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Thomas O. Maggs

December 20, 2004

Mr. Paul Laudato
Chief Counsel
New York State Office of Parks, Recreation and Historic Preservation
Empire State Plaza
Agency Building 1
Albany, New York 12238

Dear Mr. Laudato,

In compliance with your request, enclosed with this letter please find the responses to the several findings contained in your Preliminary Audit Report dated November 22, 2004.

The Board understands the concerns of OPRHP and appreciates the time spent and the effort taken to complete the audit report. A Committee of the Board was established to review the audit. The Committee studied closely the Managerial Review and found many worthwhile suggestions and recommendations that the Board will implement, as is stated further in our responses.

Looking forward, we believe that the principal findings of the audit are three:

1. That the current president is paid at the higher end of the scale for arts related non-profit organizations;

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2. That SPAC needs to significantly increase its unearned revenue in order to continue to present the New York City Ballet and the Philadelphia Orchestra; and
3. That governance by the Board should be transparent and in conformance with current best practices and the principles of Sarbanes-Oxley.

The Board agrees with these findings. Many of these suggestions made in the audit report are already in process. With regard to the above findings, please be advised of the following:

1. The current president is prepared to resign immediately pending the execution of a new severance agreement. The Board is committed to complete this negotiation as soon as possible. It is the express intention of the parties that the new severance agreement be negotiated in consultation with appropriate government officials.
2. It is anticipated that a new president will be selected by the Board within ninety days and will be prepared to immediately take over effective leadership of SPAC. The employment terms of the new president's contract will provide clear, measurable, and ascertainable goals in line with the pressing needs of the organization. The Board, in consultation with the new president, intends to review the mission/vision statement of SPAC and formulate a near term business plan to effectively deal with the challenges confronted by SPAC.
3. The Board confirms its commitment to good governance that is transparent and in line with current best practices. The Board through its governance committee had earlier this year begun a review of its own organization and structure. An independent Audit Committee was formed. The committee structure will be reviewed to be sure that each plays a significant role in


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furthering the mission of the organization. A new Whistleblower Policy was adopted and the Records Retention Policy was formalized. The Conflicts of Interest Policy will be reviewed and amended as recommended in the findings.

We all know that the arts in America are in turmoil. It seems each week we read about another orchestra or ballet announcing a shortened or cancelled season. Some companies have filed for bankruptcy. This is the social and financial environment in which SPAC is operating. Good governance is first and foremost, responsible governance; i.e. governance responsible to those who perform at SPAC, to the supporters, patrons and audience of SPAC and to this Region. This requires the organization to be in a firm financial position. The Board takes this responsibility seriously. The Board, an unpaid board, has been relentlessly committed to providing this region with the best in performing arts and to responsibly evaluate where SPAC is today and where it will be in the future.

The Board is firmly in charge of this organization and is charting a path for its future. We are prepared to move forward in a cooperative effort with OPRHP but firmly believe that cooperation must begin now. The Board sees no advantage in engaging in a protracted audit process or debate to question or confirm a set of findings with which the Board essentially agrees. Rather the Board would invite the parties to engage in dialectic on the assumption that we share a vision for this great institution and are truly motivated to maintain SPAC in its rightful place as the preeminent arts center in upstate New York.

Sincerely,



Stephen M. Serlin
Chairman

Findings & Recommendations

Set forth below please find the responses to the Executive Summary of your Preliminary Audit Report dated November 22, 2004

1. SPAC's financial difficulties are the result of inadequate fund raising and outside support.

The Board understands the need for fundraising. It fully realizes the need to increase the unearned income of the organization. It recognizes the need to add to the endowment and to build the fund to one of at least \$10,000,000. The Board is currently interviewing candidates and will hire a new President/Executive Director of SPAC within the next ninety days. The new President/Executive Director will have extensive and proven fund raising experience and ability. A fundraising committee will be formed and new programs with emphasis on established goals will be put in place to improve and enhance all fund raising efforts. All fundraising programs will be instituted consistent with a Long Range/ Strategic Business Plan to be developed in consultation with the new president and approved by the Board. The Board intends to advance the mission of SPAC by working with the broad community of patrons and supporters to improve SPAC's public image and to maximize its fundraising efforts.

2. The decision to eliminate the New York City Ballet was flawed and was presented based on inaccurate and incomplete information.

SPAC's initial decision to change the dance program was made as a result of the large deficits incurred in presenting the New York City Ballet programs. It was never the Board's intention to eliminate dance at SPAC, rather, consistent with its mission, the Board sought to create more variety in the dance programs in the hope of appealing to a broader segment of the SPAC audience and to do so with a significant reduction in cost. It was the Board's intention to attempt to present the New York City Ballet in rotation, each third year. The decision to change the dance program and not the orchestra was based in part on the belief of the Board that while there were several dance companies of national reputation that could perform with distinction at SPAC the same could not be said of a replacement for the Philadelphia Orchestra. Additionally, orchestra members staff the very successful Chamber Music Series at SPAC. While the preliminary audit questioned the methodology use by SPAC to calculate the losses attributable to the ballet, it is clear, by whichever methodology is used, that both the ballet and the orchestra require significant underwriting. The Board is committed to maintaining the New York City Ballet and the Philadelphia Orchestra at SPAC. However to succeed in this goal, the Board understands that revenues, both earned and unearned, must be improved from all sources and expenses must be controlled in all areas.

3. The President, an employee of SPAC, does not perform at the level commensurate with his compensation. The duties of the SPAC President and its Director of Development should be clearly defined, performance goals established, and compensation awarded based on attainment of those goals, commensurate with similar positions in like organizations.

The Board understands that SPAC's President is compensated at the higher end of the scale for arts related non-profit organizations. Mr. Chesbrough has been employed by SPAC for more than

33 years, 27 of those as president. In addition to his duties as president, Mr. Chesbrough has functioned as the program director and administrative director; additional job responsibilities that in many of the benchmark companies are performed by individuals other than the president. The Board believes that any comparison to benchmarks should take both tenure and responsibility and function into consideration. The Board relied on compensation consultants at the time the contract was entered into and subsequently when the compensation was questioned. Although the audit questions the conclusions reached by these consultants, the Board relied on these consultants when approving the contract. The Board will hire a new President within the next ninety days whose compensation will be determined by reference to benchmarked surveys prepared by independent compensation consultants.

4. SPAC needs to reaffirm its mission and commitment to the fine arts.

The Board remains committed to the original mission/vision of SPAC. The Board understands the need to review its business plan in light of the changes and challenges facing all arts organizations in America today. The Board will strive in every way possible to continue residency of the New York City Ballet and the Philadelphia Orchestra at SPAC. It is understood that this will require significant financial support from all constituents within the SPAC community, including patrons, businesses and government. The Board strongly agrees with the finding that SPAC's partnership with the State and the OPRHP is fundamental to SPAC achieving its mission, a partnership that would insure that funding is available from OPRHP to bring the SPAC facilities to a state of good repair as is required by the lease agreement and one that would encourage the State to provide significant and sustained annual operating support. The Board will endeavor to increase the unearned income of SPAC through comprehensive and well-executed fund raising programs. The Board will study expanding the SPAC season not only in length but also in the breadth of the artistic offerings in order to further integrate SPAC into the cultural fabric of the Region.

5. The Board of Directors needs to expand its oversight and management roles in the operation of SPAC and reach out to its community of patrons, members, and supporters.

The Board is expanding its oversight and management roles and has established a Governance/Nominating committee that is reorganizing the Board and committee structure in line with current best practices and in accordance with the principles of Sarbanes-Oxley. The Board currently has the following Committees: Executive, Audit, Campaign, Investment, Compensation, Governance/ Nominating, Long Range Planning, Museum of Dance, Retirement, Search, Marketing and the Action Council. A qualified Board member heads each committee. The Board is committed to transparency consistent with responsible governance. SPAC is one of the very few organizations that invites the media to its board meetings. The Board understands its role as the ambassadors of SPAC and the need for connection with and presence in the community. The Board believes, however, that the President and the Board Chair must be the principal spokespersons for SPAC. The Board agrees with the recommendations regarding board size and continues to actively seek new members to aid it in furthering the mission of SPAC.

6. The Severance Agreement for SPAC's President as approved by the Board of Directors on November 15th, 2004, is excessive and should be reconsidered.

The Severance Agreement could not be read without reference to the existing Employment Agreement. Absent a severance agreement, the termination of the President arguably entitled him to the full payout of his current contract. The Severance Agreement negotiated between the parties was evaluated by Mercer Human Resource Consulting, an independent consulting firm, and provided for a payout less than the existing Employment Agreement. This issue is moot, however,

in that the Severance Agreement was terminated by agreement of the parties on December 14th, 2004. A new severance agreement will be negotiated between the parties in consultation with appropriate government officials.

Preliminary Audit Report

Set forth below please find the responses to your Preliminary Audit Report dated November 22, 2004.

1. Record Keeping and Security

The Board this year adopted a Records Retention Policy consistent with the principles of Sarbanes- Oxley. The Board will adopt a security policy dealing with records and use of computers and the Internet. The security policy will include a direction that all SPAC management and employees change their security password every 90 days.

2. Staff and Organization

The Board will direct the incoming President to develop job descriptions for each staff position with clearly identified objectives and responsibilities.

3. Financial Management Practices

The President's expense account will continue to be approved as a separate line item in all future budgets. This account will be reviewed periodically, at the Board level, to assure compliance with both record keeping requirements and budget limits. The Board recognizes that separation of duties in handling of financial transactions is a basic principle of financial management and in this regard it should be noted that nothing came to the auditor's attention that would lead them to believe that there were significant internal accounting control deficiencies.

4. Minutes of Meetings of the Board of Directors

The Board of Directors will approve a policy to announce regular board meetings with a proposed agenda at least 7 days in advance. Minutes of the meetings will be distributed within 30 days of the meeting. The Board agrees to include more details as to discussion and Board decisions.

5. Procurement - Payments to/for Individuals

SPAC will develop a policy that precludes donations to charitable organizations unless approved in advance by the Board of Directors. All such donations will be made in the name of SPAC.

6. Competitive Bidding and Best Value Procurement

The Board will re-evaluate current practices and establish a policy to consolidate purchasing and confirm its procurement policy whereby several proposals are received for all material purchases of goods or services. The Board will also review its current conflicts of interest policy and amend it to require compliance with the Intermediate Sanctions Rules and to be consistent with the principles of Sarbanes-Oxley. This policy will apply to all new contracts and services. Further no staff members may receive any compensation from any firms associated with any Board member.

7. SPAC President's Expense Account

The Board agrees that only expenses incurred to advance the mission of SPAC should be reimbursed and that adequate records must be maintained to evidence compliance with this policy. Please note the response to items 3. and 5. above.

8. Duties and Compensation of the President of SPAC

Please refer to the response to the 3rd Finding of the Preliminary Audit Report.

9. Decision Making and Accountability to the Public

SPAC's by-laws provide that OPRHP may appoint two members to the board of directors. Recently, OPRHP has appointed its second representative. These representatives serve as full voting members of the Board and consistent with the Board's current practice it is understood that these board members will continue to have representation on key committees, including any committees on which either representative may choose to serve. One representative currently sits on the Search Committee that will select the incoming president. The Board agrees governance should be transparent and intends to make use of the media and its website to keep the public fully informed. Members of the media are invited to attend all Board meetings. Each year SPAC's books and records are audited by an independent certified public accounting firm that has in the past rendered an unqualified opinion. At no time has SPAC engaged an accounting firm with ties to SPAC or members of the Board.

10. Financial Data Used in Support of the Ballet Decision

Please refer to the responses to the 2nd and 4th Finding of Preliminary Audit Report. The Board agrees that all decisions must be made based on full and complete financial information.

11. SPAC needs to continue to use independent, outside auditors. SPAC should expand the number and types of audits, to include performance audits encompassing different program areas.

The Board acknowledges that SPAC has always used independent, outside auditors and will continue this practice. The Board will retain a new audit firm for the year-end 2005 to conduct a certified audit of the operations of SPAC in accordance with all professional standards.

12. Board Independence

Please refer to the response to the 5th Finding of Preliminary Audit Report. Also, please note response to item 6. above.

13. Box Office Practices

Some cash payments are contractually required by touring acts. All such cash transactions were documented. The auditors were informed of this, but chose not to review the documentation. This documentation remains available for examination. The Board will continue its policy of strict accounting when such cash transactions are contractually required.

14. Fundraising Events.

Income from fundraising events are shown on two separate line items, one as income earned on the event and the second as event related contributions. The Board believes that the auditor's conclusion that certain fund-raising events lost money resulted from the auditor's failure to include the contribution income portion of the special events. The Directors understand that it is important to continue fund raising events such as the Ballet Gala, Wine Festival and other events to be determined. These events must continue to be successful and the Board will review all fund-raising proposals and outcomes annually.