



In Brief

Smithsonian Institution's Implementation of the Smithsonian Networks Contracts Report Number A-09-05, September 23, 2009

Why We Did This Audit

We performed this review at the request of the Chairman of the Committee on House Administration to provide a report on the Smithsonian Institution's implementation of the Smithsonian Networks contracts. These contracts are the basis for a joint venture to create new television channels inspired by the collections and work of the Smithsonian. The objectives of this review were to assess (1) how the Smithsonian processes film requests under the contract and, in particular, how the Smithsonian documented its decisions on proposals that were declined; (2) total contract-related revenues received to date and how the proceeds have been spent; (3) total costs of administering the contract and whether policies and procedures established for tracking those costs are adequate; and (4) whether revenues received are consistent with earlier projections.

What We Recommended

Based on our review, we made no recommendations to Smithsonian management.

What We Found

We reviewed third-party film requests and contract-related costs and revenues for the period January 1, 2006 (the effective date of the contract) through December 31, 2008.

Based on our review of film request decisions made during the period, we believe that the contract has had a minimal impact on third-party filmmakers who want to use Smithsonian content in their programs. The Smithsonian has strengthened its decision-making process by implementing a central monitoring and tracking system which includes supporting files for each film request decision.

During the period we reviewed, the Smithsonian received approximately 446 film requests and declined only two requests based on restrictions in the contract. Further, the Smithsonian has not declined any film requests because of those restrictions since August 2006.

For the review period, the Smithsonian's total revenues were in accordance with the minimum guarantee in the contract.

The Smithsonian developed a revenue-sharing plan to distribute revenue received from Smithsonian Networks to cover costs and to distribute the remaining balances to the Central Trust and to the Units (museums, research centers, and offices). Under the revenue-sharing plan, annual licensing and other fees received from Smithsonian Networks are split evenly between the Central Pool and the Unit Pool. In our opinion, the Smithsonian has adequate procedures for tracking costs of administering the contract.

Under the contract, the Smithsonian receives a guaranteed annual payment and a share of Networks revenues when gross revenues exceed a stipulated amount. During our review period, the Smithsonian received the guaranteed annual payment, in accordance with the contract. The Networks has not generated the additional revenue that was projected in the initial five-year business plan, so the Smithsonian has not yet received additional payment beyond the guarantee. Nevertheless, comparisons to projections in the initial business plan are difficult because of a five-month delay in completing the contract, negative publicity connected to the announcement of the joint venture, and changes in the product strategy.

For additional information, contact the Office of the Inspector General at (202) 633-7050 or visit <http://www.si.edu/oig>.



Smithsonian Institution

Office of the Inspector General

Date September 23, 2009

To The Honorable Robert A. Brady, Chairman, Committee on House Administration

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Subject Review of the Smithsonian Institution's Implementation of the Smithsonian Networks Contracts, Number A-09-05

We performed this review at the request of the Chairman of the Committee on House Administration to provide a report on the Smithsonian Institution's implementation of the Smithsonian Networks contracts. These contracts are the basis for a joint venture to create new television channels inspired by the collections and work of the Smithsonian. The objectives of this review were to assess (1) how the Smithsonian processes film requests under the contract and, in particular, how the Smithsonian documented its decisions on proposals it declined; (2) total contract-related revenues received to date and how the proceeds have been spent; (3) total costs of administering the contract and whether policies and procedures established for tracking those costs are adequate; and (4) whether revenues have been consistent with earlier projections.

We reviewed third-party film requests and contract-related costs and revenues for the period January 1, 2006 (the effective date of the contract) through December 31, 2008. We include a detailed description of our scope and methodology in Appendix A.

BACKGROUND

The Smithsonian entered into several agreements (referred to from this point forward as the “contract”) with Showtime Networks Inc., effective January 2006, in connection with the formation of a joint venture called SNI/SI Networks L.L.C. (Smithsonian Networks or Networks). Smithsonian Networks was formed to create new television channels that showcase scientific, cultural, and historical programming largely inspired by the assets of the Smithsonian. The Smithsonian envisioned that the channels would be distributed by cable, satellite, and internet broadband service providers and allow the Institution to share its national collections and research with TV viewers.

In March 2006, when the contract was announced, Congress, filmmakers, and historians raised concerns about the contract’s potential effect on access to and use of the Smithsonian’s collections by third-party filmmakers. The non-compete clause in the contract generally prohibits the Smithsonian from engaging in media activities that would conflict with the new venture and is intended to safeguard the financial interests of the Networks by limiting the use of Smithsonian content in third-party television projects that would compete with the Networks.¹ Specifically, filmmakers seeking to use Smithsonian assets in commercial television projects may, in some cases, be restricted from using Smithsonian content for more than incidental use. However, the non-compete clause contains exceptions for various types of programs, such as news, public affairs, and academic programs. Also, the contract allows the Smithsonian to approve a limited number of additional exceptions each year. Because of these exceptions, known as one-offs, filmmakers are able to produce and exhibit programs with significant Smithsonian content outside of the Smithsonian Channel (Channel), even though the programs would otherwise be considered competitive with the Channel.

Smithsonian Networks initially planned to offer programs on an “on-demand” service, which is a library of selected programs to be watched at the customer’s convenience. However, Smithsonian Networks changed its product strategy to a high-definition (HD) linear channel with continuous programming running 7 days week, 24 hours a day, with a complementary “on-demand” service to follow. A linear channel is the standard television service where viewers watch a scheduled TV program on a particular channel at a specific time. The Smithsonian Channel launched in September 2007 as a linear channel in HD. An on-demand service launched in March 2008.

Smithsonian Networks produces and acquires programs to be aired on Smithsonian Channel. The Smithsonian created an Institution-wide Networks Review Committee to oversee reviews of program content for their factual accuracy and to ensure they meet the Smithsonian’s reputational standards. This committee also evaluates program ideas generated annually by curators and other Smithsonian staff to determine which are of particular interest to the Smithsonian. These ideas are submitted to the Networks and the

¹ The non-compete clause applies to programs for a television audience and does not apply to feature films for theatrical distribution.

Networks is contractually obligated to select up to 15 programs to produce each year based on program proposals submitted by the Smithsonian. As of December 31, 2008, the Smithsonian Networks Review Committee had reviewed 262 Networks programs.

Smithsonian Networks has agreements with numerous distributors, including major providers such as Time Warner Cable, Direct TV, and Verizon. In 2008, Smithsonian Channel won an Emmy Award from the National Academy of Television Arts and Sciences and was nominated for two additional Emmy Awards.

Many offices throughout the Institution are involved in the administration of the contract, including Smithsonian Enterprises; the Under Secretary for History, Art, and Culture; the Office of Public Affairs; the Office of Contracting and Personal Property Management; the Office of General Counsel; and staff in the Museums. The Smithsonian established new positions, the Smithsonian Coordinators and the Contract Administrator, to oversee compliance with the contract.

RESULTS OF REVIEW

Processing of Third-Party Film Requests

Even before the existence of the contract, the Smithsonian already had processes and procedures in place for reviewing and approving requests by third-party filmmakers to use Smithsonian content in their films. After entering into the contract, the Smithsonian updated the procedures for processing and approving such requests. To assure that, in addition to other museum considerations, these requests are evaluated consistently with the non-compete clause of the contract, the Smithsonian added a step to the process by introducing a central review committee overseen by the Office of Public Affairs (OPA). OPA coordinates public relations and communications in conjunction with museums, research centers, and offices.

Film requests for academic and non-commercial programs, or for programs involving only incidental use of Smithsonian content, are a few of the types of programs that fall outside of the non-compete restrictions and are permitted.

Film Request Review Process

For third-party producers wishing to film at the Smithsonian or use Smithsonian content in the film, the Smithsonian relies on a two-stage review process. The first review examines whether requests are appropriate and consistent with the Smithsonian's overall filming policy and whether museum staff has the resources to cooperate with the project. If the request passes that review, the second review determines whether it is permissible under the non-compete terms of the contract.

For filming requests, the filmmaker or independent producer submits an online application to the museum public information officer (PIO) where they expect to film.² The application asks for a brief description of the program to be produced, the content, length of time they expect to film, film crew numbers, estimated length of the Smithsonian content in the completed program, the distributor, and other relevant information. The museum's PIO reviews the application and consults with curatorial staff to determine whether the request is appropriate and consistent with the Smithsonian's filming policy and whether the museum has the resources to cooperate. Long-standing considerations for determining whether the request is appropriate and consistent with policy include: consistency with the Smithsonian's mission; appropriate use of Smithsonian facilities, collections, and staff resources; whether costs are reasonable; availability of relevant staff; and whether the intended use may negatively affect the Smithsonian's reputation.

If the PIO concludes that the film request is consistent with Smithsonian filming policy, he or she forwards the request to the OPA Review Committee, which consists of two representatives from OPA and one museum representative. The OPA Review Committee, in consultation with the contract administrator, reviews requests using three additional criteria and decides whether the use of Smithsonian content in each proposed film is allowable under the non-compete clause in the contract. These criteria include whether the programs:

- are academic, curriculum-based, or scholarly programs;
- will be distributed by non-commercial distributors; or
- are programs with only incidental use of Smithsonian content.³

The OPA Review Committee accepts requests that meet any of the three criteria.

In determining if a request is for more than incidental use, the OPA Review Committee considers a number of factors, among them: the total run-time of the film; the estimated time for Smithsonian content; and how many other organizations or experts are participating in the program.

For those requests that do not meet any of the criteria, the committee may recommend to the Under Secretary for History, Art and Culture to approve the film request as a one-off exception, as authorized under the contract. The OPA Review Committee also confirms that the Smithsonian has not exceeded the annual allotment of one-offs. See Appendix B for a detailed flowchart describing the filming application process.

² Requests for non-recurring news and public affairs purposes do not require an application.

³ Smithsonian content includes collections, exhibitions, archival and research materials, publications, audiovisual works, Web-site content, and other works of authorship; and Smithsonian personnel, events, and buildings and grounds.

Film Request Decisions

Based on our review of selected decisions regarding film requests made from January 1, 2006 through December 31, 2008, we believe that the contract has had a minimal impact on third-party filmmakers who want to use Smithsonian content in their programs. During that period, the Smithsonian received approximately 446 film requests. It declined only two requests because of restrictions in the contract.⁴ The Government Accountability Office identified these two requests in its December 2006 report ***Additional Information Should be Developed and Provided to Filmmakers on the Impact of the Showtime Contract***. There have been requests that did not satisfy any of the three criteria used by OPA's Review Committee (academic, non-commercial, and only incidental use), but the Smithsonian has been able to accommodate them through the one-off allotments. The Smithsonian has accepted 14 requests for one-offs. The table below identifies decisions made by the OPA Review Committee and museum PIOs:

Table 1: Filming Request Summary January 1, 2006 through December 31, 2008				
Decision Made	2006	2007	2008	Total
Accepted	57	92	112	261
Accepted as a One-Off	4	5	5	14
Declined (unrelated to the Contract) ⁵	37	21	17	75
Declined (because of the Contract)	2	0	0	2
Withdrawn or Closed	34	23	19	76
Pending	<u>0</u>	<u>3</u>	<u>15</u>	<u>18</u>
Total Requests	<u>134</u>	<u>144</u>	<u>168</u>	<u>446</u>

Adequacy of Documentation and Guidance to Filmmakers

The Smithsonian has not declined any film requests because of contract restrictions since August 2006. Consequently, there was no need to assess the adequacy of the documentation to support decisions to deny filmmakers use of Smithsonian content due to the contract. All the same, we did assess the overall adequacy of the documents and records supporting a sample of film requests. We included requests that the Smithsonian declined for reasons unrelated to the contract, were withdrawn, or were accepted.

⁴ One request was for a one-hour show, focusing entirely on the Smithsonian, and the other was a proposal for a partnership with the Smithsonian on a children's series. In one instance the Institution had not fully implemented procedures for reviewing third-party requests. In both cases there were no written applications on file. Under the current system, the Smithsonian would have required that an application be submitted and it might have considered these two requests under the one-off option.

⁵ Reasons for denials at the museum level unrelated to the contract include issues regarding availability of collections or staff or the appropriateness of the request.

We believe the Smithsonian has adequate documentation to support its decisions. Based on our review of a selected sample of third-party film requests, we determined that the Smithsonian has improved its process for documenting its decisions since the inception of the contract. OPA centrally monitors and tracks decisions on an Excel spreadsheet. The museum PIO maintains files for each film request, which include applications, emails, contracts, and other correspondence. In addition, OPA maintains files on all approved film requests.

OPA has also improved the information available on its public website, including information for filmmakers about the contract. OPA has included descriptions of the factors for determining more than incidental use in the Frequently Asked Questions (FAQs) document on its public website. Additionally, the Smithsonian has added an electronic application process as well as updated the fact sheet that provides an overview of the Smithsonian Networks programming and how the contract affects filmmakers' use of Smithsonian content.

Financial Analysis

Revenue from Smithsonian Networks Contract

The Smithsonian's revenues from the Smithsonian Networks Contract for the period January 1, 2006 (the effective date of the contract) through December 31, 2008, were in accordance with the minimum guarantee in the contract.

Costs and Revenue Sharing

Museums and offices throughout the Institution support the Smithsonian Networks contract. They include: Smithsonian Enterprises; Office of Contracting and Personal Property Management; Office of Public Affairs; Under Secretary for History, Art, and Culture; and staff in the museums, research centers, and offices. The Smithsonian developed a revenue-sharing plan to distribute revenue received from Smithsonian Networks to cover costs and to distribute the remaining balances to the Central Trust⁶ and to the Units (museums, research centers, and offices).

Under the revenue-sharing plan, annual licensing and other fees received from Smithsonian Networks are split evenly between the Central Pool and the Unit Pool. For both funding pools, revenues are first distributed to cover the costs incurred to support the contract and then the remainder is distributed to the Central Trust and to the Units. See Appendix C for a flowchart of this cost-recovery and revenue-sharing process.

⁶ The Central Trust is managed centrally by the Office of Planning, Management and Budget.

Central Pool – The Central Pool is distributed as follows:

- Smithsonian Enterprises and Smithsonian Operating Costs - The Central Pool is first used to finance the costs of Smithsonian Enterprises and Smithsonian central offices to administer and manage the contract. Smithsonian Enterprises operating costs included outside legal fees related to the creation of the contract, financial staff salaries, rent, and shared services allocations. Smithsonian-wide operating costs included the following:
 - Office of Contracting and Personal Property Management – Costs included a portion of the salary and benefits of the Smithsonian Contract Administrator in the central Office of Contracting and Personal Property Management. The contract administrator is responsible for ensuring the Smithsonian Networks’ compliance with financial and other administrative terms of the contract.
 - Office of Public Affairs – Costs included the salary and benefits of a public affairs liaison in the Office of Public Affairs to accompany filming crews at Smithsonian location shoots. These OPA costs stopped in early FY 2008 because the museums’ staff assumed this function.
 - Chairman, Smithsonian Networks Review Committee – This allocation was to reimburse the Center for Folklife and Cultural Heritage for the services of its Director as the Chairman of the committee. This Institution-wide committee oversees the administration and review of Smithsonian Networks programs and evaluates program ideas generated by curators and other Smithsonian staff for annual submission to the Networks.
- Residual to the Central Trust Budget – The Office of the Comptroller transfers the residual amount at year-end to the Smithsonian Central Trust. This fund is an unrestricted trust operating fund. The Smithsonian spends the unrestricted funds on general management and administrative costs and program costs.

Unit Pool - The Unit Pool is distributed as follows:

- Content Review and Filming Location Fees - Smithsonian Enterprises submits requests to the Office of the Comptroller to distribute money, when applicable, to the units based on two sets of fees: standardized content review fees and filming location fees. Smithsonian curators conduct content reviews, checking the programs produced or acquired by Smithsonian Networks for factual accuracy. The Institution established a fee schedule for these reviews based on the length of the program. The Smithsonian pays content review fees directly to the reviewer’s department. The money is deposited to unrestricted unit fund accounts. The units use these unrestricted funds for collections care, office supplies, equipment, travel for conferences, professional associations, and research.

Filming location fees are based on the number of hours of onsite filming by the Networks. The units generally use the money from location fees to pay salaries of staff in the museum public affairs offices who accompany filming crews.

- Balance for Revenue-Share Distribution - At the end of the year, the Smithsonian Networks Review Committee distributes the remainder of the unit pool to the units based on participation in program development and production. Smithsonian staff may participate in informational discussions or standard consultations with the Networks producers in the development of a program.

For the period January 1, 2006 through December 31, 2008, the Smithsonian covered all Central and Unit pools costs, and had funds left over to distribute to the Central Trust and to the units as a revenue share. In addition to the licensing and other fees the Network reimburses the Smithsonian for certain additional operating and business costs.

The Smithsonian also received advertising revenue which is not part of the revenue share. On October 29, 2007, the Smithsonian entered into an Advertising and Amendment Agreement with the Networks. This Amendment gave the Smithsonian the right to sell and retain the revenue from a portion of the advertising on the Channel as well as on the Networks and Smithsonian websites. Advertising revenue is tracked by the Magazine Division of Smithsonian Enterprises and any net gain from advertising passes through to the Central Trust budget.

In our opinion, the Smithsonian has adequate procedures for tracking costs of administering the contract. Costs are tracked in the Smithsonian Enterprises accounting system under a separate accounting unit code, and Smithsonian-wide costs are tracked in the Smithsonian central accounting system using separate designated accounting codes. Also, the Smithsonian Coordinators review all invoices submitted by the units and track the total fees for content reviews and location filming. Quarterly, Smithsonian Enterprises submits the invoices to the central Office of the Comptroller, which prepares internal transfers to the units. For reimbursable costs, Smithsonian Enterprises invoices the Networks quarterly for certain operating expenses. The Smithsonian Contract Administrator reviews these expenses for reimbursement.

Based on our interviews and our review of income statements, transaction listings, internal spreadsheets, and invoices, we believe that the Smithsonian has accounted for all significant costs. We found no other financial costs from the implementation of the contract provisions that might have reduced net proceeds to the Institution.

Actual Revenue Received Thus Far Versus Original Business Plan

Under the contract, the Smithsonian receives a guaranteed annual payment and a share of Networks revenues when gross revenues exceed a stipulated amount. During our review period January 1, 2006 through December 31, 2008, the Smithsonian received the guaranteed annual payment, in accordance with the contract. However, the Networks has

not generated the additional revenue that was projected in the initial five-year business plan included in the contract dated December 22, 2005, and so the Smithsonian has not yet received additional payment beyond the guarantee.

There were at least three factors that contributed to the Networks not generating additional revenue. First, the contract took five months longer than anticipated to complete, but the business plan was not adjusted to reflect this delay. Second, the negative publicity in connection with the announcement of the joint venture resulted in delays in launching the Channel.

Finally, the Networks changed its product strategy, which was agreed to by the Smithsonian. The initial business plan anticipated that the Networks would offer an on-demand service first, to be launched in July 2006, and projected that the Smithsonian would start receiving additional revenues above the guarantee in 2007. However, Smithsonian Networks changed its product strategy to an HD linear channel with continuous programming 7 days a week, 24 hours a day, with a complementary “on-demand” service to follow later. Linear channels require more programming than on-demand channels, and therefore Networks needed more time to develop these programs.

The Smithsonian was advised of the product strategy changes in the Smithsonian Networks Management Committee meetings and through annual budgets submitted by the Networks. Because of these changes, the parties agreed to delay the launch date. Smithsonian Channel was launched in September 2007 as a linear channel in HD. An on-demand service launched in March 2008. Consequently the Networks’ gross revenue did not reach the amount originally projected. Given these factors, which delayed the launch date and the revenue share, comparisons to projections in the original business plan are difficult.

APPENDIX A. Scope and Methodology

We reviewed third-party film requests and contract-related costs and revenues for the period January 1, 2006 (the effective date of the contract) through December 31, 2008.

We interviewed management and staff from Smithsonian Enterprises, including the Smithsonian Institution Coordinator, the Media Group General Manager, and the Controller. We also interviewed the General Manager, Smithsonian Networks. We interviewed the Under Secretary for History, Art and Culture, and management and staff from the Office of Contracting and Personal Property Management, the Office of Public Affairs (OPA), the Office of General Counsel, and the Office of Planning Management and Budget. We also interviewed museum Public Information Officers (PIO) and curators at the National Museum Natural History (NMNH), the National Museum of American History (NMAH), and the National Air and Space Museum (NASM).

We detail below how we reviewed the Smithsonian's processing of film requests and how we conducted our financial analysis of contract-related costs and revenues.

Processing of Film Requests

To determine if the Smithsonian had adequate policies and procedures in place for making decisions on accepting or declining third-party film requests we reviewed the Smithsonian's filming request policy, FAQs, Fact Sheets, the Government Accountability Office Report on the Showtime Contract (dated December 2006), and the Smithsonian Networks contracts and associated amendments.

To identify the total universe of film requests, we obtained three spreadsheets from OPA, which contain all requests received between January 1, 2006 and December 31, 2008. Using these spreadsheets we identified a total of 446 filming requests. For these filming requests, the Smithsonian made decisions to accept, decline, withdraw or close these requests. For some requests where additional information was needed the Smithsonian put them in a pending status.

We judgmentally selected 28 requests from the top 3 museums: NMNH, NASM, and NMAH. These three museums were responsible for 55% or 247 film requests and included the various types of decisions identified in the OPA spreadsheets.

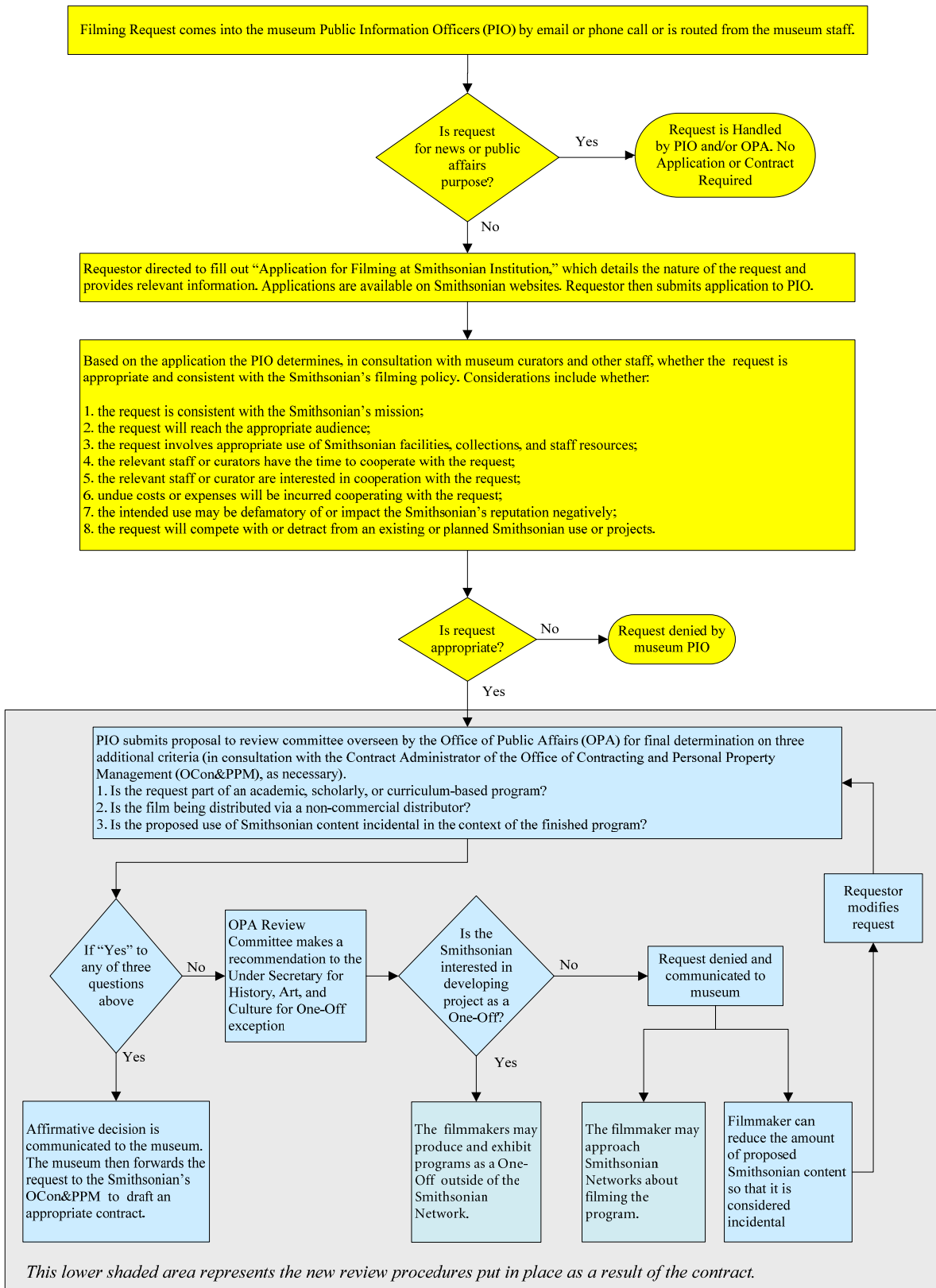
Since August of 2006 we found no additional instances where Smithsonian declined requests because of the contract and therefore, there was no need to assess the adequacy of the documentation to support this type of decision. However, we did assess the adequacy of the documents and records supporting a sample of other decisions, including accepted, accepted as a one-off, declined for reasons other than the contract, and withdrawn or closed. We focused our review by selecting a sample of requests from the five types of decisions: 3 accepted, 3 accepted as one-offs, 10 declined for reasons other

than the contract, 2 declined because of the contract (decisions from April and August 2006), and 10 withdrawn or closed. For this sample we reviewed the museums' filming request files as well as OPA files to determine whether documentation existed to support the decisions.

Financial Analysis

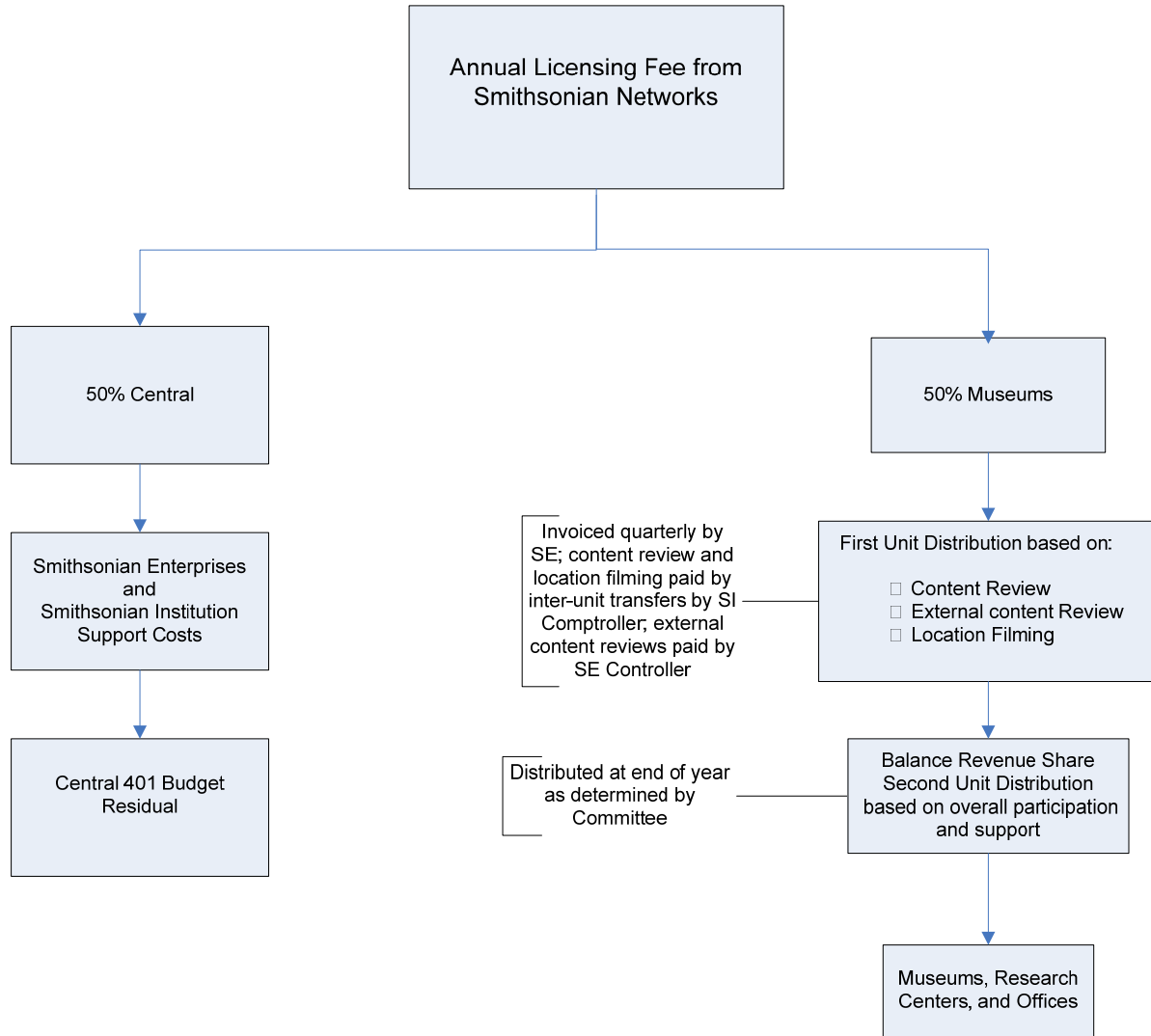
To evaluate revenues and costs, we reviewed the contract and associated amendments and clarification agreements. We reviewed internal compliance reports, payment schedules, invoices, and copies of checks. We reviewed Smithsonian Enterprises income statements and general ledger transaction listings, as well as detailed spreadsheets of unit content review and location filming fees. We reviewed relevant budget documents, including decision papers, allocation history sheets, and transfer reports. We reviewed administrative memoranda on revenue-share procedures and quarterly and annual revenue-share schedules. We reviewed income statements, annual budgets, and long-range plans from Smithsonian Networks. We reviewed minutes of the meetings of the Smithsonian Networks Management Committee.

APPENDIX B. Smithsonian Filming Application Review Process Chart



Source: This flowchart is an updated version of the flowchart in the December 2006 GAO report.

APPENDIX C. Financial Flow Chart



APPENDIX D. CONTRIBUTORS TO THE REPORT

The following individuals from the Smithsonian Office of the Inspector General contributed to this report:

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