

MINUTES OF THE APRIL 4, 2011, FINANCE COMMITTEE MEETING

The Finance Committee (“the Committee”) of the Smithsonian Board of Regents met on Monday, April 4, 2011, at 2:00 p.m. at the Smithsonian Institution in Washington, D.C. Participating were Committee Chair David M. Rubenstein, members Senator Thad Cochran* and Roger W. Sant, and ex officio member Patricia Q. Stonesifer. Staff in attendance were Secretary G. Wayne Clough; Treasurer Sudeep Anand; Chief of Staff to the Secretary Patricia Bartlett; Smithsonian Enterprises Chief Financial Officer Gregory Bokman; Director of Advancement and Philanthropic Giving Virginia Clark; Acting Chief Financial Officer Bruce Dauer; Chief of Staff to the Regents John K. Lapiana; General Counsel Judith Leonard; Under Secretary for Finance and Administration Alison McNally; Smithsonian Enterprises President Tom Ott; Director of Government Relations Nell Payne; and Inspector General A. Sprightley Ryan. Also in attendance was Budget Analyst Ed Patrick, who recorded the minutes.

Call to Order and Approval of Minutes

Committee Chair David Rubenstein called the meeting to order and greeted the members. The Committee approved the minutes of the December 9, 2010, meeting.

Fiscal Year 2013 Budget Priorities

Mr. Dauer presented the fiscal year 2013 budget priorities proposed by the Secretary. The Committee will review the Institution’s fiscal year 2013 Federal budget request at its meeting in August 2011, prior to the budget’s submission to the Office of Management and Budget in early September 2011. In order to build the fiscal year 2013 budget request the Institution needs Committee approval of the proposed budget priorities for fiscal year 2013. With the prospect for tight Federal budgets, the Institution will concentrate its request for Federal budget increases on the following priorities: non-discretionary items, including rent and utilities; items that leverage fundraising, such as the National Museum of African American History and Culture (NMAAHC) construction and the Federal portion of public/private partnerships; and items for which fundraising is unlikely, including collections care, information technology infrastructure for Broadening Access, and facilities maintenance and revitalization. The Secretary’s remaining priority is to achieve efficiencies through the SI Redesign initiative. Funding facilities maintenance and revitalization was included in the Secretary’s priorities after the Committee emphasized its importance during a discussion with the Secretary and staff.

The Committee approved the following motion:

VOTED that the Finance Committee recommends that the Board of Regents approves the fiscal year 2013 annual budget priorities proposed by the Secretary, as amended above to include facilities maintenance and revitalization.

Fiscal Years 2011 and 2012 Federal Budget Updates

Mr. Dauer updated the Committee on the outlook for fiscal years 2011 and 2012 Federal

** participated by teleconference*

budgets. If the current debate on reducing the fiscal year 2011 budget continues to focus on specific cuts, the budget for fiscal year 2011 is expected to be only slightly below fiscal year 2010 levels. If negotiations over specific cuts fail, a large across-the-board cut may result that could entail significant budget cuts to the Smithsonian.

The Institution plans to realign \$3.8 million of the fiscal year 2011 budget into the key Strategic Plan priorities of Grand Challenges research (\$2.0 million); Broadening Access (\$0.5 million); and Strengthening Collections (\$1.3 million).

Under the President's fiscal year 2012 Federal budget, and excluding \$125 million included for NMAAHC, the Institution is at \$737 million, \$4 million below the fiscal year 2010 level. Within this budget is an additional \$3.5 million realignment to Strategic Plan priorities. In order to be prepared for severe budget reductions in fiscal year 2012, management has developed plans, which have been reviewed by the unit directors and Under Secretaries, to meet as much as a \$54 million additional budget reduction with specific cuts.

Smithsonian Institution Fiscal Year 2011 Financial Report

Mr. Dauer presented the Institution's financial situation through February 2011. This report summarizes the Institution's financial performance against budget from October 1, 2010, to February 28, 2011. It highlights the five key funding sources that have the most impact on the Institution's operations and financial stability and tracks performance against quarterly goals. With respect to Federal appropriations, the report shows the Institution is significantly under plan. This reflects receiving partial funding under the six continuing resolutions. The plan was based on the President's budget which has been overtaken by events. However, the Institution has a very workable plan for fiscal year 2011 at the fiscal year 2010 level. On the private side, fundraising is ahead of plan by \$27.2 million, and government grants and contracts are ahead by \$24.8 million. Smithsonian Enterprises is slightly ahead of plan on net gain, however it is below plan on the revenue line by \$5 million. The report also tracks expenses against quarterly goals. The variances for data through February 2011 show expenses down by \$14.1 million. Slowed expenses are normal when operating under multiple continuing resolutions.

Smithsonian Enterprises — Update on Fiscal Year 2011

Mr. Ott reviewed Smithsonian Enterprises' (SE) fiscal year 2011 performance. SE performance year-to-date through February 2011 is \$1.1 million above budget; however, Mr. Ott said this was mostly due to timing factors and not a sustainable pace. The outlook for the remainder of the year, despite some revenue challenges with magazine advertising and the catalog, shows SE on track to meet its net gain goal of \$28.2 million.

The holiday 2010 catalog experienced disappointing results and was expected to be unprofitable for the year. Due to its declining performance, SE created an internal review team to analyze that segment. It was determined that a viable business for e-commerce/catalog can be developed for the future, and that it will be necessary to restructure the e-commerce/catalog operation and add dedicated resources to this business. During the restructuring, SE

will continue with a web-only store to generate product sales and will return to a printed holiday catalog in October 2011. These actions will allow the e-commerce/catalog business to continue to function while a revitalization plan is being created; however, due to the current low-margin nature of the business, there is not an expectation of any significant net gain recovery this fiscal year. Regarding other business potential, new initiatives planned to come online are the Union Station store in May 2011 and adding digital theater capabilities to Baird Auditorium in the National Museum of Natural History in May/June 2011. The “Buy America” provision won’t have material impact this fiscal year; however, it may have financial implications in future fiscal years, depending on the nature of any transitional activities.

SE may defer some of its planned capital spending depending on the results over the next few months. As capital investments were also deferred in fiscal year 2010, SE must be careful not to cut too much investment for the future. One item SE wants to move forward with is increased seating for the Mitsitam Restaurant in the National Museum of the American Indian by expanding into the adjacent store.

Mr. Bokman then reviewed the February 2011 Balance Sheet. SE does not maintain its own cash accounts, and all cash activity is swept to the Institution’s bank accounts. SE’s balance sheet is largely traditional working capital and deferred income, primarily from magazine subscriptions not yet serviced. Receivables are down almost 25 percent, and half of that is from Media. Inventory is down about \$3 million from September 2010 and is all catalog-driven because of seasonal changes and the reduction of stock related to plans to not issue print versions of the catalog this year. Assets also reflect lower capital spending of \$3.5 million driven by the current revenue softness in theaters and stores mentioned earlier to the Committee by Mr. Ott. The \$9.1 million additional equity investment in the Smithsonian Channel is also shown in the other assets section on the SE balance sheet.

The Committee and staff discussed maximizing the bottom line versus investing in future businesses. The Committee requested that, as part of its future planning process, SE should bring forward five big investment ideas for fiscal year 2012 and beyond and indicate how these investments may impact the bottom line in the short and long term.

Update on Smithsonian Institution External Debt

Mr. Anand provided an update on the Smithsonian’s external debt. As of September 30, 2010, the Institution had \$108 million of tax-exempt debt outstanding. It was noted that the debt consisted of \$30.5 million issued for the construction of the Discovery Center at the National Museum of Natural History and \$77.5 million for the National Air and Space Museum’s Udvar-Hazy Center. The Hazy Center debt is a variable rate, tax-exempt bond that matures in 2033 and is being serviced through the fulfillment of pledges and income earned from business activities and parking at the Center. The rate resets each week with the current rate being 0.25 percent. At the end of fiscal year 2010, the Institution had collected \$50.6 million towards repayment of this debt. These funds are currently held in the Institution’s short-term portfolio, providing a natural hedge against interest rate risk on the Institution’s variable rate debt. The

Institution completed the refinancing of the Discovery Center debt in May 2010, reducing the interest rate from 5 percent to 3.8 percent and saving the Institution more than \$250,000 annually in debt service and \$4.4 million over the life of the bonds.

Wrap Up

The Chair thanked the members of the Committee and staff for their active participation and adjourned the meeting at 3:50 p.m.