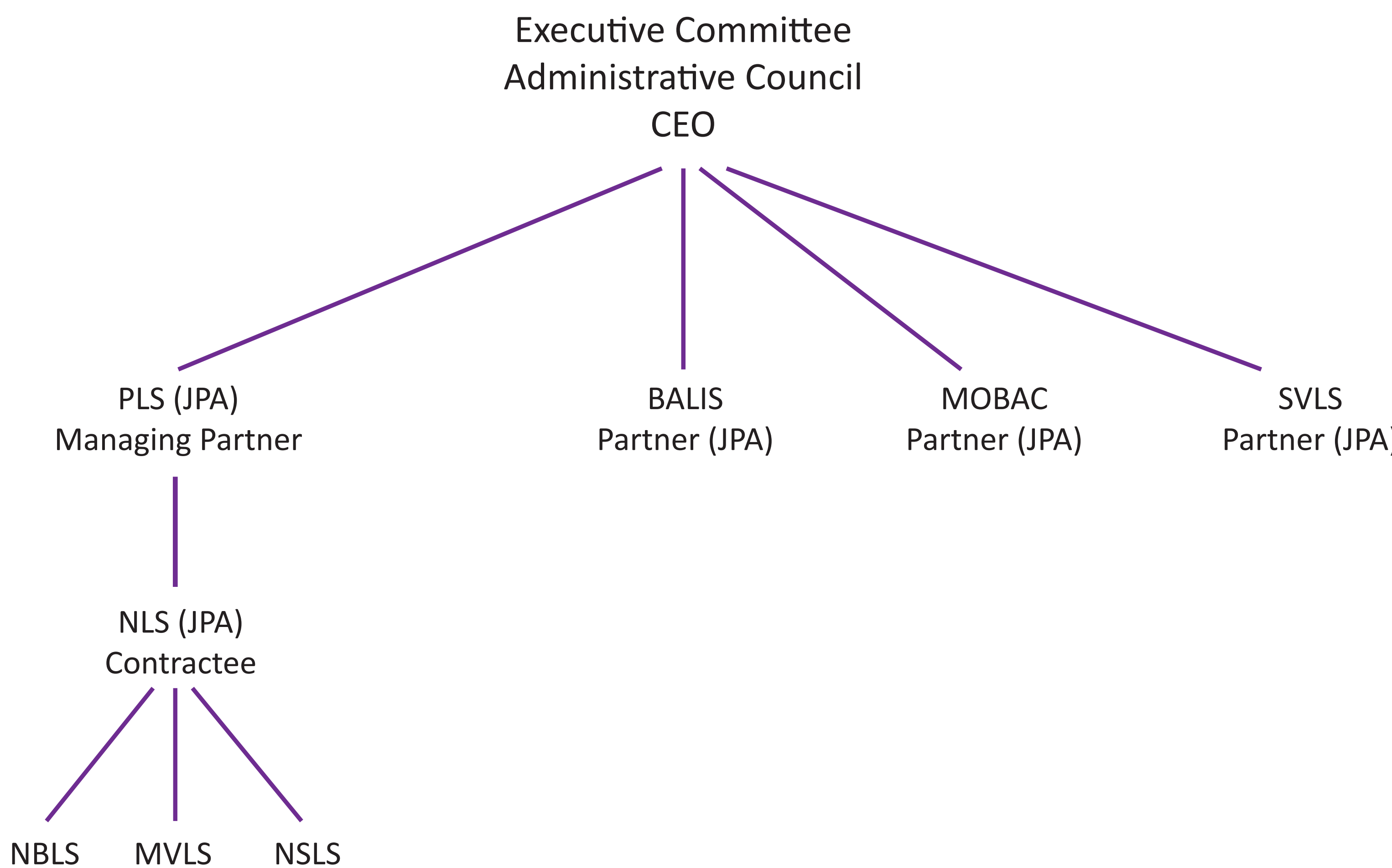
PACIFIC LIBRARY PARTNERSHIP

ORGANIZATION CHART

Organizational and Governance Description

Pacific Library Partnership

Established under CLSA as a JPA in 2009



PLS provides administration and all staff support in order to fulfill contractual obligations to PLP, BALIS, MOBAC, SVLS, and NorthNet, (all CLSA Library Systems); CALIFA; and other entities such as the California State Library and Infopeople.

EXHIBIT D

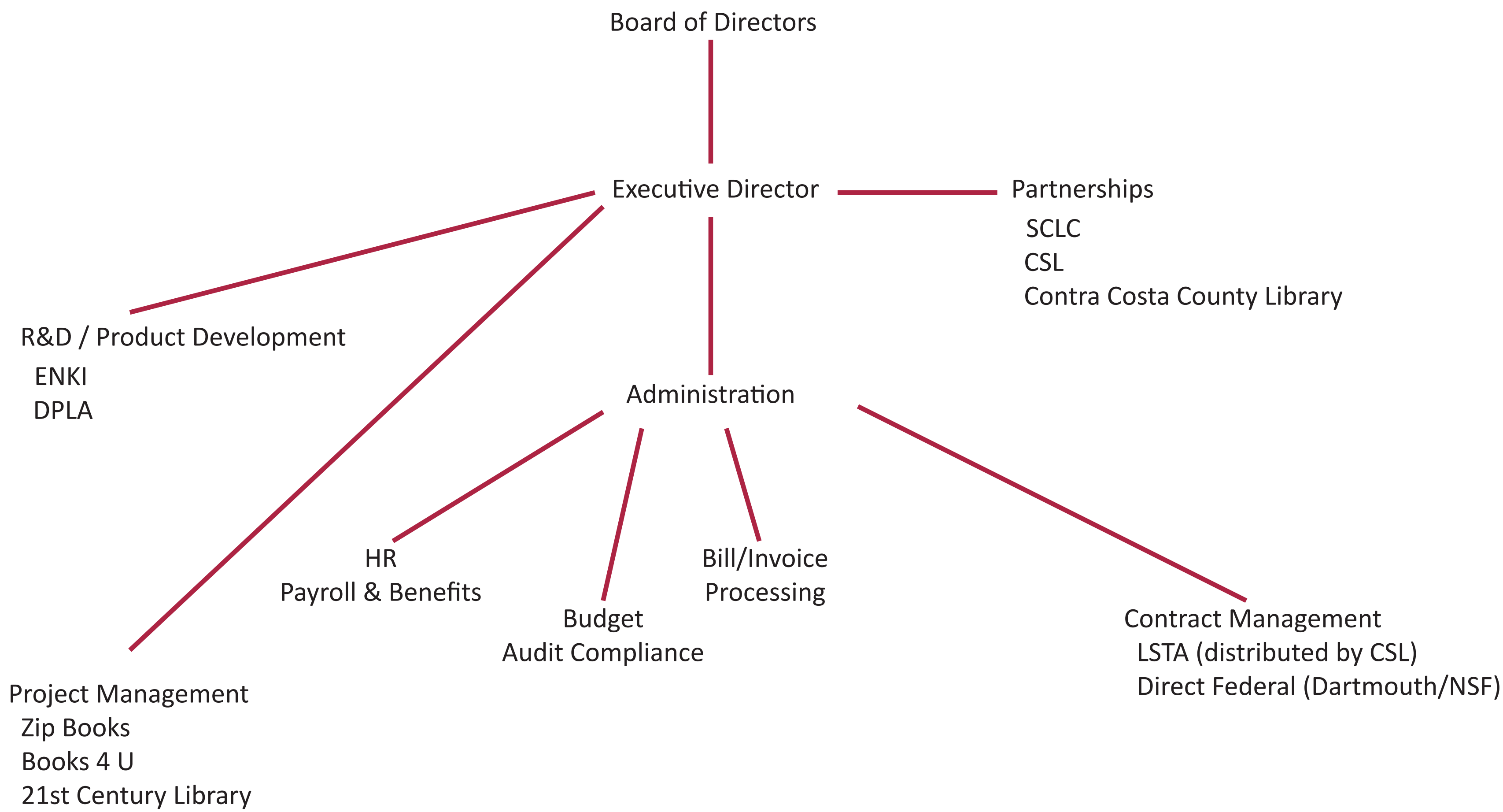
CALIFA

ORGANIZATION CHART

Organizational and Governance Description

califa

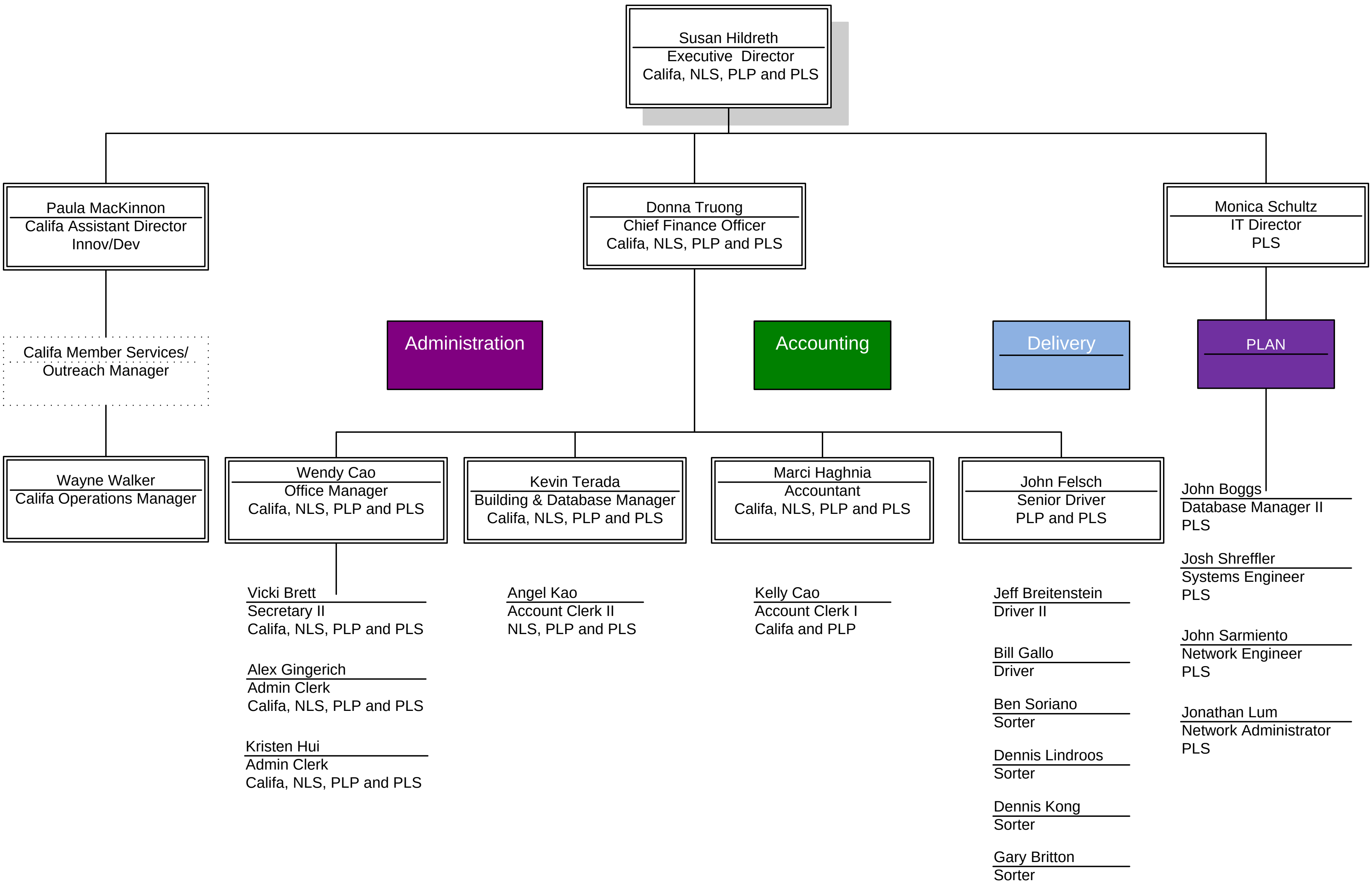
Created by PLS with LSTA funding in 2002/03. CALIFA was established as an independent 501(c)3 in 2004.



CALIFA contracts with PLS to provide the necessary administration and staff, human resources support, financial support, including budget and audit compliance, contract administration and invoicing/bill paying. The CALIFA Board of Directors approves its annual budget and its contract with PLS.

EXHIBIT E

EXISTING STAFF ORGANIZATION CHART



Updated: 2016

EXHIBIT F

PROPOSED NEW PLP ORGANIZATIONAL MODEL

Pacific Library Partnership

PROPOSED NEW PLP ORGANIZATIONAL MODEL

- **Pacific Library Partnership**
  Executive Committee
  Administrtative Council
  Executive Director
  PLP Staff
  - **REGIONAL**
    (Program and administrative support service s, e.g. CLSA system services, training)
    - Pacific Library Partnership (Regional System Services)
      - BALIS
      - MOBAC
      - PLS
      - SVLS
    - NorthNet Library System
      - MVLS
      - NBLS
      - NSLS
  - **LOCAL**
    (Program and administrative support services for legacy system services)
    - PLAN
  - **CONTRACT**
    (Administrative support services for non-CLSA organizations, e.g. finance, IT, HR)
    - CALIFA