

**San Diego Convention Center Corporation**  
(a component unit of the  
City of San Diego, California)

Annual Financial Report

For the Year Ended June 30, 2017



Certified  
Public  
Accountants



**San Diego Convention Center Corporation  
Annual Financial Report**

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## Independent Auditor's Report

To the Board of Directors  
San Diego Convention Center Corporation  
City of San Diego, California

### Report on the Financial Statements

We have audited the accompanying financial statements of the San Diego Convention Center Corporation (SDCCC), a component unit of the City of San Diego, California, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the SDCCC's basic financial statements as listed in the table of contents.

#### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

#### *Auditor's Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

#### *Opinion*

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the San Diego Convention Center Corporation as of June 30, 2017, and the changes in its financial position and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

***Other Matters***

***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3-9 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

***Other Reporting Required by Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated October 25, 2017, on our consideration of the SDCCC's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the SDCCC's internal control over financial reporting and compliance.

*Macias Gini & O'Connell LLP*

San Diego, California  
October 25, 2017

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)**



**San Diego Convention Center Corporation**  
Management's Discussion and Analysis  
For the Year Ended June 30, 2017  
(Unaudited)

As management of the San Diego Convention Center Corporation (SDCCC), we offer readers of SDCCC's financial statements this narrative overview and analysis of the financial activities of SDCCC for the year ended June 30, 2017. We encourage readers to consider the information presented here in conjunction with additional information that has been furnished.

**OVERVIEW OF THE FINANCIAL STATEMENTS**

This discussion and analysis is intended to serve as the introduction to SDCCC's basic financial statements. The financial statements of SDCCC report information about SDCCC using accounting methods similar to those used by private-sector companies. These statements offer short-term and long-term financial information about its activities.

The Statement of Net Position presents information on all SDCCC's assets, deferred outflows of resources, liabilities, and deferred inflows of resources as of June 30, 2017. The difference between (a) assets and deferred outflows of resources and (b) liabilities and deferred inflows of resources is reported as net position. Over time, increases and decreases in net position may serve as a useful indicator of whether the financial position of SDCCC is improving or deteriorating. SDCCC did not have any deferred outflows or deferred inflows of resources as of June 30, 2017.

The Statement of Revenues, Expenses and Changes in Net Position presents information showing changes in SDCCC's net position during the most recent fiscal year. All changes in net position are reported when the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., earned but unused paid time off).

The Statement of Cash Flows presents information showing cash receipts and cash payments during the fiscal year, a reconciliation of operating income to net cash provided by operating activities, and detail of noncash investing, capital and financing activities.

**San Diego Convention Center Corporation**  
Management's Discussion and Analysis (Continued)  
For the Year Ended June 30, 2017  
(Unaudited)

**SDCCC FINANCIAL STATEMENT ANALYSIS**

The following is a summary of SDCCC's assets, liabilities and net position comparing FY 2017 with FY 2016.

	<u>FY 2017</u>	<u>FY 2016</u>	<u>Percentage Increase (Decrease)</u>
<b>ASSETS:</b>			
Cash	\$ 10,951,043	\$ 12,544,121	(13%)
Receivables	8,373,155	7,658,400	9%
Prepaid expenses	630,506	821,668	(23%)
Deposits with others	124,702	112,959	10%
Inventory	38,416	38,416	--
Restricted cash - I-Bank contingency	826,954	--	--
Restricted investment - I-Bank construction fund	19,128,822	--	--
Capital assets, net	<u>23,589,252</u>	<u>11,706,839</u>	101%
Total assets	<u>63,662,850</u>	<u>32,882,403</u>	94%
<b>LIABILITIES:</b>			
Accounts payable	1,068,083	744,057	44%
Accrued liabilities and compensated absences	4,108,732	2,932,720	40%
Unearned income	5,741,756	5,380,957	7%
Current portion of long-term debt	2,197	2,197	--
Long-term portion of unearned income	4,874,725	5,501,155	(11%)
Long-term debt	<u>25,510,437</u>	<u>12,635</u>	201,819%
Total liabilities	<u>41,305,930</u>	<u>14,573,721</u>	183%
<b>NET POSITION:</b>			
Net investment in capital assets	16,898,738	11,692,007	45%
Restricted – I-Bank contingency	826,954	--	--
Unrestricted	<u>4,631,228</u>	<u>6,616,675</u>	(30%)
Total Net Position	<u>\$ 22,356,920</u>	<u>\$ 18,308,682</u>	22%

**San Diego Convention Center Corporation**  
Management's Discussion and Analysis (Continued)  
For the Year Ended June 30, 2017  
(Unaudited)

**SDCCC FINANCIAL STATEMENT ANALYSIS (Continued)**

Assets

Total Assets of \$63.7 million at FY 2017 year-end increased by \$30.8 million, or 94%, from the prior year-end balance of \$32.9 million. The changes were substantially the result of acquiring restricted cash from loan proceeds received, with a net balance of \$19.1 million at the year-end, from the California Infrastructure and Economic Development Bank ("I-Bank") related to capital infrastructure improvement projects, as well as capital asset purchases, net of depreciation, of \$11.9 million, a 101% increase compared to prior-year. The loan proceeds are earmarked for specific capital infrastructure improvement projects which funded \$0.3 million of loan initiation costs and \$6.1 million of infrastructure project costs by year-end.

Liabilities

Total Liabilities of \$41.3 million at FY 2017 year-end increased by \$26.7 million, or 183%, from a balance of \$14.6 million in FY 2016. The change was due to an increase in long-term debt of \$25.5 million, as a result of securing a \$25.5 million I-Bank loan for capital infrastructure improvement project costs, as well as a \$1.2 million, or 40%, increase in accrued liabilities for accrued loan payable interest expense due in August 2017, and from an increase in retention liabilities for capital infrastructure projects.

Net Position

Total Net Position of \$22.4 million at FY 2017 year-end increased by \$4.0 million, or 22%, compared to the prior year balance of \$18.3 million. Net investment in capital assets increased by \$5.2 million compared to the prior year due to capital expenses exceeding depreciation expense and retention liabilities, net of loan proceeds received during FY 2017. The increase in restricted net position of \$0.8 million was the result of reserve requirements related to the I-Bank financing lease agreement established from existing SDCCC resources, which reduced unrestricted net position by the same amount. Unrestricted net position decreased by \$2.0 million compared to the prior year due to \$5.2 million investment of capital assets as well as the \$0.8 million reserve requirements exceeding the increase of \$4.0 million excess revenues over expenses at year-end. SDCCC expects to receive reimbursements of \$2.8 million in October 2017 from I-Bank proceeds related to infrastructure capital assets purchased at year-end which caused a temporarily decrease in unrestricted net position at year-end.

**San Diego Convention Center Corporation**  
Management's Discussion and Analysis (Continued)  
For the Year Ended June 30, 2017  
(Unaudited)

**SDCCC FINANCIAL STATEMENT ANALYSIS (Continued)**

The following table summarizes the changes in net position for SDCCC comparing FY 2017 with FY 2016.

	<u>FY 2017</u>	<u>FY 2016</u>	<u>Percentage Increase (Decrease)</u>
<b>Operating Revenues:</b>			
Rental	\$ 9,178,411	\$ 8,617,929	7%
Food and beverage	11,330,266	9,170,843	24%
Ancillary services	15,997,246	13,460,121	19%
Contributions from the City of San Diego	3,436,000	3,405,000	1%
Other revenue	<u>83,445</u>	<u>43,345</u>	93%
Total operating revenues	<u>40,025,368</u>	<u>34,697,238</u>	15%
<b>Operating Expenses:</b>			
Salaries and benefits	21,468,463	21,464,772	--
Services and supplies	11,012,446	9,042,903	22%
Depreciation	1,778,470	1,603,504	11%
Marketing contract	<u>1,931,000</u>	<u>1,931,000</u>	--
Total operating expenses	<u>36,190,379</u>	<u>34,042,179</u>	6%
<b>Operating Income</b>	<u>3,834,989</u>	<u>655,059</u>	
<b>Nonoperating Revenues (Expenses):</b>			
Interest income	77,791	3,870	1,910%
Interest expense	(151,469)	--	--
Loan origination fee	(255,000)	--	--
Loss on disposal of capital assets	(418,255)	(8,822)	4,641%
Other income	<u>791,631</u>	<u>797,786</u>	(1%)
Total nonoperating revenues (expenses), net	<u>44,698</u>	<u>792,834</u>	
Income before capital contributions	3,879,687	1,447,893	
<b>Capital Contributions</b>	<u>168,551</u>	<u>84,226</u>	100%
Change in net position	4,048,238	1,532,119	
Net position - beginning of year	<u>18,308,682</u>	<u>16,776,563</u>	
Net position - end of year	<u>\$ 22,356,920</u>	<u>\$ 18,308,682</u>	22%

**San Diego Convention Center Corporation**  
Management's Discussion and Analysis (Continued)  
For the Year Ended June 30, 2017  
(Unaudited)

**SDCCC FINANCIAL STATEMENT ANALYSIS (Continued)**

Operating Revenues

Total operating revenues generated in FY 2017 amounted to \$40.0 million, a \$5.3 million, or 15% increase compared to the prior year's total of \$34.7 million. The change was primarily the result of increased event spending per attendee along with a higher contracted data, internet and telecommunications service commission rate which resulted in increased ancillary services of \$2.5 million, or 19%, increased food and beverage commissions of \$2.2 million, or 24%, as well as increased rental revenue of \$0.6 million, or 7%, compared to prior year.

Operating Expenses

Total operating expenses incurred during FY 2017 amounted to \$36.2 million, a \$2.1 million, or 6% increase compared to the prior year's total of \$34.0 million. Services and supplies increased by \$2.0 million, or 22%, compared to prior year primarily due to non-capitalized replacement costs for various furniture, fixtures and equipment, including \$1.2 million for folding chairs as well as an increase of \$0.3 million related to building maintenance and repair costs. A small increase in depreciation expense of \$0.2 million, or 11%, resulted from increased capital asset purchases.

Nonoperating Revenues and Expenses

During FY 2017, nonoperating revenues and expenses produced netted to virtually zero, with offsetting category fluctuations, compared to \$0.8 million of net revenues in the prior year. The decrease of \$0.8 million was the result of I-Bank loan origination fees and interest expense of \$0.4 million, as well as \$0.4 million loss on disposal of capital assets, net of accumulated depreciation.

**CAPITAL ASSET ANALYSIS**

As of June 30, 2017, SDCCC had a capital asset book value of \$23.6 million, net of accumulated depreciation of \$26.7 million, or 101% more than the prior year figure of \$11.7 million. Capital assets are spread across a broad range of computer, office and operating equipment, telecommunications and leasehold improvements. The gross value of capital purchases in FY 2017 of \$13.9 million, of which \$9.5 million related to capital infrastructure improvements projects funded from I-Bank loan proceeds, were directly offset by disposals of \$0.4 million.

Major capital asset additions during FY 2017 included:

- \$3,674,711 for concrete replacement in the Sails Pavilion
- \$1,608,671 for escalator retrofit work
- \$1,608,478 for cooling tower replacements
- \$1,333,234 for Sails Pavilion roof fabric replacement
- \$910,419 for elevator modernization work

**San Diego Convention Center Corporation**  
Management's Discussion and Analysis (Continued)  
For the Year Ended June 30, 2017  
(Unaudited)

**DEBT ANALYSIS**

Effective December 6, 2016, SDCCC together with the City of San Diego jointly entered into a financing lease agreement with the California Infrastructure and Economic Development Bank to finance capital infrastructure improvement projects. The agreement calls for the total loan amount of \$25.5 million to be amortized beginning August 1, 2019, at a 3.59 percent annual interest rate and a 0.3 percent annual fee on outstanding loan balance with a maturity of 25 years. Per agreement with the City, SDCCC will budget for and make payments on the full amount due under the financing lease annually beginning on August 1, 2019. In any given year, to the extent that financing lease payment obligations and infrastructure capital and operations and maintenance expenditures exceed SDCCC's available funding. SDCCC will seek further budgetary allocation from the City. For the year ended June 30, 2017, SDCCC accrued \$521,097 in interest that is due and payable in August 2017.

Effective April 15, 2013, SDCCC entered into a commercial lease agreement with CG 7600, LLC in which the Lessor financed a warehouse capital improvement for SDCCC valued at \$21,972. The agreement calls for the loan to be amortized in the Lessee's monthly rent over 10 years at zero percent interest. In the event the Lessee does not exercise the option to extend, the unamortized portion becomes payable and due upon termination of the contract. For the year ended June 30, 2017, SDCCC paid \$2,197 in principal payments on the warehouse loan.

**ECONOMIC FACTORS AND NEXT YEAR'S BUDGET**

FY 2017 operational contributions from the City were budgeted and approved by the City at \$3,436,000, a 0.9% increase compared to prior year contributions. The contribution had been flat for the previous six years. As described in Note 6, contributions from the City funded marketing, promotion and capital projects for the Convention Center. During FY 2017, total expenses on capital projects exceeded the City's contributions.

Effective July 1, 2012, approved San Diego City Council action provided for the long-term sales, marketing and promotional activities of the Convention Center to be transferred to a third party contractor (the San Diego Tourist Authority (SDTA)). A contract between SDCCC and SDTA exists detailing the terms set forth by the City. For the year ended June 30, 2017, SDCCC paid \$1.9 million in marketing contract payments to SDTA.

Management is anticipating a decrease in financial performance during FY 2018 as compared to FY 2017 due primarily to events not generating as high a level of revenue as compared to prior year. The City's operational contributions to SDCCC are anticipated to remain at \$3,436,000.

**San Diego Convention Center Corporation**  
Management's Discussion and Analysis (Continued)  
For the Year Ended June 30, 2017  
(Unaudited)

**REQUEST FOR INFORMATION**

This financial report is designed to provide a general overview of SDCCC's finances. Questions concerning any of the information provided in this report or request for additional financial information should be addressed to the Senior Vice President & CFO at the San Diego Convention Center Corporation, 111 West Harbor Drive, San Diego, CA 92101.

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## **BASIC FINANCIAL STATEMENTS**



**San Diego Convention Center Corporation**  
Statement of Net Position  
June 30, 2017

**ASSETS**

Current assets:

Cash	\$ 10,951,043
Receivables	5,623,155
Prepaid expenses	630,506
Deposits with others	124,702
Inventory	38,416
Total current assets	17,367,822

Noncurrent assets:

Restricted cash - I-Bank contingency reserve	826,954
Restricted investment - I-Bank construction loan proceeds	19,128,822
Receivables	2,750,000

Capital assets:

Construction in progress	3,980,097
Furniture, equipment and software	5,349,561
Leasehold improvements	40,929,180
Less accumulated depreciation	(26,669,586)
Total capital assets	23,589,252

Total noncurrent assets	46,295,028
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<b>TOTAL ASSETS</b>	63,662,850
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**LIABILITIES**

Current liabilities:

Accounts payable	1,068,083
Accrued liabilities	2,766,884
Unearned income	5,741,756
Compensated employee absences	1,341,848
Current portion of long-term debt	2,197
Total current liabilities	10,920,768

Noncurrent liabilities:

Long-term debt	25,510,437
Long-term portion of unearned income	4,874,725
Total noncurrent liabilities	30,385,162

<b>TOTAL LIABILITIES</b>	41,305,930
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**NET POSITION**

Net investment in capital assets	16,898,738
Restricted - I-Bank contingency	826,954
Unrestricted	4,631,228
Total net position	42,356,920

<b>TOTAL NET POSITION</b>	\$ 22,356,920
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See accompanying notes to the basic financial statements.

**San Diego Convention Center Corporation**  
**Statements of Revenues, Expenses and Changes in Net Position**  
**For the Year Ended June 30, 2017**

<b>Operating Revenues</b>	
Rental Revenue:	
Convention and trade shows	\$ 7,262,536
Corporate/incentive events	618,226
Consumer shows	602,135
Meetings and seminars	222,687
Cancelled events	118,461
Community events	227,650
Local trade shows	126,716
Food and beverage revenue	11,330,266
Ancillary service revenue:	
Utilities	5,687,813
Telecommunications	4,777,060
Event and cleaning services	3,936,169
Audio visual	1,596,204
Contributions:	
City of San Diego	3,436,000
Other revenue	83,445
Total operating revenues	<u>40,025,368</u>
<b>Operating Expenses</b>	
Salaries and wages	16,673,164
Fringe benefits	4,795,299
Utilities	4,004,904
General	2,591,627
Repairs and maintenance	2,413,177
Contractual marketing and sales	1,931,000
Depreciation	1,778,470
Contracted services	793,967
Supplies	638,067
Insurance	324,377
Sales and marketing	122,544
Travel and transportation	81,757
Telecommunications	42,026
Total operating expenses	<u>36,190,379</u>
Operating income	<u>3,834,989</u>
<b>Nonoperating Revenues</b>	
Interest income	77,791
Interest expense	(151,469)
Loan origination fee	(255,000)
Loss on disposal of capital assets	(418,255)
Other income	791,631
Total nonoperating revenues	<u>44,698</u>
<b>Income before capital contributions</b>	3,879,687
<b>Capital contributions</b>	<u>168,551</u>
<b>Change in net position</b>	4,048,238
<b>Net position - beginning of year</b>	<u>18,308,682</u>
<b>Net position - end of year</b>	<u>\$ 22,356,920</u>

See accompanying notes to the basic financial statements.

**San Diego Convention Center Corporation**  
Statement of Cash Flows  
For the Year Ended June 30, 2017

<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>	
Receipts from customers	\$ 36,400,613
Contributions received from City of San Diego	3,436,000
Payments to suppliers for goods and services	(12,738,003)
Payments to employees for services	<u>(21,378,502)</u>
Net cash provided by operating activities	<u>5,720,108</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>	
Acquisition and construction of capital assets	(12,692,426)
Proceeds from financing lease payable	6,116,178
Principal payments on note payable	(2,198)
Proceeds from the sale of capital assets	<u>14,423</u>
Net cash used by capital and related financing activities	<u>(6,564,023)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>	
Interest received	<u>77,791</u>
<b>DECREASE IN CASH AND CASH EQUIVALENTS</b>	(766,124)
<b>CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR</b>	<u>12,544,121</u>
<b>CASH AND CASH EQUIVALENTS - END OF YEAR</b>	<u><u>\$ 11,777,997</u></u>

See accompanying notes to the basic financial statements.

**San Diego Convention Center Corporation**  
Statement of Cash Flows  
For the Year Ended June 30, 2017

**RECONCILIATION OF CASH AND CASH EQUIVALENTS TO THE  
STATEMENT OF NET POSITION**

Cash	\$ 10,951,043
Restricted cash - I-Bank contingency reserve	<u>826,954</u>
Total cash and cash equivalents	<u><u>\$ 11,777,997</u></u>

**RECONCILIATION OF OPERATING INCOME TO NET  
CASH PROVIDED BY OPERATING ACTIVITIES**

Operating income	\$ 3,834,989
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	1,778,470
Other income	791,631
Changes in operating assets and liabilities:	
Increase in receivables	(714,755)
Decrease in prepaid expenses	191,162
Increase in deposits with others	(11,743)
Increase in accounts payable	26,024
Increase in accrued compensated absences	22,068
Increase in accrued liabilities	67,893
Decrease in unearned income	(265,631)
Net cash provided by operating activities	<u><u>\$ 5,720,108</u></u>

**NONCASH CAPITAL AND FINANCING ACTIVITIES**

Capital asset contributions	\$ 168,551
Financing lease proceeds deposited to a restricted investment for construction costs	25,500,000
Loan origination fee paid from financing lease proceeds	(255,000)
Acquisition of capital assets included in accounts payable and accrued liabilities	862,755
Capitalized interest	369,829
Carrying value of disposed capital assets	(432,678)

See accompanying notes to the basic financial statements.

**NOTES TO THE BASIC FINANCIAL STATEMENTS**



**San Diego Convention Center Corporation**  
Notes to the Basic Financial Statements  
For the Year Ended June 30, 2017

**NOTE 1. REPORTING ENTITY**

San Diego Convention Center Corporation (SDCCC) is a not-for-profit public benefit corporation originally organized to market, operate and maintain the San Diego Convention Center (Convention Center).

SDCCC acts in accordance with its By-Laws, the City of San Diego's (City) Charter, and the City's Municipal Code. The City is a sole member of SDCCC and appoints seven voting members to the Board of Directors of SDCCC. Since the City appoints the voting members of the Board of Directors of SDCCC and is able to impose its will on the SDCCC, the City, as the primary government, is financially accountable for SDCCC. In accordance with Government Accounting Standards Board (GASB) Statement No. 80, *Blending Requirements for Certain Component Units - An amendment of GASB Statement No.14*, which was effective July 1, 2016, SDCCC is a blended component unit of the City of San Diego.

The Convention Center was constructed by the San Diego Unified Port District (District) on land owned by the District. Construction was completed in the fall of 1989 and the Convention Center opened in November 1989. An expansion of the Convention Center that roughly doubled the size of the facility was constructed by the City and completed in September 2001. The City has an agreement with the District to manage the Convention Center.

SDCCC has a management agreement with the City to provide sales and marketing, operating and maintenance services for the Convention Center. The agreement provides that the City will allocate to SDCCC approved budgetary amounts for marketing, promotion and capital projects for the Convention Center (refer to Note 6).

**NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**A. *Basis of Accounting and Measurement Focus***

The financial transactions of SDCCC are accounted for on the accrual basis under which revenues are recognized as earned and expenses are recognized as incurred. SDCCC distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing event meeting space, goods and services in connection with SDCCC's principal ongoing operations. SDCCC's principal operating revenues include event meeting space rental revenues, food and beverage commissions, event and cleaning service revenues, other ancillary service revenues and contributions from the City that are used to fund marketing, promotion and capital projects. SDCCC's principal operating expenses includes salaries and wages, fringe benefits, utilities, repairs & maintenance, contractual marketing & sales, and depreciation. If not operating, all other revenues and expenses are reported as nonoperating revenues and expenses. When both restricted and unrestricted resources are available for use, it is SDCCC's policy to use restricted resources first, then unrestricted resources as they are needed.

**B. *Cash and Cash Equivalents***

SDCCC's cash and cash equivalents for purposes of the statement of cash flows are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition. The government money market fund restricted investment is not considered as cash and cash equivalents.

**San Diego Convention Center Corporation**  
Notes to the Basic Financial Statements (Continued)  
For the Year Ended June 30, 2017

**NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**C. *Accounts Receivable***

Long-term receivables in the amount of \$2,750,000 represent incentive payments to be received by SDCCC in equal installments of \$625,000 on July 1, 2018 and January 1, 2019, and in equal installments of \$500,000 on July 1, 2020, July 1, 2022, and July 1, 2024 from Centerplate in consideration of the SDCCC's extension of Centerplate's exclusive food and beverage contract through June 30, 2026.

**D. *Prepaid Expenses***

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid expenses.

**E. *Inventory***

Inventory consists of spare parts that will be used and capitalized when the assets are placed into service.

**F. *Capital Assets***

Capital assets are reported at cost. Capital assets are defined as assets with initial cost of more than \$5,000 per item and a useful life of greater than one year. Capital assets are depreciated using the straight-line method over the following estimated useful lives:

	<u>Years</u>
Data processing equipment and software	3
Telecommunication equipment	5
Office furniture and operating equipment	7 - 15
Leasehold improvements	10 - 30

**G. *Unearned Income***

Unearned income represents funds due or received from customers that pertain to enforceable future contractual obligations. Building rent deposits, revenue contract incentive payments and advertising payments are recognized once the event has occurred or the contractual obligation has been fulfilled.

**H. *Compensated Employee Absences***

Accumulated annual leave (PTO) is compensated time off for eligible employees who are absent from work and is recorded in the Statement of Net Position. The amount recorded is expected to be used in accordance with SDCCC's personnel guidelines for vacation, illness, and personal business, with a maximum accumulation of 480 hours per employee. Full-time employees are allowed up to 80 hours paid compensation in lieu of annual leave provided they maintain a minimum balance of 40 hours. Additionally, part-time employees who have PTO balances in excess of 24 hours at fiscal year-end are paid their excess annual leave balance within 30 days of fiscal year-end and carry over the remaining balance each year.

**San Diego Convention Center Corporation**  
Notes to the Basic Financial Statements (Continued)  
For the Year Ended June 30, 2017

**NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**I. *Components of Net Position***

Net Investment in Capital Assets – This amount consists of capital assets net of accumulated depreciation and reduced by outstanding debt that is attributed to the acquisition, construction or improvement of the assets, net of any unspent loan proceeds, which as of June 30, 2017 was \$19,128,822.

Restricted – This amount consists of restricted assets which are reduced by liabilities related to those assets. As of June 30, 2017, the amount of restricted net position was \$826,954 due to the required reserves to the financing lease agreement.

Unrestricted – This amount is the portion of net position that does not meet the definition of “net investment in capital assets” or “restricted net position”.

**J. *Income Taxes***

SDCCC has received notice from the Internal Revenue Service that it is exempt from federal income taxes pursuant to Section 501 (c) (3) of the Internal Revenue Code. SDCCC is also exempt from state franchise taxes on related income pursuant to California Revenue and Taxation Code Section 23701(d).

**K. *Use of Estimates***

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates. Management believes that the estimates made are reasonable.

**NOTE 3. CASH/RESTRICTED CASH AND RESTRICTED INVESTMENT**

At June 30, 2017, the book balance of SDCCC's cash on hand, deposits, and bank money market account deposits was \$11,777,997 and the bank balance was \$11,988,376. Of the bank balance, \$250,000 was covered by Federal depository insurance. The remaining uninsured balance is collateralized, with the collateral held by an affiliate of the counterparty's financial institution. A formal deposit and investment policy was approved in August 2010 by SDCCC's Board of Directors, which addresses custodial credit risk, credit quality risk and allowable investments. SDCCC places no limit on the amount that may be invested in any one account or fund. SDCCC's allowable investments include: obligations of the U.S. government, its agencies and instrumentalities; investment grade state and local government securities; certificates of deposit; bankers' acceptances; repurchase agreements; and money market mutual funds whose portfolios consist only of domestic securities.

**San Diego Convention Center Corporation**  
Notes to the Basic Financial Statements (Continued)  
For the Year Ended June 30, 2017

**NOTE 3. CASH/RESTRICTED CASH AND RESTRICTED INVESTMENT (Continued)**

Cash/restricted cash and restricted investment are categorized as follows at June 30, 2017:

Cash and restricted cash:	
Cash on hand	\$ 287,803
Deposits	2,313,105
Bank money market account deposits	9,177,089
Cash and restricted cash	11,777,997
Restricted investment:	
Government money market mutual fund	19,128,822
Total cash/restricted cash and restricted investment	\$ 30,906,819

GASB Statement No. 72 requires that investments be categorized within a fair value hierarchy based upon fair value measurements. The hierarchy is based on the valuation of inputs used to measure fair values of the assets. Level 1 inputs are quoted prices in an active market for identical assets; Level 2 inputs are significant other observable inputs; and Level 3 inputs are significant unobservable inputs. The government money market mutual fund is measured at fair value using the net asset value (NAV) per share. As such, the investment in the government money market mutual fund is not classified pursuant to the fair value hierarchy.

**NOTE 4. CAPITAL ASSETS**

A summary of changes in capital assets for the year ended June 30, 2017, is as follows:

	Beginning Balance June 30, 2016	Additions and Transfer In	Deletions and Transfers Out	Ending Balance June 30, 2017
Non-Depreciable Capital Assets:				
Construction in progress	\$ 1,397,078	\$ 5,161,703	\$ (2,578,684)	\$ 3,980,097
Depreciable Capital Assets:				
Furniture, equipment and software	4,669,700	781,487	(101,626)	5,349,561
Leasehold improvements	30,957,699	10,886,141	(914,660)	40,929,180
Total Depreciable Capital Assets	35,627,399	11,667,628	(1,016,286)	46,278,741
Less Accumulated Depreciation:				
Furniture, equipment and software	(3,667,882)	(303,276)	99,840	(3,871,318)
Leasehold improvements	(21,649,756)	(1,475,194)	326,682	(22,798,268)
Total Accumulated Depreciation	(25,317,638)	(1,778,470)	426,522	(26,669,586)
Total Depreciable Capital Assets - Net	10,309,761	9,889,158	(589,764)	19,609,155
Capital Assets, Net	\$ 11,706,839	\$ 15,050,861	\$ (3,168,448)	\$ 23,589,252

Depreciation expense for the year ended June 30, 2017 was \$1,778,470. \$369,829 of interest incurred during the year ended June 30, 2017 was capitalized.

**San Diego Convention Center Corporation**  
Notes to the Basic Financial Statements (Continued)  
For the Year Ended June 30, 2017

**NOTE 5. LONG-TERM LIABILITIES**

**A. *Compensated Employee Absences***

A summary of changes in accrued compensated employee absences for the year ended June 30, 2017 is as follows:

	<u>Balance June 30, 2016</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance June 30, 2017</u>	<u>Current Portion</u>
Compensated Employee Absences	\$ 1,319,780	\$ 1,574,086	\$ (1,552,018)	\$ 1,341,848	\$ 1,341,848

**B. *Notes Payable and Financing Lease***

On April 15, 2013, SDCCC entered into a commercial lease agreement with CG 7600, LP (lessor) in which the lessor financed a warehouse capital improvement for SDCCC valued at \$21,972. The agreement calls for the loan to be amortized as part of SDCCC's monthly rent over 10 years at a zero percent per annum rate. In the event SDCCC does not exercise the option to extend the lease, the unamortized portion becomes payable and due upon termination of the contract.

On December 6, 2016, SDCCC (lessee) together with the City jointly entered into a financing lease agreement with California Infrastructure and Economic Development Bank (I-Bank), as the lessor, to finance capital infrastructure projects anticipated to cost a total of approximately \$23,300,000, which excludes capitalized interest. The total loan amount is \$25,500,000 with a 3.59% annual interest rate, a 0.3% annual fee based upon the outstanding loan balance, and a repayment period of 25 years. The principal repayment commences on August 1, 2019 and ends on August 1, 2041. Per agreement with the City, SDCCC will budget for and make payments on the full amount due under the financing lease annually beginning on August 1, 2019. In any given year, to the extent that financing lease payment obligations and infrastructure capital and operations and maintenance expenditures exceed SDCCC's available funding, SDCCC will seek further budgetary allocation from the City.

A summary of changes in notes payable and the financing lease for the year ended June 30, 2017, is as follows:

	<u>Balance June 30, 2016</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance June 30, 2017</u>	<u>Current Portion</u>
CG 7600 LP	\$ 14,832	\$ -	\$ (2,198)	\$ 12,634	\$ 2,197
I-Bank financing lease	-	25,500,000	-	25,500,000	-
Total	<u>\$ 14,832</u>	<u>\$ 25,500,000</u>	<u>\$ (2,198)</u>	<u>\$ 25,512,634</u>	<u>\$ 2,197</u>

**San Diego Convention Center Corporation**  
Notes to the Basic Financial Statements (Continued)  
For the Year Ended June 30, 2017

**NOTE 5. LONG-TERM LIABILITIES (Continued)**

Annual requirements to amortize the notes payable as of June 30, 2017, including interest payments and the 0.3% annual fee on the financing lease to maturity, are as follows:

<b>Year Ending June 30,</b>	<b>Principal</b>	<b>Interest</b>	<b>Annual Fee</b>	<b>Total</b>
2018	\$ 2,197	\$ 1,055,310	\$ -	\$ 1,057,507
2019	2,197	915,450	-	917,647
2020	734,170	902,311	76,500	1,712,981
2021	760,448	875,562	74,304	1,710,314
2022	787,669	847,852	72,029	1,707,550
2023 - 2027	4,372,784	3,787,517	323,062	8,483,363
2028 - 2032	5,214,148	2,929,372	252,616	8,396,136
2033 - 2037	6,219,743	1,905,725	168,582	8,294,050
2038 - 2042	7,419,278	684,659	68,343	8,172,280
<b>Total</b>	<b>\$ 25,512,634</b>	<b>\$ 13,903,758</b>	<b>\$ 1,035,436</b>	<b>\$ 40,451,828</b>

**NOTE 6. ECONOMIC DEPENDENCY**

SDCCC receives contributions from the City as specified in a management agreement between SDCCC and the City. The agreement provides that the City will allocate to SDCCC approved budgetary amounts for marketing, promotion and capital projects for the Convention Center. During the year ended June 30, 2017, SDCCC received \$3,436,000 from the City, of which \$1,931,000 was used to fund marketing contract expenses paid to the San Diego Tourism Authority related to certain sales, marketing and promotional aspects of long-term events at the Convention Center. The remaining \$1,505,000 was used to fund various capital projects.

Moving into FY 2018, SDCCC anticipates that contributions from the City will remain unchanged at \$3,436,000, of which \$1,931,000 is expected to be used for marketing contract expenses. The remaining \$1,505,000 is expected to fund capital projects at the Convention Center.

**NOTE 7. DEFINED CONTRIBUTION PLAN**

The San Diego Convention Center Corporation's Money Purchase Pension Plan (Plan) is a governmental plan under section 414(d) of the Internal Revenue Code, which was established effective January 1, 1986, by SDCCC's Board of Directors. The Plan is administered by SDCCC through a Defined Contribution Committee, represented by the SDCCC Board and staff, who act by a majority of its members in office to carry out the general administration of the Plan. Any recommended Plan amendments are subject to the approval and adoption by SDCCC's Board of Directors. As part of the Plan, SDCCC through Board action selected Wells Fargo & Company as Trustee, to hold and administer Plan assets subject to the terms of the Plan. The Plan is a qualified defined contribution plan and, as such, benefits depend on amounts contributed to the Plan plus investment earnings less allowable plan expenses. The Plan covers all employees who have completed at least 1,000 hours of service in one year and are not covered through a union retirement plan.

**San Diego Convention Center Corporation**  
Notes to the Basic Financial Statements (Continued)  
For the Year Ended June 30, 2017

**NOTE 7. DEFINED CONTRIBUTION PLAN (Continued)**

Employees are eligible to participate in the Plan on the first day of the month after completion of 1,000 hours of service during the twelve-month period beginning from the employee’s hire date (or during any subsequent Plan year). For each Plan year, SDCCC contributes 10% of compensation paid after the employee becomes an eligible participant, which is transferred to the trustee on behalf of each qualifying individual.

A Plan year is defined as a calendar year. The balance in the Plan for each eligible employee is vested gradually over five years of continuing service, with an eligible employee becoming fully vested after five years. Forfeitures and Plan expenses are allocated in accordance with Plan provisions.

For the year ended June 30, 2017, pension expense amounted to \$1,241,173, with no employee contributions made to the Plan. Included in pension expense were forfeitures in the amount of \$3,482 SDCCC records pension expense during the fiscal year based upon employee compensation that is included in qualified gross compensation.

**NOTE 9. COMMITMENTS**

**SDCCC as Lessor**

Effective March 22, 2013, SDCCC entered into a sublease agreement for truck marshal yard space for an initial term of 60 months, from April 1, 2013 through March 31, 2018. Future minimum annual rental lease revenues are as follows:

<b>Year Ending June 30,</b>	<b>Amount</b>
2018	<u>\$ 102,358</u>

Rental income related to the sublease was \$133,852 for the year ended June 30, 2017.

**SDCCC as Lessee**

SDCCC has noncancelable operating leases with terms greater than one year for photocopiers as well as truck marshal yard and warehouse space. The lease commitments are as follows:

<b>Year Ending June 30,</b>	<b>Amount</b>
2018	\$ 182,864
2019	31,428
2020	31,428
2021	28,809
<b>Total</b>	<u>\$ 274,529</u>

Lease expense for the year ended June 30, 2017 was \$229,074.

**San Diego Convention Center Corporation**  
Notes to the Basic Financial Statements (Continued)  
For the Year Ended June 30, 2017

**NOTE 9. COMMITMENTS (Continued)**

**Construction Commitments**

SDCCC has material commitments under construction contracts as of June 30, 2017 as follows:

<u>Construction Projects</u>	<u>Remaining Construction Value</u>	<u>Expected Completion Year</u>
Sails Pavilion Fabric Replacement	\$ 9,346,011	FY 2018
Retrofit Escalators	2,056,017	FY 2019
Replace Fire Cannons	1,567,898	FY 2018
Convert Pneumatic Controls	1,225,474	FY 2018
Fire Alarm System Replacement	973,439	FY 2018
Elevator Modernization	433,546	FY 2019

**NOTE 10. CONTINGENT LIABILITIES**

SDCCC is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disaster.

SDCCC is subject to various lawsuits as well as grievances by labor unions. SDCCC's management believes, based upon consultation with SDCCC attorneys, that any unasserted claims, in the aggregate, will not result in a material adverse financial impact on SDCCC. SDCCC is covered by various insurance policies, the largest of which include property, liability and workers' compensation, with deductibles that vary from \$5,000 to \$250,000. SDCCC management believes that SDCCC's insurance programs are sufficient to cover any potential losses should an unfavorable outcome materialize. There have been no insurance claim settlements that exceeded insurance coverage during the past three fiscal years.

## **OTHER REPORT**





**Independent Auditor’s Report on Internal Control Over Financial Reporting  
and on Compliance and Other Matters Based on an Audit of Financial  
Statements Performed in Accordance with *Government Auditing Standards***

To the Board of Directors  
San Diego Convention Center Corporation  
City of San Diego, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the San Diego Convention Center Corporation (SDCCC), a component unit of the City of San Diego, California (City), as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the SDCCC’s basic financial statements, and have issued our report thereon dated October 25, 2017.

**Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the SDCCC’s internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the SDCCC’s internal control. Accordingly, we do not express an opinion on the effectiveness of the SDCCC’s internal control.

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity’s financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the SDCCC’s financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Macias Gini & O'Connell LLP

San Diego, California  
October 25, 2017