Innovations in Financial Structures

Roche Schulfer (Executive Director, the Goodman Theatre), moderates a panel with Itamar Kubovy (Executive Director, Pilobolus), Susan Medak (Managing Director, Berkeley Repertory Theatre), Michael Robertson (Managing Director, Lark Play Development Center) and Zannie Voss (Chair and Professor, Southern Methodist University)

Roche Schulfer:
Hello, everybody. I’m Roche Schulfer, executive director at the Goodman Theatre. Welcome to the final panel of the day. And given the enviable task of having the last in a daylong group of panels, and with a title of Innovations in Financial Structures, we decided to fool you all into paying attention by saying that what we’re really going to talk about is money, money…yes! We figured at this point that after talking for a day about money in the abstract with a bunch of managers and trustees that we would talk about money in the specific.

What we hope to do in the time we have allotted today is to shed some light on the origins of what is considered the traditional business model or financial structures for not-for-profits—the model that has evolved over the last 50 years or so. What we want to talk about is the revenue streams that we all have available to us and what is the appropriate balance between ticket sales, concessions, other sources of earned income, annual support, endowment support, rentals, etc. The notion being that a financial structure, a business model, a budget is really a tool—a means to an end—and that end should be how to generate the maximum resources for the mission of our theatre and to figure out how to get the most from those resources that we possibly can. So we’re going to look at some of those traditional assumptions about how much you should earn at the box office and what role endowment should play, and see if those expectations are reasonable today.

Susie and I will talk about some of things that we’ve been talking about at our institutions; both Berkeley Rep and the Goodman are on the larger end of the spectrum, but we think that there are similar questions being asked at theatres large and small. Zannie will provide prospective on the field, given her extraordinary work with Theatre Facts over the years, which really is one of the best repositories of industry data in any arts industry, at this point. And Michael and Itamar will talk about the very different ways that their companies operate—ways that have turned the traditional models on their head. Then we’ll have a discussion with you that will be absolutely thrilling. (Laughter.)

I’m going to start with a little bit of context about how we got to where we are. The not-for-profit theatre in this country is really a new phenomena—only 50 years old or so. We were talking earlier at lunch about symphonies, museums and opera companies, and that they tend to have been around a lot longer. So theatre, relatively speaking, is a new industry. Although someone pointed out that 50 years is still a good period of time to begin to analyze, and look at how we operate, and see if the models that we’ve adopted
are valid, and how they might be changed or should be changed. Obviously, the
movement began with a group of artists and theatre professionals who wanted to get out
of the pressures of commercial theatre in New York and go to communities across the
country to create ongoing companies that were freer than the commercial pressures of
Broadway. They wanted to do classics, revivals, things that didn’t have a ready audience
in the commercial theatre. And they wanted to operate in a way that they would charge
prices to their audiences that were less than commercial theatres—mainly through the
sale of season subscriptions.

The model for our industry really evolved, to a large extent, out of the work of William
Baumol and William Bowen in Performing Arts: The Economic Dilemma, from back in
the 1960s, which was, parenthetically, one of the reasons that I go into the business. I
was a drifting college student who enjoyed going to theatre. I was in the library one
day—I was an economics major—and I saw a book whose title included the words
“economics” and “performing arts,” and I thought: “That’s it, that’s what I can do. I’m an
economics major and I like to go to theatre.” I stole the book from the library—yes, I did.
(Laughter.) I stole it because I couldn’t find any place to buy it. I sent a contribution and a
letter to the university years later, but enough about my neurosis…

Anyway, Baumol and Bowen, for the first time, articulated the dilemma facing the live
performing arts—and Zannie can do this part by heart, but I have to read it. Since
inflation reflects productivity gain in the larger market and since productivity gains in the
arts industry are limited (for example, technological advances can’t cut the amount of
rehearsal time you need); and since the industry is labor-intensive (for example, you can
do so many performances and you need a certain amount of actors unless you don’t go
beyond one-man shows); a greater rate of cost increase occurs than in the overall
economy. So we’re always faced with an industry where costs are rising faster than the
price rise in the overall economy. They really made a case in their book for subsidy for
the performing arts as an ongoing need, particularly in regards to ticket prices and
access to performing arts—it has to be affordable to a general audience. Now, over the
years, certain rules or standards have evolved about the financial model for not-for-profit
theatres, and almost all of us who worked in this industry grew up with these rules.

When I started at the Goodman Theatre years ago, it was basically understood that we
needed to earn 60 percent of our total budget at the box office. I just accepted that as a
given and operated and managed on that principle. Now, across the industry that’s
tended to be a certain norm. In other words, we all operate with the notion that in larger
institutions, 50 to 70 percent of your budget should come from ticket sales. And I guess
one of the things that we want to talk about today is that we don’t know exactly when
Moses came down from the mountain with a tablet that read that was the way it should
be. In other words, how did that become a measure for success as opposed to part of an
overall analysis of your financial operation, your mission and your priorities? This is what
we want to get into today. We want to reexamine the expectation that market forces are
driving ticket pricing strategies in a way that is disconnected from the mission and values
of our organizations. Are we effectively pricing ourselves out of the marketplace? Susie,
who are those consultants who came and talked at the LORT meeting?

Susie Medak:
Genovese Vanderhoof and Associates.

Shulfer:
They talked about the fact that, over the course of time, we were pricing ourselves out of the marketplace and that we were not connecting the demand for our product with the price we were charging for our product. The bias was toward the fact that we needed to raise a certain amount of revenue for our product, and we can’t raise enough money through annual support, so we have to do it through the box office.

In general, our premise is that revenue stream goals are both mission-based and market-based; in other words, are you looking at the budget for your organization, looking at your mission and looking at your community—the market that you’re serving? Instead of there being one rule of thumb about how much you should be earning at the box office, really what’s implied from all of this is that almost every organization should have a different financial model. There will be some organizations where they’re earning 50 to 60 percent or more and it’s perfectly logical, rational and appropriate. There will be other organizations where 10, 20, 30 percent may be what can be expected. Peter Gelb talked last night about the fact that the Metropolitan Opera achieved 40 percent of its budget through ticket sales. I thought, that would be great if I only had to get 40 percent of my budget from ticket sales—I would have so much more support for the work that we do on stage. The thing we want to put out there for people to think about is this notion of what is appropriate in terms of ticket sales, annual support, endowment… These are arbitrary notions that should and will vary from institution to institution.

I’m going to talk now about some of the things that we’re doing at the Goodman. I should preface this by saying that there are a number of things that we’ve done over the course of time that have put us in a position of having created a solid artistic and financial base over the past 20 years, and I’ll mention them to create a context for a future discussion rather than as an advertisement for ourselves. When Bob Falls became artistic director, there was one priority that he had and that was to diversify the artistic direction—and I’m not talking about cultural diversity at this point, rather, I’m talking about aesthetic diversity. He brought in and we paid a group of artists with a variety of aesthetic points of view, and they became resident artists at the Goodman. And to some extent, the sum total of their vision became the vision for the Goodman Theatre. This was based on the belief that the Goodman wanted to have as many aesthetic points of view on stage as possible, and Bob has been extraordinary in his willingness to embrace artistic points of view about which he’ll be the first to say, “I don’t get it.” When Mary Zimmerman came in and said, “I have an idea about dramatizing *The Notebooks of Leonardo Da Vinci*. I don’t have a script. I can’t tell you how I’m going to do it, but I think it can work,” Bob said, “I don’t know what you’re talking about but we’ll do it. We’ll back you and support it.” From the artistic leadership there’s been a real generosity of vision and a real attempt to embrace artists who have aesthetic points of view that may not be familiar to the artistic director. And this, I think, has been a big thing—this in essence is not a model about how you should conduct business but it is a reflection of how we approached the artistic process.

The other key element began back in the late 1970s. We made the decision that cultural diversity was going to be the fabric of our institution—simply because we exist in a community that is very culturally diverse. We didn’t think we were coming up with something remarkable at that point; we just thought that theatre is about community and the issues from that community should be reflected on stage and the people from that community should be reflected on stage. That has grown over time, and diversity is the fabric of the organization, and in the future, no one will be able to change that. We’re very proud that that occurred. I can say that there are organizations in Chicago that point
to us and say that we’re a great example of diversity initiatives. It’s not an easy thing to do and we’ve always said that we were very grateful that we did this at a time before it became kind of current. Because if we were held to the metrics that others are held to today—for instance, “Here’s a grant for $100,000; in three years diversify your organization,” we would have failed miserably. It took a long, long time to get the audience, the board, the artistic leadership and the staff all in place so that we could say that diversity was the fabric of the organization.

And the final aspect about the Goodman over the last two decades has been the willingness of our board to look at our work in a very entrepreneurial way. To a certain extent, we had the same advantage that Peter Gelb had, that Bob Falls came to the Goodman at a time when we were in a financial crisis. So the willingness to take risks was greater than perhaps it would have been if the theatre had been on more solid footing. And even if the theatre has become successful over the years or has gained a certain stability over the years, the board has continued to be willing to say that we’re going to go out on a limb to try to support new work, we will always try to develop the budget and compromise in favor of the artistic product. And the board did this when we didn’t have money in the bank. Now, we do have money in the bank, but the reason we have money in the bank is because we did this when we didn’t have money in the bank! It was that risk taking that, frankly, paid off over the course of time.

So having said all that, of course, we’re talking about the future. Now we’re in a position as an organization that is stable, that has stable artistic direction, and so, what are the issues that we need to deal with in the future? I’m going to talk about one thing, and that’s ticket prices, because that’s one thing that we’ve spent a lot of time obsessing about. And of course it’s all related to the demographics of the graying of our audiences. Is there a decline in subscription; what’s the future of subscription; etc.? We’ve been talking to our audiences, we’ve been talking to young people on our staff, we’re in the process of evaluating a lot of ideas and, yes, trying to think in a bigger box—that’s a great way to think about it. Here are a few points that cue the things that we’re asking: are our pricing strategies existing in an abstract way, and are they disconnected from the mission of our theatre? We’re trying to produce new work, a lot of unconventional versions of classics, as well as musical theatre work, and are we really looking realistically at the demand for a ticket to a new play as compared to a revival of a known play?

We have come to believe that price does play a significant role. It’s one of those things that you don’t want to be overly simplistic about and say that it’s all about price and that if we were able to lower our prices across the board, we would find demand increasing and would find a more diverse audience attending. It’s not that simple. And yet at the same time, I think price may play more of a role than we have really paid attention to up to this point. If you look at the Signature Theatre’s very heralded experiment, or the City Center’s $10 Dance Program… We’ve instituted a program by which we made all of our Sunday night tickets $20. No subscription discount—mezzanine, main floor—it was all one price. Now a night that had been so-so in attendance became a sold-out performance.

So what we’re wondering is: are our marketing strategies out of whack? We’ve been killing ourselves over the years, trying to sell the last few subscriptions each year. We keep dragging that subscription campaign out from five plays to four plays to three plays. And I’m starting to think, what are we doing? Are we ignoring other opportunities, new
ways of getting audiences in on a single-ticket basis, instead of continuing to beat the subscription campaign all the way to the very end?

And in conjunction with that, are we really doing enough with our true believers—the people who have been subscribers for many years? Because one of the paradoxes about the whole subscription issue, as Theatre Facts points out, is that new subscriptions are down but renewal rates are up. And that’s been exactly the case at our theatre this year—figure that one out, please! Also, we found at our theatre that not only are renewal rates up, but the number of people who are subscribing to all nine plays that we do is up dramatically. There’s a core audience that’s very loyal. But what do we really know about them? We think we know them, but I think sometimes we pay more attention to the people who are not coming and we’re not learning what we could learn from people who are attending.

We’ve been fantasizing about very radical ideas, like what if all the main floor seats were $30 and all the balcony seats were $20 and that were true at every performance—boom, that’s it? If we did that, would we fill our house and be able to dismantle the military industrial complex of our marketing department, thereby saving tens of thousands of dollars, not to mention freeing up time. As I said before about artistic directors and radical ideas, this is one that Bob Falls is beating me over the head with. He says, “Why don’t we just charge $30 and $20? Boom, that’s it. People will come, and we don’t have to worry about anything else.” And you think, no, that’s impossible—but if you were able to do broad-based price reductions, not discount programs…because I think that’s a very different thing. You really have to invite people by saying, “This is the price,” and not, “This is the price if you stand on your head and do a back flip at 3:00 pm in the afternoon on the day of the performance; then you can get a discount ticket.” No, X percent of the house is going to be at this low price and you’re welcome to attend for that and buy the entire season on that basis, for that matter, if you want to. If that did work, and you suddenly had new people, more people, a different group of people coming to the theatre, how would that impact your credibility in your community, how would that impact your fundraising? Again, it’s our far-fetched idea but I’m trying to explore a model where we can see what would happen or might happen if we were to do that.

We’ve talked about Internet sales, and I won’t dwell on that at length, but this is the great new opportunity, I think. Eventually, everyone will be able to sell tickets on the internet. In my opinion that will be the model that can replace the subscription model. Because the problem with getting rid of subscriptions is a practical one—how in the world do you make the numbers work? How do you pay for the advertising that it will take? We just did Passion Play by Sarah Ruhl—we never in a hundred years could have done Passion Play without having a core base of subscribers who would come to that production. You need to be able to sell tickets in an inexpensive way; that is the core of subscription. The Internet, I think, will enable us to do that. It will enable us to sell single tickets in an economical manner, so we can be less reliant on subscriptions.

Finally, then, we know that dismantling this economic model and looking at things in a different way is a very precarious thing to do. So we are actually looking at all of the target pricing things—again this has to do with technological opportunities that Internet sales provide us. One thing we’re talking about is if a portion of the audience comes as subscribers and another portion of the audience comes on an ongoing, low-priced ticket program, then maybe the people who are left, who are waiting for the reviews to come out to see if they want to attend, well, maybe they should be paying $90 a ticket, okay?
Because first of all, they’ll probably pay it, and second of all, you really want to reward the people who attend without hearing about the play or having read a review. So playing the extremes in terms of ticket prices is something that we’re looking at as well.

And to shift gears before I turn it over to Zannie: the importance of endowment, the importance of working capital, can’t be underestimated. As I said, 20 years ago, we had no money in the bank. We were operating year to year, basically. We went through a building campaign—a capital campaign—that ended up with us having money in the bank and having income from an endowment. And I can only say that it’s changed everything. It’s changed the mentality of our trustees in terms of how they look at the institution, because now they think of the institution from a long-term perspective. They’re thinking in a three-to-five-year arc of time, not a year-to-year arc of time—where, oh my God, if we have a deficit, it’s the end of the world—as somebody said earlier about the mentality of, “If you have a $1 deficit, you’re in trouble!” And that’s true; it’s only natural to have that mentality if you have no assets to fall back on. It seems to be an impossible dream for many people but I think it’s something that we all have to confront head on. Capitalization, working capital and endowment are the only way, in the long term, that we’re going to have a chance to achieve our artistic goals, fulfill our mission and maintain some financial stability. So with that, I’ll turn it over to Zannie.

Zannie Voss:
Thanks, Roche. I’m Zannie Voss, and I’m the chair and a professor at SMU. I run an MBA program in arts management, but what I really am is the data geek for TCG, for Theatre Facts. How many of you here have read Celia Wren’s article on Theatre Facts in the November issue of American Theatre? (A number of hands go up.) How many of you have actually read Theatre Facts, itself? (A number of hands go up.) There’s Chris Shuff back there, who’s nodding that, yes, he has read the full report of Theatre Facts. (Laughter.)

What I’d like to do, since many of you have already read it, is to touch on a few highlights from trends that speak to the issues that Roche brought up and some of the issues that we were talking about this morning. For the past five years, we’ve had 105 theatres that participated in TCG’s fiscal survey each year. Their average budget is $6.8 million, so we know that they tend to skew a little bit on the large side. So for some of the small organizations here, you might not necessarily feel some of the same norms. I do want to point out that these are simply statistical means, they’re not prescriptive. So when I’m talking about different percentages of budget for this or that, don’t think that if your theatre doesn’t match those numbers that there’s something wrong with your organization. It’s just saying that this is representative of the field as a whole.

Just to reinforce Roche’s point about Baumol and Bowen, and the growth in income and expenses in the nonprofit professional theatre field: earned income growth, contributed income growth and growth in expenses all exceeded inflation over the five-year period. For earned income it was 18 percent, 12 percent for contributed income, and 6 percent for expenses. The net effect on theatre’s bottom lines, CUNA (the change in unrestricted net assets)—kind of what we think of as net income—increased more than two-and-a-half times from 2002 to 2006. So that’s a good sign. There was also some good news in the last year: from 2005 to 2006, single-ticket sales increased 13 percent, in that one year. The bad news is that over the five-year period, single-ticket income fell 14 percent below inflation. At the same time, subscription income, on average, exceeded inflation by 3.5 percent, but since expense growth was 6 percent, subscription income now
supports a lower percentage of total expenses than it did in 2002. The net effect is that for these theatres, total earned income paid for 5 percent less of total expenses in 2006 than it did in 2002. So this makes you ask the question: if single tickets are down, where did the exceptional growth come from? Well, it came from all of those other earned income line items. We saw double-digit growth above inflation in tour income, presenting fees, education outreach income, income from co-productions and enhancement deals with commercial partners, rentals, advertising and endowments—not surprisingly.

Actually, the really big, big increase came in endowment earnings. It was a six-fold increase from 2002 to 2006—33 percent in the last year alone. It’s become the second greatest source of earned income from theatres aside from ticket income—pretty substantial. There was also 66-percent growth in a line item just called “other earned income.” It’s now the third largest earned income line item and covers 3 percent of total expenses. And what’s interesting to me about this 66-percent growth in other earned income, which has become such an important line item, is that we aren’t capturing all of the diversity in earned income activity that theatres engage in. I’m sure that some of my colleagues will speak to some of the more innovative ways that theatres are generating earned income a little bit later. There were only two earned income line items that fell short of inflation over the period. The first is royalty income—income that theatres generate from properties that are produced elsewhere—and the other area is interest and dividend income. Both of these plummeted in 2003 and have been slowly building ever since.

Not every theatre was better off at the end of 2006 than it was in 2002, but only 32 of the 105 theatres did not have budget growth that exceeded inflation. One theatre tripled its budget, while eight theatres doubled their budgets over the five-year period. So there’s some pretty impressive growth going on out there.

Attendance: I want to focus on attendance and ticket pricing. As many of you who did read the article know, attendance is down overall. Attendance is down by 8 percent for the five-year period and, at the same time, theatres increased the number of performances they offered by 2 percent. So you would read into that, that theatres are playing to lower capacity houses.

Let’s get into that for a moment and look at subscriptions and single tickets. Subscriptions are down. Subscribers now fill a lower percent of capacity in houses on average. They bought fewer subscriptions in terms of total ticket packages sold. The average number of plays purchased per subscription remained pretty steady even though, on average, theatres added two more productions to their seasons. So even though they are adding more product, they are not selling more product. The average price per subscription increased 3 percent above inflation—that’s the average subscription price. The highest subscription price that theatres offered actually increased 9 percent. But then the deepest discounts were 6 percent above inflation. What you see is this real expansion in the range of pricing that theatres are offering. As an industry, we have traditionally approached it as a reward for subscribing; we offer subscribers a discount off of the single-ticket price. And it is true for most theatres, but I’ve actually found that 13 percent of theatres actually charge subscribers more per ticket than they do single-ticket buyers. If someone is in your seat and they are not donating and you’re giving them a discount, is that really a better strategy than having a number of different single-ticket buyers, who are in the seat and paying a higher price and perhaps donating? From a customer-relations management perspective, I think there are some really interesting questions to be raised.
Single-ticket sales are becoming an increasingly important aspect of theatres’ earned incomes. They exceeded average subscription income in each of the five years—that was not the case before 2002. And it’s true for the majority of theatres. For 56 percent of theatres, this was reality in 2002 and it increased at up to 64 percent of theatres in 2006. It’s not just one or two theatres driving that trend. Theatres are working harder to bring in every dollar of single-ticket income. In 2002, it cost $0.19 to bring in $1 in single-ticket income, and that went up to $0.24 in 2006. The average number of single-ticket buyers was 2 percent greater in 2006 than in 2002. And even though single-ticket buyers are filling more capacity in our houses, they are not doing so at a rate that is making up for the loss in subscribers. What we saw in 2002, 2003 and 2004 is that theatres were playing to 70-percent capacity on average. That slipped in 2005 and by 2006 it was down to 67 percent. We lost 3-percent capacity.

If our houses are less full, it makes us stop and take a look at pricing. Are we reacting to loss of capacity with a diversity of pricing strategies—or have our prices, as they’ve increasingly gone up, made our capacity go down? I wanted to take a look at this and in the last couple of days, I did some fooling around with the data, and found out, not surprisingly, that theatres’ capacity utilization was all over the map. Okay, so there’s a big range out there from below 50 percent of capacity to the highest, which was 90 percent of capacity. Seven of the eleven theatres that play to half a house or less charge an average ticket price of $20. So in this case, it’s not that price is driving some great demand; either that or they’re just playing in houses that are too big.

I looked at ranges of capacities—50 to 60 percent, 60 to 70 percent, etc. and in every single capacity utilization category, at least 17 percent of theatres offered an average ticket price of $20. So again, it’s not necessarily that there’s a different correlation between capacity utilization and pricing. Only 6 of the 105 theatres charge an average ticket price above $50. Two of them play in the 70- to 80-percent capacity range, two in the 80- to 90-percent range and two in the 90-percent range and above.

It raises a question for me. If the four playing below 90-percent capacity lowered their average ticket prices, would that push them into the 90-percent range? It’s a question. I found that there was no significant correlation between a theatre’s capacity utilization and the range of ticket prices that it offered or its average high ticket price or low ticket price. In terms of discounting, theatres are employing discounting to a greater and greater extent. There’s a theatre that even has a $110 disparity between its lowest and highest single-ticket price, which is a huge range. For the same set of theatres, what we saw was 73 of the 105 are offering a broader range of ticket prices now. And most of the time, what is happening is that some are lowering their low and raising their high ticket prices; and in the other half of the cases they are raising both the low and high, but they are raising the high even higher.

With respect to pricing, it raises a lot of questions. Is it really just a case of supply and demand? I think we all realize that it’s a lot more complicated than that. It’s a supply and demand issue within the context of programming decisions, artistic quality, the size of the market and the density of competition in the market in which you operate. There’s actually a high correlation between market density and capacity utilization. If you play in a market with a lot of theatres, there are a lot of theatergoers in the market.
Getting out of the statistics for a moment, discussions I had before this session made me go back and look at different findings that other researchers have uncovered that relate to pricing and relate to strategy about it. I’m going to bring together some disparate logics that have a confluence. The first is—anyone who sat in on the teens discussion after lunch today heard the same thing; that price is not necessarily the barrier to attendance for most non-consumers. What drives consumption of the arts as an adult is predominantly four factors from youth: what are the values transmitted from the family, what are the values transmitted from the school, what was your arts exposure as a child and what was your arts involvement as an amateur? If you had engagement along those four different measures, you’re much more likely to be an arts attender as an adult.

Other factors come to play in motivation for attendance: are you looking to attend from a “thirst for knowledge” perspective; are you looking for symbolic benefits—what does it say about you? Is it due to social relationships—you go because you enjoy sharing the theater-going experience—or emotional benefits? So you can’t say that just by lowering prices it’s going to bring in non-attenders. At the same time, if you have this vast pool of people who do have these predictive factors but they’re not going to the arts, what else is going on there?

There’s another study that talks about perceptions of price. It found that price perceptions are determined by four different perceptions of risk and the greater the number of perceived risks, the more the price is perceived as being high. The four risks are: psychological risk: if I go to this event, is it going to be incompatible with my own self-image? The second kind of risk is social risk: what are other people going to think about me when they see me there? The third risk is economic risk, it’s simply the loss of money: is this worth the money that I would spend to go? And the last risk, that I think is here and now with Generation Y—more important than anything else—is the sense of functional risk: am I going to be bored? If I do this, am I going to feel like I’ve wasted my time?

How many of you are familiar with the Irvine study *The Crisis of the Arts in California*? *(Several hands go up.)* Several of you. So this is not going to be new, but there are a lot of wonderful aspects to the report, although I don’t necessarily agree with everything in it. One of the trends that they highlighted is the notion that in the past, we said the youth have short attention spans and they want control. Well, now a lot of entertainment companies have taken advantage of that and are actually enforcing that, with a set of products and services, aimed at having a short attention span and being in control. More and more people are dissatisfied or discontented just to have passive consumption of a supplier-generated set of options. Instead, people want to be their own curators of their experiences. More and more we are moving into a consumer-controlled content world. Think of iPods, YouTube—they are going to replace radio and TV. You can create your own entertainment on Facebook or on YouTube. You get to vote people off of reality TV shows. We have input into everything. People want to be involved as amateur artists. People want to be the next star. It’s the involvement that’s most important. They don’t want to just passively consume.

That works great for a museum. For museums, it’s easier. They can adapt because people walk into a museum and they can say, “I want to stand two minutes in front of this painting and then I want to walk into another gallery and do what I want to do.” For theatres, it’s much more difficult to figure out how we’re going to remain competitive, if this is a change in consumer preferences. Again, it’s the question: if I’m going to do this, am I going to be bored? Am I going to waste my time? It’s back to a question of
functional risk. If so, there’s an increase in perception that the price is too high. With the shift in consumer perceptions, do we have to price our product so that we are counteracting that perception of functional risk? And with that I’ll pass it on to Susie Medak.

Susie Medak:
Chris, did you say that we have until 9:00 tonight? (Laughter.)

Chris Shuff:
No problem, we’re having a slumber party. (Laughter.)

Medak:
Bring your pajamas, everyone!

What I thought I would do to keep us honest in this discussion about financial models is to tell you about Berkeley Rep’s dark night of the soul, our moment of crisis—what we’ve perceived of as being action-steps to address that; and five or six years later, what we perceive as being the outcome at this moment; and then to raise a question.

You on the East Coast felt that 9/11 was really your crisis, but it was in fact a national crisis, and it certainly had ripples throughout the country and at arts organizations throughout the country. We found out that not only did 9/11 have an impact but it came, unfortunately, at the same time as the dot-com bust. And I was fond of saying, at that point, that every dentist was more invested in technology in San Francisco than they were anywhere else in the country. And so the impact on organizations in our part of the country was pretty devastating.

We immediately began cutting our budgets like crazy, trying to anticipate how bad it was going to be. And we realized that no matter how bad we thought it was going to be, it ended up getting worse. And for a few years, we found that we just couldn’t figure out what was the right thing to do. I responded in one way; Tony Taccone, our artistic director, responded in another way; and I think neither of us felt, for a few years, that we could get a handle on what was going on. And one of the things that happened was that we all got very internal. Our programming got very internal and, frankly, our programming was not as strong as it had been for many years before or thankfully as it has been since then.

And as a result of that, we really did reach a point where we thought that we could not engage in business as usual. We had a lot of very serious conversations with our board. We had been in the middle of a long-range planning process and this sort of sent it into a tailspin. There was a moment when we realized that we had two choices: we could continue to make cuts; we could continue to reduce the size of our operation and try to achieve stability by spending much less; or we could do what, ultimately, our board led us to do, which was to make the decision to spend much more over a period of time. To invest heavily in the hope that, ultimately, we would see the kind of payback and payoff that would help us be stronger years later.

There’s been a lot of talk about innovation and whether money does or doesn’t make a difference. Everyone likes to say, “You can innovate without money, you can do it,” and I would say that’s absolutely true. But what we’ve seen, and I’m sure what many of you have seen, is that money really does lubricate change. There are so many things that
we’re doing now that we simply could not have done before, only because we have people in place who can do them, because we do have that extra $5,000 in some departments, $20,000 in another department, $40,000 in another department that allows us to just test ideas. So part of this planning process was about saying that we need to be able to try out and experiment with things and we’ve got to have the people power and the resources to be able to do something that is not business as usual.

There were two major decisions that we made at that point. One was that we were shifting our economic model. When I came to the theatre in 1990, we were operating off of an 82-percent earned model. (*Murmurs of shock from the audience.*) We were terribly proud of that. We had turned what might have been considered, by some of us, as a weakness into a strength and a source of pride. But it was not necessarily the place that we wanted to end up over time. Over the course of years, we’ve actually shifted that down but not by saying that we want to be earning less but by saying that we want to attract more contributed income to complement what we are earning. There was a point, though, in the earlier part of this decade, that we had one of these heart-to-heart conversations. There was a moment when we, as a board, actually agreed that we wanted to see if we could achieve, over time, a 50-to-50 ratio. And I say that not because I think that is the right ratio for everybody and not because I even think that that is the right number. I’m not sure we even know what the right number is. At this moment, we believe that the right percentage for us is 50/50. But if we’re successful in accomplishing some of the other challenges that we’ve set out for ourselves, that number may become 40 percent earned or 30 percent earned. Not only are we interested in attracting audiences, we’re also interested in attracting specific kinds of audiences for specific kinds of work. And so I say the model is fluid.

One of the reasons we decided to shift our economic model and look at that 50/50 ratio was because we are a labor intensive industry. There are a number of people on our board who realized that in their own organizations it was the people who were the assets, the people who were the source of their strength. And in many organizations they say that means the two people at the top and particularly in corporate America, there’s a real focus on, “You put your money on the top and everything else will take care of itself.” Tony and I did a lot of work to make sure that we all understood that our assets were not just the two of us but that it was our actors, our directors, our master carpenters, our technical director, who together contributed to the definition of who we were and what we were. One of the issues that we dealt with was that the cost of labor was going up because we believed that it was important for theatre professionals to live with dignity. Even at the same time that nobody in this country expects any longer to be paying the real price for what American laborers cost. So we decided that that had to be an issue that we addressed.

The second thing that we talked about—and it was a very hard decision, and we still don’t know if this was the right one—was that coming off of the dot-com bust, many people had lost their investments, many people had lost faith in the marketplace, many people had lost faith in the value of saving and many people felt that in their own businesses they would actually spend their money in a different way. That was combined with the fact that we had many people on our board who were either in real estate or were venture capitalists—people who understood that there was great value in investing in order to leverage future gain. They said to us, “We do not want to raise money for endowment. We do not think this is a good idea. We don’t think this a great value. We think that we can invest our own money more aggressively and more
responsibly than you can, because in order for you to invest responsibly, you must invest conservatively, and we feel that the five years that it would take us to build that endowment, is five years that would be lost for this theatre. It would be better for us to pour money into the organization now and hope by doing so, there will be greater resources at the other end."

So we developed a campaign and a ten-year strategic plan that basically created an assumption that we would enhance our operating fund with about $2 million a year from funds raised by this special campaign. And so, that is partially how we got to this 50/50 ratio. There’s a small amount of money being put into the endowment but most of the money is going, right now, into people, plays and infrastructure. And by people, I mean both staff and audience, as we’re doing a lot of work in audience development. We looked around and saw that everyone was doing a capital campaign every ten years. Well, in ten years, we can go back and revisit endowment, but right now, let’s see if we can strengthen the organization. I’d sleep better at night if we did have a large endowment but, you know—sleep, who needs it! (Laughter.) So, that’s one piece of the puzzle.

The other piece of this economic puzzle was this 50/50 ratio. And in order to maintain this 50/50 ratio, we did have to grow our audience. This did not assume that we were selling fewer tickets, but more tickets. So we’ve actually set out some significant goals for ourselves. Once again, the nature of what is distinctive about our organization, as opposed to your organization, is that we decided that regardless of whether subscriptions may be “trending down,” the nature of our work was sophisticated enough that we felt we needed to, as much as possible, have an ongoing relationship with our audience. And that having someone come once a year was not going to create that relationship with audience members that we felt was going to sustain the work that we do. So we don’t talk about subscription as much as we used to but we do talk about multi-play purchases. While we greatly and most highly value our people who are subscribing to five or seven of our plays, we don’t devalue any longer the people who are subscribing to three or four plays. We continue to build programs that are intended to increase the number of people who would be considered subscribers. And I will say that over the last two years, the first year we were stabilizing, and the second year we had slight growth in subscriptions. In this third year, we’re up by 500 subscriptions and by the end of this campaign, we’ll be up by more than that. So we’re feeling that we’re seeing a shift that is impacted by a number of things, not the least of which is pricing.

The last piece of this is that we looked at ticket pricing. I realized that I’ve been having conversations with boards of directors about ticket pricing for over 30 years. There’s always been this fantastic dance ritual that I’ve done with the finance committee where the marketing department and I come in with a set of ticket prices for the next year. And we all discuss the context for them and there’s a point at which the finance committee says, “Don’t you think you can move those up just a little bit more?” And we say, “Oh no, no, we can’t do that.” And we do this little dance back and forth, and in the end, they go up a little bit. But, of course, we left a little room for them to go up a bit and the finance committee feels very, very good that they’ve pushed us beyond our comfort zone.

Schulfer:
You’re giving away our trade secrets now! (Laughter.)

Medak:
But we realized that for years and years and years, we’ve been pushing the ticket prices to what we thought was the highest level of elasticity—as we used to call it. How high could we make them, where people would still purchase them. Now, what we never talked about was how high can we make them so people will purchase them many times during the year. And so there was a point years ago when the marketing director said that the ticket prices had reached a point where he couldn’t afford to go. We looked at that and said that this was really a problem, and so we started creating more discount programs to compensate. We ended up with our face-value tickets and all of these discounts. And I have to tell you, I’m one of these people who hates the Hot Tix booths. I hate them. I hate the fact that we’ve created an environment where people think they shouldn’t be paying full value for theatre tickets. It makes me crazy. And I think it’s not surprising that people say, “Why would I subscribe when I can get cheaper tickets in so many other ways?”

One of the things that we decided to do was to hire a pricing consultant. The president of Peet’s Coffee is on our board, and that company lives and breathe pricing because part of the definition of its brand is that it’s very expensive but very good, artisanal and globally concerned. Some of you heard him a few years ago when he spoke at the LORT meeting. Well, he brought in a guy who we could use and he was fantastic. He asked what our goals were and we told him that our goal was to get more people to attend more often. And our goal was to have greater age diversity, ethnic diversity, etc. in our audience; but our main intention is for people to come more than once. So he put together a really interesting economic model for us. We looked at what people were attending in other venues. How often they were attending. We looked at their pricing. He did focus groups. And we ended up with what he referred to as a sweet spot, which was a point below which it made no difference whether we discounted or not and a price above which he felt it would be discouraging people to come again. And it was a very different way for us to analyze the information.

Now, we are so retro—it’s Berkeley—we’re egalitarian, every seat is a good seat, every ticket should be the same price because we don’t want to show favorites. (Laughter.) But on the basis of this information, we decided after all of these years that we were going to give up our single-tiered pricing. What we did was raise our top-tier price, we created a section where there was no change, and we significantly reduced our ticket pricing in other areas. We also eliminated many of our discounts.

The thing that was interesting for us—and all of you have tiered ticket pricing are saying, “So what’s the big deal?”—but the thing that was a big deal for us was that we realized not so much that the ticket prices were lower but the interesting thing was that three shows into the season the average ticket price being sold was actually higher. What was really interesting was that the perception changed. All of our surveys are telling us that people are saying that it is so fantastic that Berkeley Rep is economically accessible right now. People can afford to come now. The cheapest ticket for somebody under 30 is $4 less than it was—$16.50 instead of $20 on certain nights and for certain sections. It’s not a significant difference, but the perceptual difference is really profound. And it’s too early to know if we’re trending up. But at the moment, I will say that we are seeing this year, based on these new ticket prices, a different kind of diversity in the house. What we are seeing are significantly more people in the house. I will say that it’s been an exercise that is really been interesting to us.
Finally, the last thing that I want to say is, we did all of these things because we want to be viable. We want to be viable as long as we have a reason to be viable. We didn’t do these things because we thought this was going to buy us perpetuity. We know in five years that we’re going to have to look at this again and see if this economic model is still viable. Frankly, we look all of the time whether we are artistically viable. There’s been a lot of talk about stability, there’s been a lot of talk about how do we make ourselves more stable in this field. And I just want to ask the question: is there ever been a time in the history of theatre that it has been economically stable? And do we have any right to it, or should we even want that?

**Michael Robertson:**

Do I have to answer that? Hi, I’m Michael Robertson with the Lark Play Development Center and we’re sort of the odd duck in the room, maybe. We’re a play-development center; we don’t produce. We scout plays across the world, we incubate those plays, and then we advance those plays to theatres across the country through various partnerships, both large and small. We are 95 percent contributed revenue. So I fundraise all of the time, every day, I’m fundraising now! (*Laughter.*)

When I first joined the Lark, I thought to myself, “What am I doing here?” Who steps into a 95/5 ratio situation when it’s the contributed that’s 95 percent? I came from an organization that was 95/5 the other way. So I went from extreme to extreme. And then I realized that if your business model follows your mission, then you’re doing the right thing—your ratio is right.

But the Lark has not always been as positive in its financial stability as it is now. About six years ago, the Lark had its first deficit, and that really set into play a lot of things that I’m sure most institutions who’ve encountered their first-ever deficit go through. We looked at what the board composition was. We brought on a new board president, who had run boards before, and he could help us strategize and to really build a board with depth—a board with networks, a board with the passion for the work that we were doing. That was a huge step. Then we realized that we didn’t really know what we were doing financially. Are there earned revenue sources untapped? Some board members asked, “Why don’t we take a piece of every play that we work on?” Our mission, fundamentally, is not to do that. We don’t want to encumber any play that we touch, because we want you guys to do it. We want Lark plays to end up in as many regional theatres as possible—it’s why we exist.

Luckily, in those moments of distraction, we kept going back to the mission. We are in existence to bring new plays forward, to get these plays on American stages. Because of that, we were able to take more and more positive steps towards a working economic model.

We were at that point 11 years old—I wasn’t there at the time—and we realized that we had found a niche. We did what we did really well and we wanted to keep doing that. We didn’t want to live forever. We thought there may be a time when the Lark isn’t needed because voices would be rising to the major stages on their own without our support. We went through a process with the Nonprofit Finance Fund. That was enlightening to us on so many levels. They basically came in and analyzed the history of our finances, the composition of things, and looked at things that they thought were alarming or questionable. They helped us develop a model that was wrapped with our mission. They really understood us. They didn’t base it on any other institution’s model; we didn’t
benchmark it with any other institution around the country. We based it on what we do. What is the best business model for us to do what we do? That was insightful for us.

There were a lot of specifics that came out of that but one of the most important one was—do not create an endowment. We were surprised. Everyone says that you should create an endowment—museums have them, operas have them, the big theatres have them. And they said, “You have no way to weather a storm. Lock away $500,000 in an endowment, and the interest from that is not going to weather much of a storm. You need to create a cash reserve and you need to create a play fund, an opportunity fund.” So we turned our focus on budgeting a surplus, which to me was kind of an interesting concept. Budget a surplus that you’re going to keep and roll into something for the future and not roll right back into the next year—something that created a little bit of a cushion. The idea of planning a surplus is so important. We looked at all of the benchmarks on how many months of cash you should have on hand. And we thought, well, we need at least three months cash and we’re now there, so that’s really, really exciting. We’ve built up that cushion and we can weather certain storms.

To backtrack a little bit here, right before 9/11, we had some very innovative people on the board, who said, “We’re going to need to move. We’re in a very precarious situation. Can we raise a bunch of money and just stick that in the bank?” Basically overnight, they raised more than $300,000. Our budget then was probably close to $425,000 (it’s now $700,000). So they raised an additional $300,000 on top of that—they were visionary. They knew we needed to move at some point. We’re in this crappy building on Eighth Avenue in Manhattan. It’s going to be ripped down at some point. September 11 happened, so we didn’t do anything with that money, we laid low. And then that deficit happened. Luckily, they had created this capital fund, which they then allowed us to tap into over a series of three to four years. This was supposed to be capital money but it was the board’s decision to use this money.

It was a combination of random factors. This discussion is hard because there’s not going to be one model that we can use and we need to base it on our own circumstances. We’re looking to double our budget in the next five to seven years, to double our staff, to find a new space, and we’re going to do all of these things, which is really exciting and really scary. But it’s because we went through an analysis. We had a board that really cared, looking at that analysis; we had a finance committee that got that it wasn’t about charging the writers $50 to submit their plays. We don’t really have ticket sales—we have some, and our highest ticket price is $18 and we can’t raise it—that’s as high as we can go. I have to say, at the end of the day, that we are where we are and I hope we’re going to be where we want to be in five years—although we are still on Eighth Avenue in that crappy building (laughter)—because we always went back to the mission. Who are we? Why do we exist? And do we have the right people sitting around the table advising us? So that’s the Lark’s story.

Itamar Kubovy:
Hello, I’m Itamar Kubovy, the executive director of Pilobolus. For those of you who don’t know, Pilobolus is 37 years old and has been living hand to mouth until 12 months ago. The interesting thing about Pilobolus is that it’s always been sort of anomalous, whether it’s in the dance world or the theatre world. Its particular way and style of work is very particular to it for all of its brilliance, and as some would have it, its detractions. So it’s very hard to analogize with Pilobolus, I think, to say that our experience is an experience that can be replicated or should be replicated...
The company was, as I said before, living hand to mouth. It was a very tough balanced budget and a rare balanced budget four years ago. Pilobolus had always done tours. We do about 120 shows a year and about 150,000 see the company, and that had been, and remains to this day, the core business of a touring modern dance company.

Something happened about a year ago, and this had been preceded all through the life of the company with an occasional TV commercial, the occasional appearance, the occasional application of what we do to some other medium. It was always motivated by someone with an idea from the outside and was never something that we spent any energy marketing. About a year ago, an advertising executive in Texas sent me an e-mail that had a very short description of a car commercial that involved shadows. We said, “Yeah, I think we can do that.” We hadn’t really done anything with shadows before. So we made this car commercial and it came out really good. They got a really good team of people together to do it and that caught the imagination a month later of Laura Ziskin, who was producing the Oscars. Very shortly after that, when she saw this commercial, she called and said, “I think I have an idea.” We flew out there and ended up appearing on the Oscars. And it was interesting, because going into something like that, you have no idea what the impact is going to be. Half the world tells you that it’s going to change your life forever, and the other half says that it’ll be what it is and the next day it’ll be just business as usual. Well, I can say that it was not business as usual. It was something that was really strange and mysterious to behold—the weird power of American media in that context.

The number of calls that we received over the next two months following fell somewhere between eight thousand and ten thousand. This was happening from everywhere all over the world and put the organization, frankly, into a tailspin. It was one of those things where no one knows quite what we’re supposed to be doing at that moment. Everything gets questioned immediately—everything, top to bottom! And you don’t feel like you’re in control of that questioning process. We’re still in the middle of that questioning process, although we’re beginning to sort it out.

Probably the most interesting thing that I can say here, that may have an analogy in it somewhere to others, is that we had a very entrepreneurial and courageous board of directors. We have a group of people leading us and with whom we are running the company, and they were thinking very clearly about protecting everything that Pilobolus has been over the years and moving that forward as a nonprofit, which is what Pilobolus is and always has been. And our split is 70 percent earned, 30 percent contributed. The board said, “Rather than sit back and reactively wait and see what happens after this event, let’s bring in a group of people that knows what they’re talking about and can advise us about how we can control what’s going on at this moment, and to organize the impact on the organization in such a way that everything maintains the mission and ends up funneling back into the mission.” So we too have created a creative opportunity fund where all of the excess income has been going and that essentially is a board fund—extra-budetary—that is designated only for the creation of new work and research and development that sustains the central mission—which is essentially, how do you use the body in innovative and metaphorical ways?

So that linked the opportunity with the central mission of the organization, which seemed very crucial in terms of infrastructure. And at the same time, the board said that this is a growth business and if you manage to make this amount of money on all of this extra
strange work, then you need to make one-and-a-half times that next year. And let’s aggressively pursue this work and see how we can tie this into our general mission. That decision was really a shocking moment. Essentially, when we entered the board meeting, we went there with the work that we had already completely booked, which accounted for X amount of money. And we were very proud and happy that we could say to our board, “Look, we can see the end of the tunnel and we haven’t even started the year and we’re going to be okay and there’s going to be stuff coming in…” and they said, “Wait a minute, you actually need to add a huge amount of stretch onto what this is, and go out and get it.” It was an interesting decision. It was odd sitting in this nonprofit setting and to hear this extremely entrepreneurial directive. Yet, everyone agreed that that was the thing that we wanted to do that ultimately would feed back to our central mission. It took about 45 days to hit that stretch number after that board meeting.

So, that’s really the story. It’s very interesting, the degree to which this opportunity has forced us to think about what the mission is. How do we stay true to that mission? And how can a radically changing reality continue to realize the dreams and goals of the organization?

**Schulfer:**
Thank you, Itamar. When we had our pre-conference call, the concern among the panelists was that we wouldn’t be able to fill an hour and a half. For better or for worse, we did that but there’s still time for some questions. Questions, anyone? We’ve lulled them into a stupor! *(Laughter.)*

**Audience:**
One of the conversations that comes up on ticket pricing is that I have a couple of board members who think we price tickets according to what the staff would pay, not what a board member would pay or their friends would pay. So I’m carrying around some of what I’ve heard and read and understand about what’s happening in the field about resisting increasing ticket prices. But because board members have the capacity to pay full-price and tend to hang in circles with people who also have that capacity, there’s tension there and I wanted to know if anyone else experienced that?

**Medak:**
By charging a certain price for tickets, you’re creating expectations about what the buyer will experience but it’s also goes back to how do you define success. I think one of the ways that you can define success is by thinking, is your targeted audience sitting in your theatre? And I know of very few theatres who set as their goal that their target audience has income over $160,000, that everyone is over 60, they’re all white. I don’t think that’s what most of us had as a goal. I think we’re all looking for an audience that’s more diverse. I think what we can show is that what we’re doing is not creating that. In some theatres, they may be doing that, but I don’t think that it’s necessarily the norm. And the point of the exercise to bring in a consultant was to get rid of some of the mythology of it. I think, frankly, that we know that some of these teenagers have more disposable income than many of us. That’s not the issue. The issue is what is the perceived value of the work? And as we’ve said, if we want people to come back over and over, then we have to think not about a one-time event price but what is the price that will get them to come back again and again.

**Robertson:**
I’m just wondering if people are seeing the art affected in regard to the financial model. We joked on the conference call that the Lark reads up to 1,000 plays a year—twice; we read each one twice. We are seeing plays that are written in chairs. We’re now calling them “Chair Plays”—two-person plays in chairs. It’s like the writer can’t conceive of being out of the rehearsal room or the reading. So we’re seeing a weird group of plays that are coming in that look great in chairs, and we’re trying to get them on their feet, and we say, “They should just stay in the chairs. Done! Staged!” (Laughter.) I was just curious if there are any observations about this and how the business model is effecting the art?

**Medak:**
Like there isn’t enough money?

**Robertson:**
There’s never enough money!

**Audience:**
(Inaudible)... I recently saw a play with 20 characters and an orchestra of 10, and it was a fabulous production and it was well received. Well, it never got a second production, because who wants a play with 20 actors? The next play the composer sent to us had five people, because he knew that would be produced. And it’s been produced a couple of times already. I think the playwrights understand what we’re going through when we make selections, so that’s absolutely affecting the work. For us, we’re trying to deal with that by raising money for a fund for new-play development. We are finding that our audiences are responding to that because it seems a little sexy, but it’s definitely affected our relationships with regular playwrights.

**Paul Nicholson:**
We’re talking about audiences and are they willing to come back. One of the things that we’ve done is audience research going back over 30 years, and we continue to do that. More recently, we’ve been analyzing the difference between the returning audiences and new audiences. I thought a couple of things were particularly interesting. One was that 50 percent of our new audiences had actually seen our work before. We have to be aware that they are seeing our work, but how are we connecting with them to get them back? And the second thing was that there was a very significant disparity between the number of tickets ordered online and the number of purchases from returning audiences and new audiences: 70 percent of new audiences were ordering online, versus 50 percent for returning.

**Medak:**
I was just at a conference two days ago with people from orchestras, opera companies, etc., and one thing that kept coming up in that conversation was that we’re all desperately chasing this young audience. And we all looked around and said that they are not going to come on a regular basis right now. And if we set that as our challenge, we’re going to be so disappointed. On the other hand, the other piece of the puzzle is Paul’s piece. What are we doing to get them in the door one time, so later on when they’re ready to make a habit of it, they’ve at least been here? And that was something that was hitting across all of the disciplines. And the ticket pricing issue hits all along this line.

**David Hawkanson:**
We’ve used Susie’s consultant as well. Last year, we put out a quiet online subscription of $100 that was way below normal and it was amazingly successful. So we said to ourselves, “What have we got here? Is this just a group of bottom feeders or are these people we want to keep around?” And in fact, we used the consultant to find out who these people were, find out what their price elasticity was, find out what their economic status was. And he came back and said that these people are significantly lower economically than your current median audience but they are younger than your current audience. They have the same education level, so we suggest that you keep these people. And he gave us some elasticity that allowed us to go up about 20 percent in price. At the same time, he said not to handle these people in the same way that we handle our normal subscribers, assuming that you give them the discount and move them up and in a matter of three years, they’ll be full-time people living in the suburbs propagating. (Laughter.) So, the recommendation was to track them separately.

But going back to your point, Laura, the majority of your board will say that they feel you are under-pricing and the box office people will say people come to the box office and they always want the most expensive seat. But those are not reliable anecdotal sources. What’s great about having these resources, like Susie gave us, was to have another point of view and research that we could use to make a decision somewhat intelligently.